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CORPORATE & FINANCIAL
WEEKLY DIGEST

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SEC/CORPORATE

SEC Advisory Committee on Small and Emerging Companies Makes Recommendations

On March 21, the Securities and Exchange Commission Advisory Committee on Small and Emerging Companies (Advisory Committee) submitted several recommendations to the SEC on rules, regulations and policies relating to emerging privately held small businesses and publicly traded companies with less than $250 million in public market capitalization.

Scaled Disclosure Recommendations

The Advisory Committee addressed some inconsistencies between the scaled disclosure requirements available to "smaller reporting companies" under current SEC rules and to emerging growth companies under the Jumpstart Our Business Startups Act. The Advisory Committee recommended that the SEC revise disclosure requirements for smaller reporting companies to include certain exemptions available to emerging growth companies, including exemptions from shareholder advisory votes on executive compensation and the frequency of those votes ("say-on-pay" and "say-on-frequency" votes), certain compensation disclosure requirements and certain requirements relating to compliance with financial accounting standards. In addition, the Advisory Committee recommended that smaller reporting companies no longer be required to file with their material contracts schedules or similar attachments that are not material to an investment decision or otherwise disclosed, or submit financial information in XBRL format for periodic reports and other filings. The Advisory Committee also expressed its belief that the threshold for smaller reporting companies is too low and recommended that the definition of a smaller reporting company be revised to include companies with public floats of up to $250 million (or less than $100 million in annual revenues if the public float cannot be calculated). The Advisory Committee further recommended that the definition of "accelerated filer" be revised to include companies with public floats of $250 million or more, but less than $700 million, as of the applicable measuring date (thereby excluding companies with public floats of between $75 million and $250 million from the auditor attestation requirement under Section 404(b) of the Sarbanes-Oxley Act).

Click here to read the full text of the recommendation.

In a separate recommendation, the Advisory Committee expressed its belief that the disclosure requirements in the Dodd-Frank Wall Street Reform and Consumer Protection Act relating to conflict minerals and payments by resource extraction issuers are disproportionately burdensome to small businesses and outside of the scope of the SEC's mission. The Advisory Committee recommended that the SEC inform the Committee on Banking, Housing and Urban Affairs of the Senate and the Committee on Financial Services of the House of Representatives of the Advisory Committee's belief.

Click here to read the full text of the recommendation.

Trading Recommendations

The Advisory Committee further expressed its belief that current US equity markets may be unsatisfactory for the trading of securities of small and emerging companies due to onerous listing requirements and failure to provide sufficient liquidity. The Advisory Committee recommended that the SEC encourage the creation of a separate equity market with a more flexible regulatory regime for trading in securities of small and emerging companies by accredited investors.

Click here to read the full text of the recommendation.

In a separate recommendation, the Advisory Committee expressed its belief that a change in the method of determining tick sizes for equity securities of smaller exchange-listed companies could increase their liquidity and facilitate initial public offerings and capital formation. The Advisory Committee recommended that the SEC adopt rules to increase tick size for these companies and allow them to choose their own tick sizes within a limited range determined by the SEC.

Click here to read the full text of the recommendation.

SEC Provides Guidance Regarding Social Media and Regulation Fair Disclosure (Regulation FD)

On April 2, in connection with an investigation of Netflix, Inc. and its Chief Executive Officer, Reed Hastings, regarding a possible violation of Regulation FD, the Securities and Exchange Commission released a Report of Investigation clarifying a company is permitted to use social media outlets such as Facebook and Twitter to provide important company information to the public pursuant to Regulation FD, so long as those social media outlets are viewed as “recognized channels of distribution” and the company first takes “steps sufficient to alert investors and the market to the channels it will use for the dissemination of material, nonpublic information.”

