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CORPORATE & FINANCIAL
WEEKLY DIGEST

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SEC/CORPORATE

ISS Publishes Updates to Proxy Voting Policies

On November 17, Institutional Shareholder Services (ISS) published updates to its proxy voting policies, which will be effective for meetings held on or after February 1, 2012. ISS' policy updates include the following:

Board and Proxy Access

- ISS will determine its recommendations for shareholder votes on election of compensation committee members and management say-on-pay proposals where the company's previous say-on-pay proposal received less than a 70% vote on a case-by-case basis. It will take into account the company's response to investor input (including disclosure regarding efforts to engage institutional investors regarding compensation issues, actions taken to address issues and other compensation-related actions), whether the issues raised are recurring, the company's ownership structure, and whether the level of support for the proposal was below 50%.

- ISS will recommend that shareholders vote against or withhold votes for incumbent directors if a board implements say-on-pay votes on a less frequent basis than the frequency that received the majority vote at the most recent shareholder meeting. ISS will determine its voting recommendations on a case-by-case basis if the board implements say-on-pay votes on a less frequent basis than the frequency receiving a plurality, but not a majority, of votes at the most recent shareholder meeting. ISS will take into account the board's rationale for selecting a different frequency, the company's ownership structure and vote results, ISS' analysis of compensation concerns and related issues, and the previous year's support of the company's say-on-pay proposal. ISS does not consider implementation of say-on-pay votes on a more frequent basis than the frequency that received a majority or plurality of votes to be problematic.

- ISS will continue to analyze shareholder proposals seeking proxy access on a case-by-case basis, and will take into account factors specific to both the company and the proposal, including the proposed ownership thresholds, the maximum proportion of directors shareholders may nominate each year, and the method of determining which nominations should appear in the ballot in the event of nominations from multiple shareholders.

- ISS updated its policy on recommending that shareholders vote against or withhold votes from directors due to governance or fiduciary responsibility failures, failures to replace management when appropriate and other egregious actions to explicitly include material failures relating to risk oversight.

Executive Compensation

- ISS refined its methodology for evaluating pay-for-performance alignment, which will identify companies that have demonstrated strong or satisfactory alignment between pay and performance over an extended period of time. For companies in the Russell 3000 index, ISS will consider "peer group alignment," the degree of alignment between a company's total shareholder return (TSR) rank and its CEO's total pay rank within its

peer group, measured over one and three-year periods, and the CEO's total pay relative to the median for the company's peer group, and "absolute alignment" between the trend in CEO pay and company TSR over the last five years. If the ISS' analysis demonstrates pay-for-performance alignment that is unsatisfactory, or for non-Russell 3000 index companies is misaligned, ISS will analyze various other factors to determine how pay elements may encourage or undermine value-creation and alignment with shareholder interests.

- ISS will generally recommend a vote in favor of proposals to approve or amend executive incentive bonus plan proposals if they include only administrative features, place a cap on annual grants to individual participants to comply with Section 162(m), add appropriate performance goals to comply with Section 162(m), or cover cash or cash and stock bonus plans submitted to shareholders for the purpose of exempting compensation from taxes under Section 162(m). ISS will recommend a vote against proposals if the compensation committee is not made up of independent outsiders or the plan is problematic. ISS will analyze proposals on a case-by-case basis if the plan amendment could transfer additional shareholder value to employees (i.e. adding shares, extending the term, etc.) or the company is presenting the plan to shareholders for the first time after its initial public offering, in which case ISS will perform a full equity plan analysis.

Environmental and Social

- ISS amended its policy on disclosure of a company's political spending to generally recommend votes in favor of greater disclosure, and will analyze proposals requesting information on a company's lobbying activities on a case-by-case basis.

- ISS updated and created specific policies to address environmental and other matters, including recommending votes in favor of shareholder proposals relating to greater disclosure of hydraulic fracturing operations under certain circumstances and case-by-case analysis of proposals to report on or adopt recycling programs or water-related concerns and requests for workplace safety reports.

