Katten
Katten Muchin Rosenman LLP

CORPORATE & FINANCIAL
WEEKLY DIGEST

June 21, 2012

SEC/CORPORATE

SEC Adopts Final Rules Requiring Listing Standards for Compensation Committees and Advisers

On June 20, the Securities and Exchange Commission adopted a final rule that requires national securities exchanges to adopt listing standards regarding the independence of compensation committees and compensation advisers of public companies.

The new Rule 10C-1, pursuant to Section 952 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, which added Section 10C to the Securities Exchange Act of 1934, directs that the listing standards of national securities exchanges require:

- Each member of a company's compensation committee must be a member of the board of directors and must be independent. For determinations of independence, the exchanges will be required to consider relevant factors, including the source of compensation of a director and whether a director is an affiliate of the company.
- A compensation committee may, in its sole discretion, obtain the advice of a compensation adviser and the compensation committee is directly responsible for the appointment, compensation and oversight of compensation advisers.
- A compensation committee must be appropriately funded by the company.
- A compensation committee may select a compensation consultant, legal counsel or other adviser only after considering certain specified independence factors, including whether the compensation consultant is providing any other services to the company, the amount of fees paid to the consultant as a percentage of the consultant's revenues, whether the compensation adviser has any business or personal relationship with a member of the compensation committee or an executive officer, and whether the adviser owns any stock of the company.

Rule 10C-1 also requires these listing standards to apply, with limited exceptions, to directors who oversee executive compensation matters in the absence of a compensation committee.

Rule 10C-1 exempts controlled companies and smaller reporting companies from all of the requirements of the new listing standards and authorizes the exchanges to exempt other categories of issuers. Further, Rule 10C-1 requires the exchanges to exempt from the compensation committee independence requirements (i) limited partnerships, (ii) companies in bankruptcy proceedings, (iii) open-end management investment companies registered under the Investment Company Act of 1940 and (iv) any foreign private issuer that discloses in its annual report the reasons that it does not have an independent compensation committee.

The SEC also amended Item 407 of Regulation S-K to require that companies disclose any conflicts of interest with respect to a compensation consultant and how such conflicts are being addressed. There are no issuer exemptions from the disclosure requirements.

The new rule and Item 407 amendment will take effect 30 days after publication in the Federal Register, and thereafter each national securities exchange will have 90 days to propose listing standards that comply with the new rule. The SEC must approve the new listing standards within one year of the new rule becoming effective.

Click here to view the adopting release for the rule and rule amendments (Release Nos. 33-9330; 34-67220). The final rule and compliance considerations will be discussed further in an upcoming *Katten Client Advisory*.

DERIVATIVES

ISDA to Publish Illegality/Force Majeure Protocol

The International Swaps and Derivatives Association (ISDA) is publishing a new protocol to assist derivatives counterparties with their Eurozone contingency planning. The issue addressed by the protocol, which was issued in pre-publication form on June 19, is the absence in the 1992 form of ISDA master agreement of the same type of force majeure and illegality provisions that are found in the standard text of the 2002 version of the ISDA master. These provisions are expected to be helpful in a Eurozone financial crisis that effects the use of the Euro in derivative transactions. The protocol is a multilateral contractual amendment mechanism that enables an adhering party to amend its 1992 masters to incorporate those provisions with a minimum of difficulty so long as its counterparties also adhere to the protocol.

The protocol will be open shortly for a defined adherence period after final publication. Parties adhere by sending a prescribed form of adherence letter to ISDA.

The full text of the pre-publication version of the protocol can be found here.

A full list of ISDA protocols can be found here.

CFTC

CFTC Adopts Designated Contract Market Core Principle Rules

On June 19, the Commodity Futures Trading Commission published final rules relating to core principles and other requirements for designated contract markets (DCMs). The Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) amended the DCM core principles by eliminating the eight criteria for contract market designation, amending many of the core principles for DCMs and adding five new core principles relating to disciplinary procedures, system safeguards, financial resources,. diversity of boards of directors and access to swap records by the Securities and Exchange Commission.