Regulation FD requires that if an issuer or its representatives discloses material, nonpublic information to stockholders or securities market professionals in a situation where it is reasonably foreseeable that such investors or professionals will trade on the basis of this information, the same information must be distributed to the public simultaneously for intentional disclosures and promptly for non-intentional disclosures. The investigation by the SEC was initiated after Mr. Hastings made a post on his personal Facebook page regarding the hours of content streamed by Netflix in June of 2012, which coincided with an increase in the stock price of Netflix. Prior to this post, the Facebook page of Mr. Hastings had not been used to announce any metrics of Netflix, and Netflix had not indicated to the public or its shareholders that Mr. Hastings’s Facebook page would be used to disclose information regarding Netflix. In addition, Netflix did not file a Form 8-K, issue a press release or make a post on its own Facebook page to accompany the disclosure posted by Mr. Hastings.

In the Report of Investigation, the SEC made clear that communications by issuers using social media outlets, just like communications made through more traditional channels, must be analyzed carefully for compliance with Regulation FD, and confirmed that the guidance it issued in 2008 regarding the application of Regulation FD to dissemination of information through a company’s website also applies to the dissemination of information through social media outlets. In that 2008 guidance, the SEC stated that for a company’s website to serve as a broad, non-exclusionary method of distributing information to the public pursuant to Regulation FD, the website must be a “recognized channel of distribution” for communicating with the company’s investors. This requirement is also applicable to social media outlets, and in the Report of Investigation, the SEC reminded companies that it expects them to “examine rigorously the factors indicating whether a particular channel is a recognized channel of distribution.”

The SEC also emphasized that, consistent with the guidance issued in 2008, providing investors with appropriate notice of the forms of communication that a company plans to use to disclose material, nonpublic information, including information regarding any social media outlets that may be used for such purpose and the types of information that may be disclosed through these outlets, is “critical to the fair and efficient disclosure of information.” One possible way to provide this notice to investors, as suggested by the SEC in the Report of Investigation, is to include disclosure on a company’s corporate website identifying the specific social media outlets through which that company intends to disseminate material, nonpublic information.

Based on this analysis, the SEC stated in the Report of Investigation that “disclosure of material, nonpublic information on the personal social media site of an individual corporate officer, without advance notice to investors

that the site may be used for this purpose, is unlikely to qualify as a method reasonably designed to provide broad, non-exclusionary distribution of the information to the public within the meaning of Regulation FD."

The Report of Investigation is available here.

BROKER DEALER

SEC Amends Filing Requirements for Dually Registered Clearing Agencies

The Securities and Exchange Commission issued a final rule affecting clearing agencies registered with both the SEC and the Commodity Futures Trading Commission. The final rule allows certain rule changes by such dually registered clearing agencies to become effective upon filing with the SEC, which is an expansion of an interim rule adopted by the SEC on July 7, 2011.

To become effective upon filing with the SEC, the dually registered clearing agency's rule change must primarily affect the clearing of non-securities products, such as futures, swaps and forwards that do not reference any securities. If a rule change applies generally to the operations of the entire clearing agency, such as a change to a general provision of the clearing agency's bylaws, then the change would not be considered to primarily affect the clearing of non-securities products.

In addition to the "primarily affects" requirement, the rule change also must not significantly affect the clearing agency's securities clearing operations, even if such effects are indirect. It is important to note that there is an exception to this restriction for rule changes that are necessary to maintain fair and orderly markets for non-securities products. However, the SEC would retain the power to summarily temporarily suspend such rule changes until the SEC is able to enter an order approving or disapproving such change.

The SEC also adopted corresponding amendments to the instructions to Form 19b-4.

The SEC's final rule release is available here.

SEC Extends Compliance Date for Certain Large Trader Requirements

The Securities and Exchange Commission has extended the compliance date for broker-dealers from certain large trader recordkeeping, reporting and monitoring requirements. The SEC implemented large trader requirements in two phases, the first of which began on November 30, 2012. Phase one includes recordkeeping and reporting requirements for clearing broker-dealers of large traders that (i) are US-registered broker-dealers or (ii) trade via sponsored access arrangements.