Other Corporate Matters

- ISS also addressed other corporate matters, including implementing a case-by-case analysis on exclusive venue proposals and recommending votes against proposals to create new classes of common stock unless the company discloses a compelling rationale for a dual-class structure and certain other conditions are met.

To view the complete text of ISS' U.S. Corporate Governance Policy 2012 Updates, click here.

CFTC

CFTC Request for Public Comment Regarding ICE Clear Credit Portfolio Margining Petition

The Commodity Futures Trading Commission is requesting public comment on a petition submitted by ICE Clear Credit LLC (ICC) seeking a CFTC order that would permit ICC and its clearing members that are dually-registered as futures commission merchants and securities broker-dealers to (i) commingle positions in swaps and security-based swaps and related customer money, securities, and property in a cleared swaps customer account and (ii) portfolio margin the swaps and the security-based swaps held in such an account.

The comment period for the ICC petition closes on December 22. The ICC petition may be found here.

BROKER DEALER

SEC Adopts Rule to Require Risk Management Controls for Brokers or Dealers with Market Access

The Securities and Exchange Commission has adopted Rule 15c3-5 to require broker-dealers with access or that provide access to trading securities directly on an exchange or alternative trading system to establish, document

and maintain a system of risk management controls and supervisory procedures that are reasonably designed to: i) systematically limit the financial exposure of the broker-dealer that could arise as a result of market access and ii) ensure compliance with all regulatory requirements that are applicable in connection with market access. Rule 15c3-5 requires that the financial risk management controls and supervisory procedures established are reasonably designed to: i) prevent the entry of orders that exceed appropriate pre-set credit or capital thresholds, or that appear to be erroneous; ii) prevent the entry of orders unless there has been compliance with all regulatory requirements that must be satisfied on a pre-order entry basis; iii) prevent the entry of orders that the broker or dealer or customer is restricted from trading; iv) restrict market access technology and systems to authorized persons; and v) assure appropriate surveillance personnel receive immediate post-trade execution reports.

Click here to read Release No. 34-63241.

FINRA and the SEC Issue Joint Guidance on Effective Policies and Procedures for Broker-Dealer Branch Inspections

The Financial Industry Regulatory Authority and the Securities and Exchange Commission have issued a National Exam Risk Alert (the Risk Alert) that provides broker-dealers with guidance on adopting effective policies and procedures for branch office inspections. The Risk Alert highlights some practices that examiners have identified as effective in branch office supervisory systems. Such recommended practices may include the following:

- Using risk analysis to identify whether individual non-supervising branches should be inspected more frequently than the FINRA-required minimum three-year cycle;
- Using surveillance reports to help identify risk and that considers the type of business conducted at each branch;
- Employing comprehensive checklists that incorporate previous inspection findings and trends from internal reports such as audit reports;
- Conducting unannounced branch inspections either randomly or based on certain risk factors;
- Including in a branch office inspection report any noted deficiencies and areas of improvement, as well as including an outline of agreed upon actions and timelines to correct the identified deficiencies;
- Using examiners with sufficient experience to understand the business being conducted at the particular branch being examined and the gravitas to challenge assumptions;
- Designing procedures to avoid conflicts of interest by examiners;
- Involving qualified senior personnel in several branch office examinations per year;
- Incorporating findings on results of branch office inspections into appropriate management information or risk management systems;
- Using a compliance database that enables compliance personnel in various offices to have centralized access to comprehensive information about all of the firm's registered representatives and their business activities;
- Providing branch office managers with the firm's internal inspection findings and requiring them to take and document corrective action;
- Tracking corrective action taken by each branch office manager in response to branch audit findings; and
- Elevating the frequency and/or scope of branch inspections where registered personnel are allowed to conduct business activities other than as associated persons of a broker-dealer, for example away from the firm.

Click here to read the National Exam Risk Alert.

