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SEC/CORPORATE

Voluntary Withdrawal of Appeal in Delaware Exclusive Forum Bylaw Case

In response to the wave of strike suits filed outside Delaware in connection with mergers and acquisitions and executive compensation matters, boards of some Delaware corporations adopted exclusive forum bylaws. Those bylaws require that derivative actions, stockholder class actions and other intra-corporate disputes be litigated exclusively in Delaware. The validity of the exclusive forum bylaws adopted by Chevron and FedEx was litigated in the Delaware Court of Chancery in *Boilermakers Local 154 Retirement Fund v. Chevron Corp. and IClub Investment Partnership v. FedEx Corporation*. Chancellor Strine found that the bylaws were valid both contractually and statutorily.

The plaintiffs appealed the decision to the Delaware Supreme Court, and it was anticipated that the decision would be upheld. In an unexpected development, the plaintiffs voluntarily withdrew their appeal on October 15. As a practical matter, this means that the Chancellor's decision stands, but there will be no definitive pronouncement from Delaware. The absence of such precedent could come into play when plaintiffs who have filed suit outside Delaware challenge motions to dismiss or stay such proceedings on the basis of an exclusive forum bylaw. Foreign courts generally afford less weight to a trial court opinion than a state supreme court opinion.

While exclusive forum bylaws can be a valuable tool for public companies, companies should fully evaluate the ramifications of adopting such provisions before acting.

SEC Chair Speaks on Public Company Disclosure

On October 15, Mary Jo White, Chairwoman of the Securities and Exchange Commission, delivered a speech to the National Association of Corporate Directors regarding the current state of public company disclosure. Chairwoman White emphasized that the core purpose of public company disclosure is to provide investors with the information they need to make informed investment and voting decisions, and raised the question "whether investors need or are optimally served by the detailed and lengthy disclosures about all of the topics that companies currently provide in the reports they are required to prepare and file with us." She also discussed the mandate under the Jumpstart Our Business Startups Act for the Division of Corporation Finance to review the current disclosure requirements of Regulation S-K and consider how to modernize, simplify and reduce the burden of such requirements, noting that the Division of Corporation Finance is finalizing its report in response to this mandate. Chairwoman White stated that this report would be "only the first step in any potential review effort," and went on to discuss certain areas that she would like the SEC to explore in evaluating the current disclosure regime.

In the view of Chairwoman White, some of the current requirements may not result in information being provided to investors in the most efficient manner, due in part to changes in technology that have made information such as stock prices more readily available outside an issuer's SEC filings. She also highlighted areas of disclosure that have become increasingly lengthy and complex due to reasons other than additional regulation from the SEC. For instance, according to Chairwoman White, "risk factor" disclosure has expanded due to issuers' fears of liability for material omissions, and executive compensation disclosure has expanded due to issuers' desires to do a better job of explaining the rationale for complicated compensation packages in light of the “say on pay” requirements imposed by the Dodd-Frank Wall Street Reform and Consumer Protection Act. In addition, Chairwoman White mentioned that some disclosures appear multiple times in the same filing, often with substantially the same language, and suggested that the SEC consider whether it might need to “harmonize” the disclosure requirements to avoid this repetition. Although she did admit that additional disclosures in these areas can benefit investors, she also cautioned that “we should be careful not to have too much of a good thing.” Finally, Chairwoman White discussed potential changes to the disclosure scheme in general, such as more principles-based (rather than specific line-item) disclosure, disclosure requirements tailored to the industry in which an issuer operates and/or the creation of a “core document” or “company profile” filing with the SEC that would contain information that changes infrequently.

To view the full text of Chairwoman White’s speech, click here.

LITIGATION

Identity of Heinz Traders Uncovered in $4.8 Million Insider Trading Settlement with the SEC

Last week, the Securities and Exchange Commission reminded the public that the agency can track insider trading committed in the United States by foreign account owners. Following its commencement of an action in February against multiple unnamed investors under Section 10(b) and Rule 10b-5 of the Securities Exchange Act of 1934, on October 10, the SEC filed an amended complaint identifying brothers Michael and Rodrigo Terpins for illegally trading securities of H.J. Heinz Company (Heinz) shortly before Heinz announced its acquisition by Berkshire Hathaway Inc. and 3G Capital Management. In February, the SEC became suspicious when a Swiss account, which had never previously traded Heinz securities, reaped a $1.8 million profit by investing in risky option positions the day before Heinz’s acquisition announcement. The purchase of 2,533 call options was especially unusual because, in the two months preceding the trade, not more than 61 call options had been purchased on a given day. The SEC obtained an emergency court order in February to freeze the account’s assets but could not ascertain the identity of the owners because the trade was made anonymously through an omnibus account. Even though US District Judge Jed Rakoff ordered the anonymous account owner to appear to challenge the account freeze, the men still did not come forward. The amended complaint revealed that Michael Terpins learned of the acquisition from a source with access to material nonpublic information who had a duty not to disclose the information (the identity of the tipster remains a mystery). Michael shared the tip with his brother, Rodrigo, who then called a broker from his cell phone while on vacation in Disney World. The Terpins brothers have agreed to pay $4.8 million to settle the SEC suit.

