

CORPORATE & FINANCIAL

WEEKLY DIGEST

12/21/12

Due to the holiday, *Corporate and Financial Weekly Digest* will not be published on December 28. The next issue will be distributed on January 4.

SEC/CORPORATE

Nallengara to Replace Cross as Corp. Fin. Chief

On December 17, Securities and Exchange Commission Chairman Elisse Walter named Lona Nallengara as Acting Director of the Division of Corporation Finance to replace Meredith Cross, who has announced that she will leave the SEC at the end of this year. Mr. Nallengara served as Deputy Director for Legal and Regulatory Policy of Corp. Fin. since March 20, 2011, and was responsible for overseeing the Division's Offices of Chief Counsel, Enforcement Liaison, International Corporate Finance, Mergers and Acquisitions and Small Business Policy. Mr. Nallengara joined the SEC from Shearman & Sterling where he was a partner in the Capital Markets Group.

[Read more.](#)

BROKER DEALER

FINRA Rule Relating to Private Placements of Securities Effective December 3

In the September 14, 2012, edition of [Corporate and Financial Weekly Digest](#), the firm published a summary of the Financial Industry Regulatory Authority's Rule 5123 regarding private placement of securities. Rule 5123 became effective on December 3, and it applies prospectively to private placements that began selling efforts on or after that date. In addition, member firms that file offering documents pursuant to FINRA Rule 5122 and FINRA Rule 5123 must use FINRA's new private placement filing system on FINRA's Firm Gateway system.

Additional Guidance on FINRA's Suitability Rule

In May 2012, the Financial Industry Regulatory Authority provided guidance on Rule 2111 (Suitability) by providing answers to frequently asked questions (FAQs). Answers that supersede some of these FAQs and additional FAQs have been addressed in FINRA Regulatory Notice 12-55. The new material addresses the scope of the terms "customer" and "investment strategy."

Specifically, the following questions have new answers:

- What constitutes a "customer" for purposes of the suitability rule?
- The new suitability rule requires that a recommended investment strategy involving security or securities must be suitable. Can you provide some examples of what would and would not be considered an "investment strategy" under the rule?

- Does the new rule’s “investment strategy” language cover a registered representative’s recommendation involving both a security and a non-security investment?

In addition, the following are new FAQs:

- Does the suitability rule apply when a broker-dealer or registered representative makes a recommendation to a potential investor?
- What are a broker-dealer’s supervisory responsibilities for a registered representative’s recommendation of an investment strategy involving both a security and a non-security investment?

Regulatory Notice 12-55 also notes that FINRA has created a suitability web page that locates in one place questions and answers regarding FINRA Rule 2111.

Click [here](#) for Regulatory Notice 12-55. Click [here](#) for FINRA’s suitability web page.

No-Action Relief Granted with Respect to Classification of Certain Persons as Owners of Broker-Dealers for Purposes of the Net Capital and Customer Protection Rules

On December 10, 2012, the Securities and Exchange Commission granted no-action relief in a situation in which a broker-dealer classifies: (1) a person (in one or more classes of ownership of the broker-dealer) as an owner of the firm (and not as a customer) for purposes of SEC Rule 15c3-3 (also known as the Customer Protection Rule) and (2) such person’s contributions in the firm as equity capital for purposes of SEC Rule 15c3-1 (also known as the Net Capital Rule). This situation applies, for example, where owners of a proprietary trading firm trade their own capital through the firm. The No-Action letter provides guidance that such classifications are permissible as long as the following conditions are met:

- 1 The broker-dealer obtains an opinion of independent legal counsel that: (a) it is duly formed, validly existing and in good standing; and (b) its governing documents are enforceable in accordance with their terms, each in the jurisdiction in which the broker-dealer was formed, organized or incorporated.
- 2 Upon request by the SEC or the Financial Industry Regulatory Authority, the broker-dealer must be able to establish that the person is an equity participant in the firm under applicable law in the jurisdiction in which the broker-dealer was formed, organized or incorporated.
- 3 The relationship between the person and the broker-dealer, and all applicable conditions of the arrangement, must be documented in an executed agreement wherein the parties agree and acknowledge certain conditions noted in the No-Action letter.
- 4 The person annually thereafter reaffirms in writing his/her understanding of, and agreement with, the terms and conditions of the executed agreement.
- 5 The broker-dealer ensures that the person is appropriately registered with the designated examining authority for any activity performed by the person for which registration is required. If the person is not a natural person, each person authorized to perform any activity for which registration is required on behalf of that person must be so registered. Further, the broker-dealer has implemented a system of supervisory compliance and controls that apply to such activities of the person and all others authorized to perform such activities on behalf of that person.

Click [here](#) for the No-Action letter.

No-Action Letter Regarding Definition of “Ready Market” with Regard to Foreign Equity Securities Pursuant to SEC Rule 15c3-1(c)(11)(i)

Currently, under Securities and Exchange Commission Rule 15c3-1 (the Net Capital Rule), broker-dealers may treat equity securities of a foreign issuer that are listed on the FTSE World Index as having a ready market. A ready market is relevant because the Net Capital Rule requires a broker-dealer to deduct 100% of the carrying

value of securities it holds in its proprietary account for which there is no ready market. See SEC Rule 15c3-1(c)(2)(vii). Because its members were interested in expanding the criteria for recognizing foreign equity securities as having a ready market, FINRA requested no-action relief from the SEC to treat certain additional foreign equity securities as having a ready market under paragraph (c)(11) of the Net Capital Rule.

The SEC granted no-action relief on November 28, stating that it would not recommend enforcement action if a broker-dealer treats an equity security of a foreign issuer as having a ready market under paragraph (c)(11) of the Net Capital Rule (and subject to the haircuts under paragraph (c)(2)(vi)(J)), if the following conditions are met:

- 1 The security is listed for trading on a foreign securities exchange located within a country that is recognized on the FTSE World Index, when the security has been trading on that exchange for at least the previous 90 days;
- 2 Daily quotations for both bid and ask or last sale prices for the security provided by the foreign securities exchange on which the security is traded are continuously available to broker-dealers in the United States through an electronic quotation system;
- 3 The median daily trading volume (calculated over the preceding 20-business-day period) of the foreign equity security on the foreign securities exchange on which the security is traded is either at least 100,000 shares or \$500,000; and
- 4 The aggregate unrestricted market capitalization in shares of such security exceeds \$500 million over each of the preceding 10 business days.

Additionally, any foreign equity security that ceases to meet one or more of the eligibility requirements will continue to be considered to have a “ready market” for purposes of paragraph (c)(11) for five business days from the date such foreign equity security ceases to meet the requirements. After the end of the five-business-day period, the security will be considered to have a “ready market” only if and when it again meets all of the eligibility requirements.

Click [here](#) for the No-Action letter.

SEC Issues Exemptive Order in Connection with Portfolio Margining of Cleared Swaps and Security-Based Swaps

Provisions of the Securities Exchange Act of 1934 (Exchange Act) and the Commodity Exchange Act (CEA) preclude market participants from portfolio margining collateral and other property that is required by the Exchange Act and the CEA to be held in accounts for securities and commodity customers, respectively. The Dodd-Frank Wall Street Reform and Consumer Protection Act amended the Exchange Act and the CEA to facilitate the use of portfolio margining. In general, the Dodd-Frank Act instructs the Securities and Exchange Commission and the Commodity Futures Trading Commission to issue rules or exemptive orders as necessary to permit customers that hold qualifying positions at a firm that is registered as a broker-dealer (BD) and futures commission merchant (FCM) to choose whether such positions will be carried in a futures account or a securities account, similar to the treatment afforded customers that engage in single stock futures transactions. The Dodd-Frank Act further provides that a person that holds portfolio margin positions in a securities account at a joint BD/FCM should receive the benefit of the protections that are available to customers under the Securities Investor Protection Act of 1970, and directs the CFTC to ensure that portfolio margin positions held in a futures account are subject to the same customer protection regime that applies to futures contracts.