Phase two, which was originally scheduled to take effect on May 1, 2013, includes the remaining large trader recordkeeping, reporting and monitoring provisions. However, the SEC has determined to delay the implementation of phase two to November 1, 2013 to give the SEC more time to evaluate the implementation issues presented in phase one. The delayed implementation also will allow broker-dealers subject to phase two more time to prepare for compliance with the large trader requirements applicable to them under phase two.

The SEC's exemptive order is available here.

DERIVATIVES

Federal Reserve Board Approves Final "Predominately Engaged in Financial Activities" Rule

The Board of Governors of the Federal Reserve System has approved a final rule setting forth requirements for determining when a company is "predominately engaged in financial activities." Although the rule addresses the meaning of that phrase only in the context of Title I of the Dodd-Frank Wall Street Reform and Consumer Protection Act, it also provides the most comprehensive guidance to date as to when an entity will be a "financial entity" for purposes of the swap rules under Title VII. This guidance is based on the final clause of the definition of

that term (i.e., “a person predominantly engaged in activities . . . that are financial in nature, as defined in Section 4(k) of the Bank Holding Company Act of 1956”).

The rule also defines the terms “significant nonbank financial company” and “significant bank holding company.” All these definitions are relevant when the Financial Stability Oversight Council is considering designating a nonbank financial company for consolidated supervision by the Federal Reserve under the authority of Title I.

The effective date of the rule is May 6, 2013.

Some highlights from the rule:

- Predominance can be found if a company meets the relevant tests in either of its last two fiscal years.
- Engaging in physically settled derivative transactions is not considered a “financial activity.”
- The rule has a lengthy appendix setting forth all activities that have been historically determined by the Federal Reserve to be financial in nature.

The text of the final rule is available here.

The related press release is available here.

CFTC

CFTC Approves Clearing Exemption for Inter-Affiliate Swaps

On April 1, the Commodity Futures Trading Commission approved a final rule that permits certain affiliates to elect not to clear a swap. To qualify for the clearing exemption, the counterparties’ financial statements must be reported on a consolidated basis and one counterparty must hold a majority ownership interest in the other counterparty or a third party must hold a majority interest in both counterparties. In addition, the following conditions must be met: (i) both counterparties must elect not to clear the swap; (ii) the terms of the swap must be documented in swap trading relationship documentation that satisfies certain CFTC requirements; (iii) the swap must be subject to a centralized risk management program that is designed to monitor and manage the risks associated with the swap; and (iv) each “outward-facing” swap entered into by the affiliated counterparties with unaffiliated counterparties must be cleared or exempt from clearing in accordance with CFTC or comparable foreign requirements.

The requirement to clear outward-facing swaps (Clearing Requirement), which was adopted by the CFTC to address potential evasion of the mandatory clearing requirement by market participants entering into swaps with affiliates in jurisdictions that do not have mandatory clearing requirements, may be met by: (i) complying with the CFTC’s clearing requirement; (ii) complying with a foreign jurisdiction’s clearing mandate that the CFTC has determined is comparable to its clearing requirement; (iii) complying with an exception or exemption from the clearing requirement under the Commodity Exchange Act or CFTC regulations; (iv) complying with an exception or exemption from mandatory clearing under a foreign law that the CFTC has determined is comparable to the analogous CFTC exceptions or exemptions; or (v) clearing such swaps through a registered derivatives clearing organization or a clearing organization that is subject to supervision by appropriate government authorities in the home country of the clearing organization and that has been assessed to be in compliance with the Principles for Financial Market Infrastructures.

If one of the affiliates involved in a transaction in a class of swaps that is subject to mandatory clearing under CFTC rules is located in the European Union, Japan or Singapore (Qualifying Affiliate), the Clearing Requirement will not apply to the outward-facing trades effected by such affiliate until March 11, 2014. However, if a “financial entity” controls one or both of the affiliates or the affiliates are affiliated with a swap dealer or major swap participant, the affiliates may satisfy the Clearing Requirement by ensuring that the trade between the two affiliates or the trade between the Qualifying Affiliate and an unrelated counterparty is marked to market on a daily basis. This “mark-to-market” exception terminates on March 11, 2014.

