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CORPORATE & FINANCIAL
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BROKER DEALER

SEC Issues Exemptions from Large Trader Reporting Rule

On April 20, the Securities and Exchange Commission issued an order temporarily exempting broker-dealers from the recordkeeping, reporting and monitoring requirements set forth in Rule 13h-1 of the Securities Exchange Act of 1934 (the Large Trader Reporting Rule) that were scheduled to take effect on April 30, 2012. The order also permanently exempts certain transactions from the definition of "transaction" under the Large Trader Reporting Rule, but only for purposes of determining whether a person is a "large trader."

Generally, the order exempts registered broker-dealers from the Large Trader Reporting Rule's recordkeeping and reporting requirements until May 1, 2013. Notwithstanding the foregoing, clearing broker-dealers for large traders that (a) are U.S.-registered broker-dealers or (b) trade via sponsored access arrangements are temporarily exempted from such recordkeeping and reporting requirements only until November 30, 2012. In addition, the order provides an exemption to all registered broker-dealers from the Large Trader Reporting Rule's monitoring requirements, pursuant to which such broker-dealers are required to monitor their customers' accounts for unidentified large traders, until May 1, 2013.

In its order, the SEC also permanently exempts certain transactions from the definition of "transaction" for purposes of the large trader identifying activity level calculation. The Large Trader Reporting Rule already excludes certain transactions from the identifying activity level calculation, which are not "effected with an intent that is commonly associated with the arm's-length trading of securities in the secondary market and therefore would not fall within the types of transactions that are characterized by the exercise of investment discretion" for purposes of the Large Trader Reporting Rule. In addition to those transactions currently excluded, the following transactions are now excluded from the definition of "transaction" pursuant to the SEC's order:

- any transaction that is part of an offering of securities by or on behalf of an issuer, or by an underwriter on behalf of an issuer, or an agent for an issuer, whether or not such offering is subject to registration under the Securities Act of 1933, regardless of whether such transaction is effected through the facilities of a national securities exchange; and

- sales of securities by a selling shareholder in connection with an initial public offering or in a registered secondary offering if such selling shareholder is a current or former employee of the issuer and the securities being sold were acquired as part of the person's compensation as an employee of the issuer.

This limited exemption is meant to reduce the burden on issuers and selling shareholders who would not otherwise meet the definition of large trader in the absence of the transactions listed above, since these transactions typically are "infrequent in nature and are distinguishable in character from the secondary market activity" on which the Large Trader Reporting Rule focuses.

Click here to read SEC Release No. 34-66839.

CBOE – New Order Origin Code for FLEX Options

The Chicago Board Options Exchange (CBOE) has begun to transition the electronic trading capabilities of its existing FLEX options trading system (CFLEX 1.0) to its CBOEdirect trade engine. CBOE is effecting this transition by rolling out CFLEX 2.0. CBOE will initially make two classes of FLEX options available for trading on CFLEX 2.0 – the SPX and SPY. These two classes moved to CFLEX 2.0 on April 24. Additional classes will begin moving from CFLEX 1.0 to CFLEX 2.0 over the next one to three weeks.

A key difference between CFLEX 1.0 and CFLEX 2.0 is that a new order origin code applies to FLEX options for non-trading permit holder broker-dealers, *i.e.*, order origin code "D". On CFLEX 1.0, orders and responses for the account of non-trading permit holder broker-dealers use the origin code "C". It is important to note that the new order origin code "D" pertains to FLEX options only.

Click here for CFLEX 2.0 rollout schedule, and click here for CBOE order origin code requirements.

LITIGATION

Absence of Contract Bars Investment Advisers Act Claim by Private Plaintiff

The United States District Court for the District of Utah recently found that a failure to allege a contractual relationship barred the plaintiffs' Investment Advisers Act (the Act) claim as a matter of law.

The plaintiffs invested $1.65 million in a Ponzi scheme conducted by defendant Brian J. Smart. The plaintiffs alleged that Smart's co-defendants Frank Winger, AIM Winger Corporation, and AIM Winger LLC, et al. (collectively, the Winger Defendants) failed to supervise Smart and aided and abetted Smart's violations of Section 206 of the Act. The Winger Defendants moved to dismiss the claim, arguing that because the only remedy available to private plaintiffs under the Act is to void an investment advisers contract, and the plaintiffs alleged no contract with the Winger Defendants, the plaintiffs had not stated a valid claim.

The District Court agreed and granted the Winger Defendants' motion to dismiss. It found that because the plaintiffs had not alleged a contractual relationship with the Winger Defendants, the plaintiffs could not state a claim for aiding and abetting a violation of the Act.

Padilla, et al., v. Winger, et al., No. 2:11 CV 897 (D. Utah Apr. 20, 2012)

District Court Considers Defendants' Challenge to SEC's Motion for Final Judgment

The Securities and Exchange Commission filed an enforcement action against defendants Robert D. Orr and Leland G. Orr alleging massive financial fraud. As a result of the enforcement action, the court signed judgments of permanent injunctions against the defendants, with the defendants' consent. As part of this consent decree, the defendants agreed to pay disgorgement, prejudgment interest on the disgorgement amount and civil penalties, in amounts to be determined by the court upon a subsequent motion by the SEC. The SEC filed its motion seeking the above monetary penalties, and defendants opposed the motion.

In opposing the motion, the Orrs disputed the accuracy, completeness and truthfulness of allegations in the SEC's underlying complaint. The District Court rejected the defendants' arguments, finding that by entering into a consent decree, the defendants had waived their right to litigate the issues involved in the underlying case.

In addition, the Court found that the defendants offered no evidence demonstrating that they were entitled to a reduction in the amount of disgorgement. The Court also found that because the defendants previously consented to an award of prejudgment interest, they were barred from challenging the equities of awarding prejudgment interest on the disgorgement amount. Finally, the Court exercised its "equitable discretion to fashion appropriate civil penalties" and, giving weight to the defendants' efforts at "stepping into the gap and risking their own money and time to address unfolding and growing financial crises," reduced the amount of civil penalties sought by the SEC. In sum, the defendants were ordered to pay nearly $1.24 million in disgorgements and prejudgment interest, and $68,000 in civil penalties.

SEC v. Robert D. Orr, Leland G. Orr, Michael S. Lowry, Michael S. Hess, Kyle L. Garst, and Travis W. Vrbas, No. 11-2251-SAC (D. Kan. Apr. 17, 2012)

BANKING

SEC Staff Issues Observations on MD&A and Accounting Policy Disclosures of Smaller Financial Institutions

On April 20, the Division of Corporation Finance of the Securities and Exchange Commission issued guidance with respect to certain matters relating to management's discussion and analysis and certain accounting policies of smaller financial institutions. Staff stated that "we frequently issue comments on several topics that impact Management's Discussion and Analysis (MD&A) and accounting policy disclosures. We are issuing this guidance to summarize our observations on such matters in order to assist smaller financial institutions in enhancing the disclosure they provide investors in the reports they file with the Commission."

The guidance relates to the following topics: allowance for loan losses, charge-off and non-accrual policies, commercial real estate, impairment based on collateral value, credit risk concentrations, troubled debt restructurings and modifications, other real estate owned, deferred taxes, and FDIC-assisted acquisitions.

For more information, click here.

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