The CFTC's final rules address the Dodd-Frank Act requirements by implementing twenty-three new and amended core principles for DCMs and incorporating provisions related to the trading and execution of swaps on DCMs. The final rules also establish financial information and resource requirements, compliance and surveillance obligations, operational requirements, trading and product requirements and risk control mechanisms for DCMs.

The final rules also include a requirement that market participants trading on a contract market consent to the jurisdiction of the DCM. The CFTC has made clear that this requirement applies, in addition to market participants with direct market access, to persons whose trades are intermediated, persons who are customers of DCM member firms, and persons whose access to the exchange is granted by or through member firms.

In addition, the final rules revise the application process for DCMs and include a new DCM application form with a comprehensive list of instructions and exhibits. Among other things, the CFTC has eliminated its ninety-day accelerated approval procedure for DCM applications but requires all applications for designation as a contract market to be reviewed by the CFTC within 180 days, unless extended with the consent of the applicant.

The rules will become effective on August 20. With one exception related to the access requirements articulated in Rule 38.151(a), the compliance date for the new and amended rules is October 17. The compliance date for the access requirements for existing DCM members and market participants will be 180 days after the effective date to allow DCMs enough time to obtain consents to the DCM's jurisdiction from all existing market participants.

The final rule is available here.

LITIGATION

District Court Sustains Whistleblower Wrongful Termination Claim

Plaintiff Benjamin Ashmore brought a claim alleging that defendants CGI Group Inc. (CGI) and CGI Federal Inc. (CGI Federal) violated Section 806 of the Sarbanes-Oxley Act, otherwise known as the whistleblower provision. The U.S. District Court for the Southern District of New York denied the defendants' motion to dismiss, rejecting the argument that plaintiff's objections to an allegedly fraudulent scheme were not sufficiently specific under § 806. The court also rejected arguments that amendments to Section 806 enacted under the the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) not be applied retroactively.

The case involved an alleged scheme to evade a potential HUD requirement limiting the number of housing units to which private subcontractors such as defendants could provide administrative services. After HUD announced that it was considering a 300,000 unit cap on the number of units that any private subcontractor could administer, plaintiff, an employee of CGI Federal at the time, allegedly learned that a team of CGI Federal employees had developed a scheme to evade the cap. Under the scheme, which never went into effect because HUD decided against imposing the cap, CGI Federal directors would resign their positions and set up new independent companies to acquire unit contracts. CGI Federal would later acquire these companies, and with them, their contracts, thus evading the cap.

In applying Section 806 to the facts and circumstances of the case, the defendants unsuccessfully challenged the sufficiency of two allegations. As for the first allegation, a whistleblower claim requires that the plaintiff engaged in protected activity. The court held that plaintiff's belief that the scheme constituted mail and/or wire fraud was objectively and subjectively reasonable, and his communications relaying this belief to the defendants were sufficiently specific to afford him protection under the statute. He was not required to describe to defendants how the relevant conduct violated the statute.

As for the second requirement, a whistleblower claim requires that the employer knew of or suspected, actually or constructively, the protected activity. The court held that a plaintiff need only demonstrate that he communicated his reasonable belief as to the illegality of the company's conduct to his employer. Plaintiff's complaint met this requirement by alleging "how, when and to whom" he communicated his objections to the alleged scheme.

Congress amended Section 806 to explicitly apply the whistleblower provision to employees of those private subsidiaries of public companies that report financial information included in the consolidated financial statements of the public company. The defendants contended that the provision should not apply retroactively to the plaintiff, as his employment was terminated on June 16, 2010, while the amendment came into effect on July 22, 2010. The court accepted the plaintiff's argument that the 2010 amendment clarified, rather than substantively altered, the meaning of Section 806. As a result, the general presumption against retroactivity should not apply. Similarly, as a result of the retroactivity, the court considered plaintiff's complaint timely despite the fact that he filed it 177 days after the alleged violation occurred. As of his termination, whistleblowers had 90 days to file their complaints. However, the Dodd-Frank Act doubled this period, giving whistleblowers 180 days to file complaints.