LITIGATION

Seventh Circuit Vacates Class Certification Based on Counsel Misconduct

The U.S. Court of Appeals for the Seventh Circuit vacated the lower court's decision to grant class certification based on the misconduct of plaintiff's counsel.

The lower court certified a class consisting of more than 14,000 recipients of unsolicited faxed advertisements from Ashford Gear LLC, a small California home furnishings wholesaler. The Telephone Consumer Protection Act imposes a fine of $500 per "junk" fax and provides for treble damages in cases of willful violations. Class counsel learned about the potential violations from the fax broadcaster who sent the faxes on behalf of Ashford. Counsel allegedly asked the broadcaster for the transmission reports of the junk faxes and promised to keep information about the faxes confidential. Nevertheless, based on information procured from the fax broadcaster, the attorneys contacted Creative Montessori Learning Center, and misleadingly implied that Creative could join a class that had already been formed.

The district court found that the lawyers engaged in misconduct, but, applying a standard whereby only the most egregious attorney misconduct could result in denial of class certification, ruled that the misconduct did not preclude counsel from representing the class and granted class certification. The Seventh Circuit reversed, finding that misconduct that creates "serious doubt" about counsel's ability to represent the class loyally was sufficient to deny class certification. The case was remanded to the district court with instructions to apply the proper standard.

Creative Montessori Learning Centers v. Ashford Gear LLC, No. 11-8020 (7th Cir. Nov. 22, 2011).

Civil RICO Case Fails In Absence of Specific Fraud Allegations

A Colorado federal district court dismissed RICO claims in a case involving a property owner and a homeowners' association, finding that the plaintiffs failed to plead specific instances of fraud necessary to sustain the claims.

Plaintiff Western States Enterprises agreed to build homes for resale and to be the record owner of the lots until ownership was transferred to purchasers of the homes. Defendant Lloyd Land, president of the local homeowners' association (HOA), filed Notice of Assessment liens and instructed HOA attorneys to send debt collection letters to plaintiff and other local homeowners, asserting that they owed past due amounts.

The plaintiffs asserted claims under the federal RICO statute and its state equivalent, alleging that Land used "coercive tactics and fraudulent information" to force the property owners to pay amounts they did not owe, and also engaged in a conspiracy to defraud. The complaint disputed only the specific amounts due, not that delinquencies existed. The defendants moved to dismiss on multiple grounds, including failure to state a claim.

A civil RICO claim requires four elements: (i) conduct (ii) of an enterprise (iii) through a pattern (iv) of racketeering activity. Two or more predicate acts are necessary to demonstrate the requisite pattern of the third element. The plaintiffs alleged mail fraud as the predicate acts. However, the court ruled that the complaint failed to plead fraud with the necessary particularity. The plaintiffs did not allege specific information to show any material false representation in the debt collection letters, and only conclusorily alleged a conspiracy without alleging facts to show that a scheme was devised. In light of these pleading failures, the court granted the motion to dismiss.

Western States Enterprises, Inc. v. Land, 2011 WL 5882181 (D.Colo. Nov. 22, 2011).

EXECUTIVE COMPENSATION AND ERISA

DOL Warns on Indemnification of Brokers for IRA Trading Losses

In Advisory Opinion 2011-09A, the U.S. Department of Labor (DOL) indicated that a personal indemnification of a broker by the holder of an individual retirement account (IRA), for losses in excess of the value of the assets in a futures trading account established for the IRA, raises prohibited transaction issues under section 4975 of the

Internal Revenue Code of 1986 (the Code). Further, the DOL said that Prohibited Transaction Class Exemption 80-26 (PTE 80-26) does not provide an exemption for such a prohibited transaction. Previously, the DOL has advised practitioners informally of this position, but the Advisory Opinion formalizes it.

