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Corporate and Financial Weekly Digest

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SEC/CORPORATE

SEC Proposes Creation of Large Trader Reporting System

On April 14, the Securities and Exchange Commission proposed the creation, under Section 13(h) of the Securities Exchange Act of 1934 (Exchange Act), of a large trader reporting system.

Currently, the SEC collects information on securities transactions from registered broker-dealers through the Electronic Blue Sheets (EBS) system, which the SEC uses to assist in the investigation of violations of federal securities laws and conduct market reconstructions. The EBS does not provide information regarding the timing of a trade or the identity of the customer. The EBS also does not efficiently collect large volumes of trade data in a timely manner that would permit contemporaneous analysis of market events. Accordingly, while the SEC believes that the EBS is useful in narrow enforcement investigations, it is ineffective for large-scale market reconstructions and analyses during peak trading periods.

The SEC is proposing the new Rule and Form to enhance its ability to identify large traders and their affiliates, promptly obtain trading data on the activity of large trades and aggregate and analyze trading data among affiliated large traders. The SEC has proposed classifying a large trader as a person who, in exercising investment discretion, effects transactions in any exchange-listed securities, including equities and options, in an amount equal to or greater than (1) during a calendar day, either 2 million shares or shares with a fair market value of $20 million; or (2) during a calendar month, either 20 million shares or shares with a fair market value of $200 million.

The proposed Rule 13(h) would require all large traders to identify themselves by filing a Form 13H with the SEC, which would be updated at least annually and more frequently if the information contained therein became inaccurate. Upon the receipt of a Form 13H, the SEC would assign each large trader a unique large trader identification number (LTID) which the large trader would be required to disclose to registered broker-dealers. The large trader's broker-dealers would be required to maintain records of transactions effected for large traders that are identified by the LTID, electronically report large trader information to the SEC upon its request and monitor compliance with the proposed Rules.

The proposed Form 13H would also require the large trader to disclose its contact information, certain business information, information about its affiliates and information about its accounts. The information contained on a Form 13H, as well as any additional information requested by the SEC, would be considered confidential and exempt from disclosure under the Freedom of Information Act. The proposed Rule 13(h) would also require registered broker-dealers to maintain substantial information about the large trader and its transactions, which would be required to be available to the SEC the morning of the day following the date the transactions were effected. The SEC believes that prompt access to such trading information would help it reconstruct market activity and investigate potentially manipulative or illegal trading activity.

Read more.

Pink OTC Markets Inc. Announces Creation of OTCQB™ Marketplace

On April 5, in an effort to better identify over-the-counter (OTC) securities that are registered and reporting with U.S. regulators, Pink OTC Markets Inc. announced the creation of the OTCQB™ marketplace, a new comprehensive OTC market tier that will include the securities of over 768 Securities and Exchange Commission reporting companies and banks formerly designated as Pink Sheets® stocks, in addition to the 3,050 securities that are currently quoted in both Pink OTC Markets' electronic interdealer quotation system and the Financial Industry Regulatory Authority's OTCBB™.

According to Pink OTC Markets Inc., with the creation of OTCQB™, investors will now be able to more easily identify all companies that are registered with the SEC or banking regulators, remain current in their reporting obligations and are quoted on the Pink OTC platform.

Click here for the press release issued by Pink OTC Markets Inc.

BROKER DEALER

SEC Proposes New Measures to Protect Investors in Options Markets

The Securities and Exchange Commission has proposed to put in place two investor protection measures in options markets that currently apply only to transactions involving exchange-listed stocks. Proposed Rule 610 of Regulation NMS would prohibit an options exchange from unfairly impeding access to displayed quotations and would establish a limit on the fees that an options exchange could charge investors for access to its best bid and offer for listed options on its exchange. By expanding the protections that are available in options markets, the SEC's proposal is aimed at helping to provide investors with the ability to achieve best execution for their orders and remove barriers that an options exchange might erect to keep non-members from accessing a quote on the exchange.

Public comments on the proposal should be received by the SEC within 60 days after publication in the Federal Register.

Click here to read SEC Release No. 34-61902.