Ashmore v. CGI Group Inc., No. 11 Civ. 8611(LBS), 2012 WL 2148899 (S.D.N.Y. June 12, 2012).

District Court Dismisses Private Securities Fraud Action Due to Plaintiff's Failure to Meet Heightened Pleading Standards

The U.S. District Court for the District of Montana granted defendants Simonsen and Kapidiya's (Simonsen) motion to dismiss plaintiff Krohne Fund LP's (Krohne) securities fraud claim arising under Section 10(b) of the

Securities Exchange Act of 1934, but denied Simonsen's motion to dismiss Krohne's common law fraud claim based on the same set of operative facts.

Krohne engaged Simonsen to manage its financial investments, based on the latter's Optimus trading software. Simonsen allegedly assured Krohne that its investments would remain within the Optimus trading program's algorithm, and that Krohne could choose the degree of risk to be programmed into the algorithm. On September 29, 2011, Krohne's account showed a loss $437,627 in excess of the expected loss based on a simulation of the Optimus program over the period. When questioned, Simonsen allegedly could not explain the discrepancy. Krohne withdrew its funds and filed several claims, including a Section 10(b) claim and a state law fraud claim contending that Simonsen wrongfully traded securities outside of the algorithm.

The district court held that the heightened pleading standard of the Private Securities Litigation Reform Act of 1995 (PSLRA) requires a plaintiff to plead specific facts establishing a strong inference of scienter. Krohne's allegation that Simonsen traded outside or not in accordance with the algorithm does not, standing alone, establish the necessary strong inference. In contrast, the state law claims survived dismissal because Rule 9(b) of the Federal Rules of Civil Procedure allows for general allegations of malice, intent and knowledge.

Krohne Fund LP v. Simonsen, No. CV 12-04-BLG-RFC, 2012 WL 2120785 (D.Mont. June 12, 2012).

EXECUTIVE COMPENSATION AND ERISA

IRS Provides Guidance on Reduction in Health FSA Limit to $2,500

The Internal Revenue Service recently published Notice 2012-40 in which it provided guidance with regard to the $2,500 limitation effective next year for health flexible spending arrangements (Health FSAs) subject to Internal Revenue Code (Code) Section 125. The reduction in the maximum amount of contribution (from the current limit of $5,000) was enacted as part of the Patient Protection and Affordable Care Act. Health FSAs with a cap on employee contributions which exceed $2,500 will have to be amended to come into line with this new limitation.

The key points contained in Notice 2012-40 are as follows:

- The $2,500 limit does not apply for plan years that begin before 2013.
- Plans may adopt the required amendment to reflect the new limit at any time before January 1, 2015 (despite the rule that generally prohibits retroactive amendments to FSAs), provided that the cafeteria plan operates in accordance with the limitation for plan years beginning after 2012.
- In the case of a plan providing a grace period (which may be up to two months and 15 days), unused contributions for plan years beginning in 2012 or later that are carried over into the grace period will not count against the $2,500 limit for the subsequent plan year.
- Salary reduction contributions exceeding the $2,500 limit that are due to a reasonable mistake of fact and not willful neglect and that are corrected by the employer in a timely manner (including reporting them as wages for income tax withholding and employment tax purposes on Form W-2) will continue to qualify as a cafeteria plan under Code Section 125.

Additional Points of Interest

Note that the new $2,500 limitation applies only to salary reduction contributions to a Health FSA and does not apply to certain employer non-elective contributions (sometimes called flex credits), to any types of contributions or amounts available for reimbursement under other types of FSAs, health savings accounts, health reimbursement arrangements, or to salary reduction contributions to cafeteria plans that are used to pay an employee's share of health coverage premiums for an insured or self-insured health plan.

The $2,500 limitation will be indexed for cost-of-living adjustments for plan years beginning after 2013.

The Treasury Department and IRS also intend to amend the regulations under Code Section 125 to provide for the new $2,500 limitation. Notice 2012-40 provides that until such amended regulations are issued, taxpayers may rely on the guidance in Notice 2012-40.