If one of the affiliates involved in a transaction in a class of swaps that is subject to mandatory clearing under CFTC rules is not located in the United States, the European Union, Japan or Singapore, and the aggregate notional value of such swaps between the affiliates does not exceed five percent of the aggregate notional value of all such swaps between all counterparties (as measured on a quarterly basis), then the outward-facing trades effected by such affiliate are exempt from the Clearing Requirement until March 11, 2014 if mark-to-market requirements similar to those described above are satisfied.

If the inter-affiliate clearing exemption is elected, the reporting counterparty must provide to a swap data repository: (i) confirmation that both counterparties meet the criteria for the inter-affiliate clearing exemption and are electing not to clear the swap; (ii) information regarding how the counterparties meet their financial obligations associated with the uncleared swaps; and (iii) certain additional information if the counterparties are issuers of registered securities or are subject to reporting requirements under Section 15(d) of the Securities Exchange Act of 1934.

The final rule will become effective 60 days after publication in the *Federal Register*.

For more information, click here.

CFTC Issues Rule Regarding Persons Associated with Multiple Swap Dealers or Major Swap Participants

On April 1, the Commodity Futures Trading Commission issued a final rule clarifying that each swap dealer (SD), major swap participant (MSP) or other CFTC registrant with whom an associated person (AP) is associated is required to supervise the AP and may be held jointly and severally liable for the AP's activities related to customers that are common to it and any other SD, MSP or CFTC registrant. The final rule is similar to the current requirement that applies to futures commission merchants, retail foreign exchange dealers, introducing brokers, commodity trading advisors, commodity pool operators and leverage transaction merchants with dually registered APs. The supervision and joint and several liability requirements for dual APs apply to SDs and MSPs even though their APs are not required to register with the CFTC.

For more information, click here.

CFTC Staff Issues No-Action Letters

The Commodity Futures Trading Commission staff recently released a series of letters relating to a variety of regulatory issues, including registration relief for certain entities and recordkeeping requirements for certain swap dealers (SDs) and major swap participants (MSPs).

- **IB and CTA Registration.** In CFTC Letter No. 13-04, the Division of Swap Dealer and Intermediary Oversight (DSIO) granted no-action relief from registration as an introducing broker (IB) or a commodity trading advisor (CTA) to certain affiliates of a swap counterparty and the affiliates' employees. The letter makes available registration relief to certain persons who would not otherwise be eligible for the relief DSIO previously provided to Agent Affiliates under CFTC Letter No. 12-70. The relief is subject to a number of conditions, including that the swap counterparty be registered as an SD within a specific period of time and conditions similar to those specified in CFTC Letter No. 12-70. CFTC Letter No. 13-04 is available here. CFTC Letter No. 12-70 is available here.

- **CPO Registration.** Pursuant to CFTC Letter No. 13-07, DSIO extended the relief granted to commodity pool operators (CPOs) of securitization vehicles under CFTC Letter No. 12-45 until June 30, 2013. In order to remain eligible for the no-action relief, the CPO of a securitization vehicle must satisfy numerous criteria, including having initiated its registration as a CPO by filing Forms 7-R and 8-R and any required fees by March 31 and filing an email notice with DSIO. CFTC Letter No. 13-07 is available here. CFTC Letter No. 12-45 is available here.

- **SD and MSP Recordkeeping.** Pursuant to CFTC Letter No. 13-06, DSIO issued no-action relief that will delay the compliance date for certain SD and MSP recordkeeping obligations until June 30, 2013 for all SDs and MSPs. The records covered by the no-action letter include: (i) records of oral communications related to pre-execution swap trade information and communications that lead to the conclusion of a related cash or forward transaction that occurs in a jurisdiction other than the United States, United Kingdom, Singapore, Hong Kong, Japan, Australia, Switzerland or Canada; (ii) the requirement to maintain transaction and daily

trading records in a manner that is identifiable and searchable by transaction and counterparty, provided that the firm maintains records using existing search capabilities; (iii) the requirement to use a Coordinated Universal Time (UTC) timestamp, provided that data recorded in local time can be readily converted to UTC and that the firm commits to using UTC time in new or upgraded systems; and (iv) the requirement to maintain records at the principal place of business or principal offices, provided that the records are available at such location within 72 hours. CFTC Letter No. 13-06 is available here.