FINRA Issues Guidance on Providing Consolidated Financial Account Reports to Customers

The Financial Industry Regulatory Authority has issued Regulatory Notice 10-19 reminding firms of their responsibilities when providing customers with consolidated financial account reports. These reports consolidate information regarding a customer's various financial holdings. Among other things, FINRA reminds firms that consolidated reports are communications with the public, and, as such, must be accurate, clear and not misleading. Also, consolidated reports must be structured in such a manner that neither customers nor third parties are likely to be misled or confused as to the nature of the information presented, or mistake the reports for official account statements. The distribution of consolidated reports must comply with all applicable FINRA rules and federal securities laws.

Click here to read FINRA Regulatory Notice 10-19.

FINANCIAL MARKETS

Federal Regulators Release Model Consumer Privacy Notice Online Form Builder

Eight federal regulators have released an Online Form Builder that financial institutions can download and use to develop and print customized versions of a model consumer privacy notice under the Gramm-Leach-Bliley Act (GLBA).

The Online Form Builder, based on the model form regulation published in the Federal Register on December 1, 2009, is available with several options. Instructions for the form builder will guide an institution to select the version of the model form that fits its practices, such as whether the institution provides an opt-out for consumers.

To obtain a legal "safe harbor" and to satisfy GLBA disclosure requirements, institutions must follow the instructions in the model form regulation when using the Online Form Builder.

The model privacy form was developed jointly by the Board of Governors of the Federal Reserve System, Commodity Futures Trading Commission, Federal Deposit Insurance Corporation, Federal Trade Commission, National Credit Union Administration, Office of the Comptroller of the Currency, Office of Thrift Supervision, and Securities and Exchange Commission.

A press release from the CFTC can be found here.
The Online Form Builder can be found here.

CFTC

Chicago Mercantile Exchange Introduces Mandatory Globex Credit Controls

The Chicago Mercantile Exchange (CME) has announced that use by its clearing members of CME's enhanced Globex Credit Control functionality (GC^2) will become mandatory for clearing members on a phased schedule between June 25 and August 6.

GC^2 is a risk-management tool that allows clearing firms to establish limits on the accumulation of daily exposure on CME Globex for each of a clearing firm's Globex execution firms, and requires a clearing firm to register one or more risk administrators with the CME. The primary responsibilities of risk administrators are to establish and maintain credit limits in GC^2 for each of the clearing firm's Globex execution firms, and to maintain "notification thresholds" associated with the credit limits in place for each Globex execution firm.

Clearing firms will be required to register at least one risk administrator with the CME and enter values for the Globex's automated credit controls in CME GC^2 for each of its Globex execution firms by no later than a date between June 25 and August 6 based on the clearing firm's CME Active Clearing Firm Number.

The CME Advisory Notice can be found here.
More detail on CME Globex's credit controls can be found here.

REMINDER: New Quarterly Reporting Requirement for CPOs in Effect; First Reports Due May 17

As previously reported in the March 19 edition of *Corporate and Financial Weekly Digest*, National Futures Association (NFA) Compliance Rule 2-46 became effective on March 31. This rule requires registered commodity pool operators (CPOs), including CPOs that have claimed an exemption pursuant to Commodity Futures Trading Commission Rule 4.7, to file with NFA quarterly reports setting forth specified information. The reports are due within 45 days after the end of each calendar quarter and must include (1) the identity of the pool's administrator, carrying broker(s), trading manager(s) and custodians; (2) a statement of changes in the pool's net asset value over the quarter; (3) monthly performance information for the quarter; and (4) a schedule identifying any investments exceeding 10% of the pool's net asset value as of the end of the quarter. The new reporting requirements do not apply to persons operating pursuant to an exemption from registration under CFTC Rule 4.13.

The first quarterly reports under this new rule will be due by May 17 and must be filed electronically through NFA's EasyFile system.

The NFA Notice to Members regarding the new rule is available here.

LITIGATION

Third Circuit Rejects Novel Government Securities Fraud Theory

The U.S. Court of Appeals for the Third Circuit affirmed the lower court's dismissal of certain novel theories on which the government predicated a criminal indictment against two high-ranking executives of a pharmaceutical company.

The government indicted the executives for allegedly orchestrating a massive securities fraud in violation of 15 U.S.C. Section 78j(b) and Securities and Exchange Commission Rule 10b-5, among other charges. The company's primary sales and distribution channel for its products was through wholesalers which, in turn, supplied pharmacies, hospitals and other health care providers. Wholesalers purchased product and maintained inventory based on projected demand. The government asserted that the company entered into arrangements with the wholesalers to maintain inventory in excess of projected demand to increase short-term sales and earnings and inflate the stock price, and contended that the executives concealed this practice from its shareholders.