Securities and Exchange Commission v. *Terpins et al.*, No. 1:13-cv-01080 (S.D.N.Y. October 10, 2013).

SEC Scores in Accounting Fraud Suit Against BankAtlantic Corp. and Former CEO

On October 10, a Florida federal judge granted the Securities and Exchange Commission’s motions for partial summary judgment against BankAtlantic (now BBX Capital Corp.) and its former CEO and chairman Alan Levan, finding that the defendants’ public disclosures about their commercial real estate portfolio and their accounting treatment of certain portfolio loans violated Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder. The accounting fraud claim stems from BankAtlantic’s October 2007 attempt to sell many of the troubled loans. The company improperly recorded the loans on its books as “held-for-investment” instead of held-for-sale,” and failed to write them down. Management’s concern about the credit quality of the company’s commercial real estate land acquisition and development portfolio had been memorialized in a March 2007 email sent by the CEO in response to a cascade of borrowers requesting extensions, in which he stated, “[i]t’s pretty obvious that the music has stopped…I believe we are in for a long sustained problem in this sector.” The court found that the CEO made false statements in July 2007 during a second quarter earnings call, in which he acknowledged concerns about a subset of the portfolio but stated that, “there are no asset classes that we are concerned about in the portfolio as an asset class” and “the portfolio has always performed extremely well, continues to perform extremely well.” The company’s Forms 10-Q for the first and second quarters of 2007 did not acknowledge the trend of extensions granted and loans downgraded to non-passing status. The court also struck defendant’s affirmative defense that it relied on the professional advice of accountants, agreeing with the SEC’s assertion that the company did not completely disclose the problem to its accountants.

Securities and Exchange Commission v. BankAtlantic Bancorp Inc. et al., No. 0:12-cv-60082 (S.D.Fla. October 10, 2013).

BANKING

Federal Reserve and OCC Issue Final Rules Replacing Existing Risk-Based and Leverage Capital Rules

The Office of the Comptroller of the Currency (OCC) and the Board of Governors of the Federal Reserve System published a final rule in the *Federal Register* on October 11 that replaces their existing risk-based and leverage capital rules. The final rule is consistent with the interim final rule published by the Federal Deposit Insurance Corporation (collectively, the rule). The rule establishes a new regulatory capital framework that incorporates revisions to the Basel capital framework, including Basel III and other elements. "The rule strengthens the definition of regulatory capital, increases risk-based capital requirements, and amends the methodologies for determining risk-weighted assets" and applies to all national banks and federal savings associations (collectively, banks). Subject to various transition periods, the rule is effective for advanced approaches banks on January 1, 2014, and for all other banks on January 1, 2015.

Highlights

- Implements strict eligibility criteria for regulatory capital instruments.
- Revises the Prompt Corrective Action framework to incorporate new regulatory capital minimum thresholds.
- Adds a new common equity tier 1 capital ratio of 4.5 percent and increases the minimum tier 1 capital ratio requirement from 4.0 percent to 6.0 percent.
- Improves the measure of risk-weighted assets to enhance risk sensitivity.
- Retains the existing regulatory capital framework for one- to four-family residential mortgage exposures.
- Allows banks not subject to the advanced approaches rule to retain the existing treatment for accumulated other comprehensive income through a one-time election.
- Allows certain depository institution holding companies to continue to include in tier 1 capital previously issued trust preferred securities and cumulative perpetual preferred stock.
- Limits capital distributions and certain discretionary bonus payments if banks do not maintain a capital conservation buffer of common equity tier 1 capital above minimum capital requirements.
- Removes references to credit ratings consistent with the Dodd-Frank Wall Street Reform and Consumer Protection Act and provides alternative measures of creditworthiness.
- Establishes due diligence requirements for securitization exposures.

In addition, the rule emphasizes common equity tier 1 capital, "the most loss-absorbing form of capital," and implements strict eligibility criteria for regulatory capital instruments. The rule also replaces the existing generally applicable capital standards with a "Standardized Approach" for all but the largest banks that includes expanded recognition of collateral and guarantors and increased capital requirements for past-due loans, high-volatility commercial real estate exposures and certain short-term loan commitments.

For the largest, most internationally active banks, the rule includes a countercyclical capital buffer, a new minimum supplementary leverage ratio that takes into account off-balance-sheet exposures, and additional capital charges and standards for derivatives exposures. The rule also introduces enhanced disclosure requirements applicable to the top-tier entity in a banking organization that is domiciled in the United States and has $50 billion or more in total assets.

The rule implements transition provisions, including those applicable to the new minimum capital ratio requirements, the capital conservation buffer, and the regulatory capital adjustments and deductions. Finally, the rule also expands the scope of the market risk rule to include federal savings associations engaged in significant levels of trading activity.

The rule is available here.

A guide to assist community bankers in understanding the interim rules (which were just finalized) was recently published during the summer and may be found here.

For more information, contact:

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