The Notice also requests comments regarding potential modifications to the "use-it-or-lose-it rule." The IRS and Treasury Department are considering enacting an additional form of flexibility (instead of or in addition to the two-and-a-half month grace period rule) with respect to the use-it-or-lose-it rule, and have solicited comments by August 17.

For a copy of IRS Notice 2012-40, click here.

BANKING

OCC Issues Guidance for Evaluating Capital Planning and Adequacy

On June 7, the Office of the Comptroller of the Currency (OCC) issued guidance summarizing its expectations for national banks and savings associations (collectively, banks) regarding capital adequacy and capital planning. This guidance , set forth in OCC Bulletin 2012-16, also discusses the OCC's processes for evaluating a bank's capital planning and adequacy, and the various actions the OCC may take to ensure a bank's capital planning process and capital level remain adequate for its complexity and overall risks. This bulletin also rescinds Office of Thrift Supervision CEO Memorandum 380, "Capital Management," dated March 15, 2011.

The major take-away from the guidance suggests that banks and savings banks may no longer be able to rely on mere compliance with capital ratios in order to maintain a designation as well-capitalized. Instead, examination teams will assess capital ratios and also assess the bank's capital planning process itself. "A robust capital planning process is an integral and significant part of a bank's governance process necessary to ensure safe and sound operations and ongoing viability. The exact content, extent, and depth of the capital planning process should be commensurate with the overall risks, complexity, and corporate structure of the bank…. The supervisory review process assesses whether (1) the bank has a sound and effective process commensurate with its overall risk and complexity to determine that its overall capital is adequate and (2) the bank maintains a capital level that is commensurate with its risks and is consistent with the bank's internal assessment and identified capital needs on an ongoing basis and as underlying conditions change (for example, changes in a bank's overall risks or economic conditions)."

For more information, click here.

OCC Issues an Interim Final Lending Limit Rule

On June 20, the Office of the Comptroller of the Currency (OCC) adopted an interim final rule amending its lending limit rule to apply to certain credit exposures arising from derivative transactions and securities financing transactions. Effective July 21, 2012, section 610 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act). revises the statutory definition of "loans and extensions of credit" for purposes of the lending limit applicable to banks and savings banks to include certain credit exposures arising from a derivative transaction, repurchase agreement, reverse repurchase agreement, securities lending transaction, or securities borrowing transaction. Section 610 also amends existing law by adding a definition of "derivative transaction" to include any transaction that is a contract, agreement, swap, warrant, note, or option that is based, in whole or in part, on the value of, any interest in, or any quantitative measure or the occurrence of any event relating to, one or more commodities, securities, currencies, interest or other rates, indices, or other assets. A "securities financing transaction" is defined as a repurchase agreement, reverse repurchase agreement, securities lending transaction, or securities borrowing transaction. To complement these changes, the rule amends the definition of "borrower" to include a party to whom the bank has credit exposure arising from a derivative transaction or a securities financing transaction.

The interim final rule implements the statutory change which applies to both national banks and savings associations. (State banks are subject to separate restrictions under section 611 of the Dodd-Frank Act.) The OCC provided a short-term exception under its lending limits authority to allow time for national banks and savings associations to adjust for compliance with the new standard. National banks and savings associations have through January 1, 2013, to comply with the rule's requirements as to derivative transactions and securities financing transactions.

The interim final rule, which amends 12 CFR Part 32, also consolidates the lending limit rules applicable to national banks and savings associations and removes the separate regulation governing lending limits for savings associations. The interim final rule applies to both federal and state savings associations, pursuant to section 312 of the Dodd-Frank Act, which gives the OCC rulemaking authority for both federal and state savings associations. The interim final rule is effective July 21, 2012.

"To reduce the burden of these new credit exposure calculations, particularly for smaller and mid-size banks and savings associations, the rule permits use in certain circumstances of look-up tables for measuring the exposures for each transaction type. This method permits institutions to adopt compliance alternatives that fit their size and risk management requirements, consistent with safety and soundness and the goals of the statute," according to the OCC. The OCC also stated that "[t]he revised lending limit rule continues to provide that loans and extensions of credit, including those that arise from derivative and securities financing transactions, must be consistent with safe and sound banking practices."