LITIGATION

Southern District Rejects Evidence from "Confidential Witnesses" as Basis for Securities Class Action

A securities class action lawsuit against Canadian Solar, Inc. (CSI) was recently dismissed in the US District Court for the Southern District of New York for failing to adequately plead the required elements of a federal securities fraud claim. Plaintiffs alleged that CSI made false and misleading statements, including: (i) two of CSI's 2009 financial reports, which were false and misleading because they incorporated a "sham" transaction; and (ii) statements about its internal controls.

District Court Judge Robert W. Sweet found that the plaintiffs had failed to state a claim for securities fraud for three independent reasons. First, none of the statements that the plaintiffs identified, which generally consisted of Securities and Exchange Commission filings and press releases, were false or misleading. In particular, the court noted that plaintiffs failed to provide any "specific facts" about any transactions that plaintiffs alleged to be "sham" transactions. The court rejected the allegations from four "confidential witnesses" because the basis for the witnesses' knowledge was not stated with any particularity.

Second, the court found that plaintiffs failed to plead *scienter* because there was a "more cogent and compelling," "non-culpable" explanation for the allegations regarding the "sham" transaction and that the plaintiffs' failed to provide particularized facts as to the knowledge of the "fraud" of anyone at CSI.

Third, the complaint did not adequately allege loss causation because neither of the documents on which the plaintiffs relied in their complaint (an announcement that CSI might file revised financial reports and the disclosure of an SEC subpoena) was sufficient to act as a corrective disclosure.

Janbay v. Canadian Solar, Inc., No. 10 Civ. 4430 (S.D.N.Y. Mar. 28, 2013).

Court Dismisses Securities Class Action Alleging Misrepresentations About "Cannibalization"

A class-action complaint filed against Travelzoo, Inc. (Travelzoo) in the US District Court for the Southern District of New York was recently dismissed. The complaint alleged that Travelzoo made misstatements in its Securities and Exchange Commission filings and press releases about its competition from other companies and potential for growth when it failed to disclose that its recently launched "Local Deals Getaways" business (Getaways) would compete directly with its core travel business.

The court found that the plaintiffs failed to demonstrate that mere existence of "cannibalization"—or internal competition—between Getaways and Travelzoo's core travel business was material. The court noted that cannibalization does not necessarily lead to an overall loss of revenue for a company, and is not a factual statement about a company that would lead to a drop in the company's stock price. Because the cannibalization between Getaways and Travelzoo's core travel business was only a potentially adverse effect, Travelzoo had no duty to disclose it.

In addition, the court found that the plaintiffs failed to adequately plead both *scienter* and loss causation. While some individual defendants were aware of the potential negative effect of the competition between Getaways and Travelzoo's core travel business and all individual defendants had access to Travelzoo's revenue reports, the court found that this alone was insufficient to demonstrate that any individual defendant knew that the cannibalization would negatively impact Travelzoo's revenue. Finally, the court noted that loss causation was not adequately pled as the facts indicated that the stock decline was due to general market disappointment.

In re Travelzoo Inc. Securities Litigation, 11 Civ. 5531, 11 Civ. 6845 (S.D.N.Y. Mar. 29, 2013).

Attacks on Proxy Statement Compensation Disclosure

Litigation challenging equity compensation exploded in 2012 and shows no signs of slowing, with a storm of lawsuits targeting Rule 10b5-1 trading plans threatening to strike for 2013 as well. Securities partners Lawrence Levin, William Regan, Jennifer Ryan and Richard Zelichov presented this webinar update to The Gathering Storm: Equity Compensation and 10b5-1 Plans Under Attack along with a last-minute checklist for proxy statements and thoughts for the future. The program discussed the onslaught of executive compensation lawsuits regarding disclosures concerning say-on-pay, new share authorizations and IRC Section 162(m), while providing strategies and best practices for addressing these issues.