Under both the Employee Retirement Income Security Act of 1974 (ERISA) and Code section 4975, an extension of credit between a plan and a party in interest or a disqualified person is a prohibited transaction. (A "disqualified person" is the section 4975 parallel to a "party in interest" under ERISA, and an IRA holder who self-directs the IRA's investments is a disqualified person with respect to the IRA.) 80-26 is a DOL Class Exemption applicable to ERISA and section 4975, which permits loans and extensions of credit between a plan and a party in interest or disqualified person for payment of a plan's "ordinary operating expenses" or purposes "incidental to the ordinary operation of the plan."

Earlier, in Advisory Opinion 2009-03A, the DOL advised that a security interest to a broker in an IRA holder's non-IRA assets held by the broker, to cover losses in excess of the IRA's assets, would constitute a prohibited transaction. Advisory Opinion 2011-09A provides further advice affecting a broker's attempts to protect against trading losses that exceed the value of the account's assets.

In Advisory Opinion 2011-09A the DOL stated that the IRA holder's indemnification of the broker for trading losses in excess of the IRA's assets constituted a prohibited extension of credit between the IRA holder and the IRA. The DOL stated that PTE 80-26 would not cover the indemnification because (i) it was not used to pay expenses of "an ordinary activity attributable to a plan" and (ii) it was not "incidental" to the operation of a plan, as would be the case with an extension of credit to cover, for example, a bank overdraft or liquidity problem.

While the DOL advice addresses a futures account established for an IRA, the same principles would apply to similar arrangements, such as an options trading account, and to plans subject to ERISA if, for example, the plan sponsor was asked to provide indemnification for the plan's trading losses.

Advisory Opinion 2011-9A may be found here.
Advisory Opinion 2009-3A may be found here.

BANKING

Frank to Retire; Waters is Frontrunner for Chair

On November 28, Barney Frank, long-time Chairman and currently ranking member of the House Financial Services Committee, announced he would not seek reelection in 2012. Representative Maxine Waters, D - Cal., announced on November 29 that she would seek Frank's position once vacated. Aside from Mr. Frank, Ms. Waters has seniority among all Democrats on the committee. She is currently the subject of an ethics investigation.

Five Major Financial Trade Groups Ask for Extension of Volcker Rule Comment Deadline

On November 30, five financial trade groups (the Securities Industry and Financial Markets Association, the American Bankers Association, the Financial Services Forum, The Financial Services Roundtable, and the Institute of International Bankers) requested federal banking regulators and the Securities and Exchange Commission to extend the January 13 comment deadline on the 298-page proposal to implement the Volcker Rule. In a letter the trade groups stated the extension is needed because of the proposal’s potentially far-reaching impact, its unusual request for comment on more than 1,400 questions, and the fact that the Commodity Futures Trading Commission has not yet submitted its companion Volcker proposal. One analysis, by the American Bankers Association, found the proposed rule -- purportedly affecting only the largest banks -- could actually affect the activities of more than 1,000 institutions and require nearly every bank to create a new compliance program.

For more information, click here.

Office of Comptroller of the Currency Issues Proposed Guidance for Purchase of Investment Securities by Banks and Thrifts

On November 29, the Office of the Comptroller of the Currency (OCC) proposed guidance to assist national banks and Federal savings associations in meeting due diligence requirements in assessing credit risk for portfolio investments. Comments must be received by December 29. Section 939A of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) requires each Federal agency, within one year of enactment, to review: (i) any regulations that require the use of an assessment of the creditworthiness of a security or money market instrument, and (ii) any references to or requirements in those regulations regarding credit ratings. Section 939A then requires the Federal agencies to modify the regulations identified during the review to substitute any references to or requirements of reliance on credit ratings with such standards of creditworthiness that each agency determines to be appropriate. The OCC proposes to amend the definition of ''investment grade'' in 12 CFR part 1 to no longer reference credit ratings. Instead, ''investment grade'' securities would be those where the issuer has an adequate capacity to meet the financial commitments under the security for the projected life of the investment. An issuer has an adequate capacity to meet financial commitments if the risk of default by the obligor is low and the full and timely repayment of principal and interest is expected. Generally, securities with good to very strong credit quality will meet this standard. National banks will have to meet this new standard before purchasing investment securities.