Comments on the interim final rule, which includes a series of questions posed by the OCC, are due by August 6.

For more information, click here.

For more information, contact:

SEC/CORPORATE

Robert L. Kohl	212.940.6380	robert.kohl@kattenlaw.com
Robert J. Wild	312.902.5567	robert.wild@kattenlaw.com
Daniel J. Silverthorn	312.902.5502	daniel.silverthorn@kattenlaw.com

FINANCIAL SERVICES

Janet M. Angstadt	312.902.5494	janet.angstadt@kattenlaw.com
Henry Bregstein	212.940.6615	henry.bregstein@kattenlaw.com
Wendy E. Cohen	212.940.3846	wendy.cohen@kattenlaw.com
Guy C. Dempsey, Jr.	212.940.8593	guy.dempsey@kattenlaw.com
Daren R. Domina	212.940.6517	daren.domina@kattenlaw.com
Kevin M. Foley	312.902.5372	kevin.foley@kattenlaw.com
Jack P. Governale	212.940.8525	jack.governale@kattenlaw.com
Maureen C. Guilfoile	312.902.5425	maureen.guilfoile@kattenlaw.com
Arthur W. Hahn	312.902.5241	arthur.hahn@kattenlaw.com
Joseph Iskowitz	212.940.6351	joseph.iskowitz@kattenlaw.com
Carolyn H. Jackson	44.20.7776.7625	carolyn.jackson@kattenlaw.co.uk
Kathleen H. Moriarty	212.940.6304	kathleen.moriarty@jkattenlaw.com
Raymond Mouhadeb	212.940.6762	raymond.mouhadeb@kattenlaw.com
Marilyn Selby Okoshi	212.940.8512	marilyn.okoshi@kattenlaw.com
Ross Pazzol	312.902.5554	ross.pazzol@kattenlaw.com
Kenneth M. Rosenzweig	312.902.5381	kenneth.rosenzweig@kattenlaw.com
Fred M. Santo	212.940.8720	fred.santo@kattenlaw.com
Christopher T. Shannon	312.902.5322	chris.shannon@kattenlaw.com
Peter J. Shea	212.940.6447	peter.shea@kattenlaw.com
Marybeth Sorady	202.625.3727	marybeth.sorady@kattenlaw.com
James Van De Graaff	312.902.5227	james.vandegraaff@kattenlaw.com
Robert Weiss	212.940.8584	robert.weiss@kattenlaw.com
Meryl E. Wiener	212.940.8542	meryl.wiener@kattenlaw.com
Lance A. Zinman	312.902.5212	lance.zinman@kattenlaw.com
Krassimira Zourkova	312.902.5334	krassimira.zourkova@kattenlaw.com

LITIGATION

William M. Regan	212.940.6541	william.regan@kattenlaw.com
Jason F. Clouser	212.940.6309	jason.clouser@kattenlaw.com

BANKING

Jeff Werthan	202.625.3569	jeff.werthan@kattenlaw.com

EXECUTIVE COMPENSATION AND ERISA

Gregory K. Brown	312.902.5404	gregory.brown@kattenlaw.com
Ann M. Kim	312.902.5589	ann.kim@kattenlaw.com
Christopher K. Buch	312.902.5509	christopher.buch@kattenlaw.com

* Click here to access the *Corporate and Financial Weekly Digest* archive.

Katten

Katten Muchin Rosenman LLP www.kattenlaw.com

CHARLOTTE CHICAGO IRVING LONDON LOS ANGELES NEW YORK OAKLAND ORANGE COUNTY SHANGHAI WASHINGTON, DC

Katten Muchin Rosenman LLP is an Illinois limited liability partnership including professional corporations that has elected to be governed by the Illinois Uniform Partnership Act (1997).

London affiliate: Katten Muchin Rosenman UK LLP.