To view a PDF of the presentation materials, click here.

To view a recording of the webinar, click here.

BANKING

FDIC Announces Availability of Educational Videos

On April 3, the Federal Deposit Insurance Corporation (FDIC) announced the release of the first in a series of technical assistance videos to provide useful information to bank directors, officers and employees on areas of supervisory focus and proposed regulatory changes.

The first installment of six videos is designed to provide new bank directors with information to prepare them for their important fiduciary role. Three of the videos address the roles and responsibilities of a director and the other three videos provide information about the FDIC's Risk Management and Compliance Examination processes.

A second installment, to be released by June 30, 2013, is a virtual version of the FDIC's Directors' College Program that regional offices deliver throughout the year. The initial curriculum will consist of six modules covering interest rate risk, third-party relationships, corporate governance, the Community Reinvestment Act, information technology and the Bank Secrecy Act.

A third installment, to be released by year-end, will provide virtual technical training for bank officers and employees. These videos will provide more in-depth coverage of important supervisory topics and focus on management's responsibilities. The training program will include Fair Lending, appraisals and evaluations, interest rate risk, troubled debt restructurings, the allowance for loan and lease losses, evaluation of municipal securities and flood insurance.

The videos and additional information are available here.

CFPB Releases Public Complaint Database

On March 28, the Bureau of Consumer Financial Protection (CFPB) announced the release of a public database of federal consumer financial complaints with information on more than 90,000 individual complaints on financial products and services. The release "expands significantly from about 19,000 credit card complaints to more than 90,000 complaints on mortgages, student loans, bank accounts and services, other consumer loans, and credit cards. In many cases, it includes the sub-category of products. For example, for mortgages it includes reverse mortgages, conventional fixed mortgages, conventional adjustable mortgages, and home equity loans or lines of credit."

In accompanying materials, the CFPB explained that, "We don't verify all the facts alleged in these complaints but we do take steps to confirm a commercial relationship between the consumer and company. Complaints are listed here after the company responds or after they have had the complaint for 15 calendar days, whichever comes first. We remove complaints if they don't meet all of the publication criteria. Data is refreshed nightly."

The database is available here.

Thomas J. Curry Named FFIEC Chairman

On April 1, Thomas J. Curry, Comptroller of the Currency, Office of the Comptroller of the Currency (OCC), was named Chairman of the Federal Financial Institutions Examination Council (FFIEC) for a two-year term. Curry succeeds Debbie Matz, Chairman of the National Credit Union Administration (NCUA). The FFIEC also named Daniel K. Tarullo, member of the Board of Governors of the Federal Reserve System (Board), as its new Vice Chairman for a two-year term.

The FFIEC was created by the Financial Institutions Regulatory and Interest Rate Control Act of 1978 to prescribe uniform principles, standards and report forms for the federal examination of financial institutions, and to make recommendations to promote uniformity in the supervision of financial institutions. It also conducts schools for examiners employed by the five federal member agencies represented on the FFIEC and makes those schools available to employees of state agencies that supervise financial institutions. The FFIEC currently consists of the following six voting members: the Comptroller of the Currency, OCC; a member of the Board, appointed by the Chairman of the Board; Chairman of the Federal Deposit Insurance Corporation; Director of the Consumer Financial Protection Bureau; Chairman of the NCUA; and the Chairman of the FFIEC's State Liaison Committee (SLC). The SLC consists of five representatives of state banking agencies that supervise financial institutions and the members are designated from the Conference of State Bank Supervisors, the American Council of State Savings Supervisors, the National Association of State Credit Union Supervisors and the FFIEC for two two-year terms.

For more information, click here.

Federal Reserve Board Approves Final "Predominately Engaged in Financial Activities" Rule

Please see "Federal Reserve Board Approves Final 'Predominately Engaged in Financial Activities' Rule" in **Derivatives** above.