The OCC also is proposing to define the term ''investment grade,'' for Federal savings associations, as it is used in Part 160, to refer to 12 U.S.C. 1831e. This effectively will reference the current ratings-based requirement until such time as the requirement is replaced by the Federal Deposit Insurance Corporation. In addition, the OCC is proposing to remove references to credit ratings applicable to commercial paper and corporate debt securities contained in §§ 160.40 and 160.93(e)(5)(ii). Under the revised rules, savings associations would be permitted to invest in commercial paper if it meets the standards set forth at 12 U.S.C. 1831e(d)(1), which currently limits savings associations to purchasing corporate debt securities that are of investment grade, but will, after July 21, 2012, include a new creditworthiness standard established by the FDIC.

In addition, the guidance calls for national banks and savings institutions to "maintain appropriate ongoing reviews" of their investment portfolios based on risk profile and the size and complexity of the securities.

For more information, click here.

FDIC, Treasury Propose Maximum Obligation Limitation Rules for FDIC Receiverships Involving Covered Financial Companies

On November 25, a notice of proposed rulemaking was published jointly by the Federal Deposit Insurance Corporation (the FDIC) and the Departmental Offices of the Department of the Treasury (the Treasury, and collectively, the Agencies) to implement applicable provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act). In accordance with the requirements of the Dodd-Frank Act, the proposed rules govern the calculation of the maximum obligation limitation (MOL), as specified in section 210(n)(6) of the Dodd-Frank Act. The MOL limits the aggregate amount of outstanding obligations that the FDIC may issue or incur in connection with the orderly liquidation of a "covered financial company." Under section 201(a)(8) of the Dodd-Frank Act, a ''covered financial company'' is a ''financial company'' for which a systemic risk determination has been made pursuant to section 203(b) of the Dodd-Frank Act but does not include an insured depository institution.

Specifically, the MOL provides that the FDIC "may not, in connection with the orderly liquidation of a covered financial company, issue or incur any obligation, if, after issuing or incurring the obligation, the aggregate amount of such obligations outstanding …for each covered financial company would exceed— (A) an amount that is equal to 10 percent of the total consolidated assets of the covered financial company, based on the most recent financial statement available, during the 30- day period immediately following the date of appointment of the FDIC as receiver (or a shorter time period if the [FDIC] has calculated the amount described under subparagraph (B)); and (B) the amount that is equal to 90 percent of the fair value of the total consolidated assets of each covered financial company that are available for repayment, after the time period described in subparagraph (A)."

Section 210(n)(7) of the Dodd-Frank Act requires the Agencies, in consultation with the Financial Stability Oversight Council (FOSC) prescribe regulations governing the calculation of the MOL. In accordance with this section, the Agencies have consulted with the FSOC, and have determined that it would be most appropriate to adopt regulations that closely follow the statutory language for calculating the MOL, while defining certain terms

referenced in the statute and seeking comment on those definitions. The proposed regulation thereafter defines the terms "obligations," "most recent financial statements available, "fair value," and "‘‘total consolidated assets of each covered financial company that are available for repayment.’’ In particular, the Agencies invited comments on whether the definitions proposed are appropriate.

Comments are due January 24, 2012. For more information, click here.

UK DEVELOPMENTS

FMLC Publishes Comments on HM Treasury Proposals for New UK Regulatory Structure

On November 22, the Financial Markets Law Committee (FMLC) published its final response comments to HM Treasury's June 2011 consultation on the government’s new UK financial services regulatory structure.

The FMLC’s response identifies several areas of concern and focuses on the following topics: coordination between regulatory authorities; enforcement; regulatory processes, permission and regulated activities; European Union passporting; listing of securities and extra-territoriality; rules and guidance; administrative discretion and other powers; and systemically important infrastructure.

For more information, click here.

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