In order to hold the first of the two executives liable, the government proposed a theory that one executive had a fiduciary duty to rectify the alleged misstatements of the other made during analyst calls and in subsequent SEC filings. The court noted that silence is not fraudulent or misleading under the securities laws unless there is a duty to disclose, which is only the case in the certain enumerated and specific circumstances. The government argued that liability for an omitted statement could be based on a general fiduciary obligation of high corporate executives to the company's shareholders, which compels a corrective statement in light of a misstatement by another. The

court rejected this theory as overbroad and unnecessarily expansive and further found that the theory encroached on conduct typically left to state law. (*U.S. v. Schiff*, Nos. 08-1903, 08-1909, 2010 WL 1338141 (3d Cir. Apr. 7, 2010))

Failure to Disclose Merger Talks Does Not Violate Securities Laws

The U.S. Court of Appeals for the Second Circuit upheld a district court's dismissal of a civil securities lawsuit, rejecting plaintiff's claims that the corporate defendant violated Sections 10(b) and 20(a) of the securities laws by failing to disclose that it was engaged in merger negotiations in a series of public statements.

The court relied on the principle that a public corporation is not required to disclose a fact merely because a reasonable investor "would very much like to know that fact." Although a corporation may have an express duty to disclose a merger agreement, disclosure of merger negotiations are not governed by the same standard. Further, although plaintiff generally identified seven public statements that were rendered misleading by omitting the fact of the merger negotiations, plaintiff did not satisfactorily identify any part of the statements that were rendered specifically misleading by virtue of the defendant's failure to disclose its negotiations. As a result the Second Circuit affirmed the lower court's dismissal of plaintiff's claims. (*Thesling and Johnson v. Bioenvision, Inc.*, No. 09 Civ. 3487, 2010 WL 1337699 (2d Cir. Apr. 7, 2010))

BANKING

Transaction Account Guarantee Program Is Extended by FDIC

On April 13, the Federal Deposit Insurance Corporation (FDIC) published an interim final rule extending the Transaction Account Guarantee (TAG) program through December 31, 2010, with the possibility of extending the program for an additional 12 months without further rulemaking if the FDIC determines that continuing economic difficulties warrant such an extension. The TAG program is a part of the Temporary Liquidity Guarantee Program adopted by the FDIC in October 2008 and provides full FDIC protection for the entire amount in all noninterest bearing transaction accounts. Without such protection, these accounts would only be insured up to $250,000 under the FDIC's general deposit insurance rules.

Insured depository institutions currently participating in the program that do not wish to participate in the extension must notify the FDIC of their intention to opt out on or before April 30. Such election will be effective on July 1. If an insured depository institution currently participating in the TAG program participates in the extension, it will be obligated to participate in the additional 12-month extension if the TAG program is further extended.

In addition, the rule states that the total dollar amount of TAG-qualifying accounts and the total number of accounts must be reported as an average daily balance beginning with the September 30 report date for the Report of Condition or Thrift Financial Report (covering the period from July 1 through September 30).

For more information, click here.

UK DEVELOPMENTS

Financial Services Act 2010 Passed

The Financial Services Act 2010 received Royal Assent on April 8. The Act has made a number of changes to certain objectives, powers and duties of the UK Financial Services Authority (FSA).

These include:

- Financial stability—The new financial stability objective for the FSA includes a duty for the FSA to determine and review its financial stability strategy, in consultation with the Treasury.
- Consumer education—The FSA is required to establish a new consumer financial education body. When this body becomes operational, it will take over the FSA's current responsibilities in relation to financial education.
- Enforcement powers—Key changes include the power to suspend individuals, and firms, along with the ability to fine those who are carrying out a role that needs FSA approval without the necessary approval being in place. The time limit to issue a warning notice against an individual in relation to misconduct increases from two years to three years from the time the FSA first becomes aware of it.
- Remuneration—The FSA will have the power to specify that remuneration agreements in breach of its remuneration rules are void.

- Consumer redress scheme—The FSA is given the power to introduce a consumer redress scheme. It will come into effect only by order of the Treasury.

Some of the new powers require the FSA to make rules or publish statements of policy. The FSA has stated that it will publish a consultation paper "in due course" concerning implementation of the provisions in the Act. Generally, the Act's changes were anticipated in the FSA's Business Plan for 2010-2011, published in March.

Read more.

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