EXECUTIVE COMPENSATION AND ERISA

US Supreme Court's Impending Decision on DOMA May Impact Most Employee Benefit Plans

Late last month the US Supreme Court heard oral arguments in two cases concerning same-sex marriage. The Court's decisions are expected by the end of June and, depending on how the Court rules, the decisions could have a significant impact on employee welfare and retirement plans.

One of the cases (*Hollingsworth v. Perry*) is somewhat limited in that it concerns the constitutionality of a 2008 California ballot measure (Prop 8) that, in response to a decision by the California Supreme Court recognizing the right of same-sex couples to marry, restricted marriage to one man and one woman. It is likely that the outcome of this case would apply only to the state of California and the determination of married persons under California law.

The case with more potential for broad impact, *Windsor v. United States*, directly challenges the constitutionality of Section 3 of the Defense of Marriage Act of 1996 (DOMA). DOMA defines "spouse" and "marriage" for purposes of federal laws, including the Internal Revenue Code, Employee Retirement Income Security Act (ERISA), Consolidated Omnibus Budget Reconciliation Act (COBRA), and Family and Medical Leave Act (FMLA) and Health Insurance Portability and Accountability Act of 1996 (HIPAA). It defines "spouse" as a person of an opposite sex who is an individual's husband or wife, and it defines "marriage" as a legal union between one man and one woman as husband and wife.

Various provisions of ERISA benefit plans use the term "spouse" to determine entitlement to benefits or to administer the plans. Unless the plan document contains a contrary definition, the definition typically used is the one established under federal law, which incorporates the DOMA definition. In many respects federal law guarantees benefits/rights only to "spouses" as defined by federal law, but the plan provisions are permitted (but not required) to go further and extend benefits/rights to other people, such as same-sex partners.

If Section 3 of DOMA is held to be unconstitutional, there would no longer be any basis for distinguishing under federal law between same-sex and opposite-sex spouses. If this occurs, federal common law will likely provide

that “spouse” for purposes of federal laws will be determined based upon the substantive law of the state in which the employee/spouse resides. As a result, an ERISA plan would be administered in a manner that treats as spouses same-sex partners who reside in a jurisdiction where same-sex marriages are recognized, and will not treat them as spouses in jurisdictions where same-sex marriages are not recognized.

Examples of benefit plan provisions which may need to be addressed or amended include:

GROUP HEALTH AND WELFARE PLANS

- Medical Benefits: Under current federal tax law, employees typically are unable to exclude from taxable income the value of employer-provided group health benefits provided to same-sex partners. Currently this results in additional income tax and payroll tax.

- Flexible Spending Arrangements (FSA), Health Reimbursement Arrangements (HRA) and Health Savings Accounts (HSA): Under federal tax law, the reimbursement of same-sex spouse expenses under an FSA, HRA or HSA would typically result in taxable income to the employee.

- COBRA Coverage: COBRA does not currently require extending continuation coverage rights to same-sex spouses (or their children).

- Family and Medical Leave Act Leave: Employees are not currently guaranteed the right to take leave to care for same-sex spouses.

- Health Insurance Portability and Accountability Act (HIPAA): Same-sex spouses are not currently guaranteed HIPAA special enrollment rights.

RETIREMENT PLANS

- Qualified Domestic Relations Orders (QDROs): Currently, domestic relations orders regarding same-sex spouses do not typically qualify as QDROs.

- Qualified Joint and Survivor Annuities (QJSA): Currently, ERISA plans are not required (but they are permitted) to provide to same-sex spouses a “QJSA” equivalent benefit.

- Timing of Required Distributions: Currently, a same-sex spouse cannot defer the receipt of required minimum distributions from retirement plans until April 1 of the year after the year in which the spouse would have reached age 70½. Instead, the same-sex spouse must begin receiving benefits either within one year of the employee’s death or receive full payment within five years.

In preparation for any action taken by the US Supreme Court, employers and administrators should: (1) review the definition of “spouse” in their benefit plans; (2) determine whether the plan’s definition of “spouse” is based upon federal or state law; (3) identify those states where employees are employed or reside which recognize same-sex spouses; and (4) start the process for determining which benefits (and administration) would need to be revised.

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