The SEC has now issued an order granting conditional exemptive relief from compliance with certain provisions of the Exchange Act in order to facilitate portfolio margining treatment for customer-related positions in cleared credit default swaps (CDS). In particular, the SEC order permits cleared broad-based index CDS (which are swaps under the CEA) and cleared single name and narrow-based index CDS (which are security-based swaps under the Exchange Act) to be held in segregated accounts established and maintained in accordance with Section 4d(f) of the CEA.

The SEC order conditionally exempts dually registered securities clearing agencies/derivatives clearing organizations (clearing agencies/DCOs) from relevant provisions of the Exchange Act and SEC rules thereunder. The clearing agency/DCO exemption is subject to five conditions, including a requirement that the clearing

agency/DCO take steps to obtain relief from the CFTC. The order notes the SEC's anticipation that the CFTC will consider appropriate regulatory action to facilitate portfolio margining.

The SEC order conditionally exempts BDs/FCMs that elect to commingle and portfolio margin customer positions in CDS in customer accounts maintained in accordance with Section 4d(f) of the CEA. The BD/FCM exemption is subject to six conditions which, in part, seek to preserve customers' ability to select between the segregation requirements and customer protections afforded a securities account under the Exchange Act versus those afforded a swap account under the CEA.

The SEC order is effective on December 19, 2012. The SEC has requested comment on all aspects of the exemptions. Comments must be received on or before February 19, 2013.

Click [here](#) for the Exemptive Order.

CFTC

CFTC Extends Compliance Dates for Certain Swap Dealer and Major Swap Participant Requirements

The Commodity Futures Trading Commission has issued interim final rules extending the effective dates for certain business conduct and documentation requirements for swap dealers (SDs) and major swap participants (MSPs). Specifically, the CFTC deferred the compliance dates for provisions in Part 23 relating to general records and documentation requirements, including user exemption documentation requirements, until May 1, 2013. In addition, the CFTC deferred the compliance dates for Part 23 provisions relating to portfolio reconciliation and swap trading relationship documentation until July 1, 2013.

The CFTC interim final rule is available [here](#).

CFTC Issues No-Action Letters Relating to Swaps

Commodity Futures Trading Commission Staff have released several no-action letters relating to various requirements associated with swap trading, including swap dealer (SD) reporting requirements, SD chief compliance officer (CCO) annual reports, swap data recordkeeping and reporting requirements, mandatory clearing requirements and *de minimis* calculations for participants on the Japan Securities Clearing Corporation (JSCC) and Natural Gas Exchange (NGX), and SD/major swap participant (MSP) pre-trade mid-market mark reporting obligations.

- **SD Reporting Requirements.** In CFTC Letter No. 12-51, the CFTC's Division of Market Oversight (DMO) issued no-action relief from certain SD reporting requirements. Pursuant to the letter, non-clearing member SDs will not be required to comply with the daily large swap trader reporting requirements in CFTC Regulation 20.4 until March 1, 2013. Furthermore, SDs that are not bank holding company affiliates, futures commission merchants (FCM), FCM affiliates, broker-dealers or broker-dealer affiliates are permitted to wait until September 1, 2013, to submit Section 20.4 reports. In order to rely on the relief provided under this letter, an entity must submit a notice by e-mail to the DMO no later than the date the entity applies for registration as an SD. CFTC Letter No. 12-51 is available [here](#).
- **Annual Reports by SD Chief Compliance Officers.** Pursuant to CFTC Letter No. 12-52, the CFTC's Division of Swap Dealer and Intermediary Oversight (DSIO) granted no-action relief to certain SDs and SD CCOs from the annual report filing requirement for the fiscal year ending on December 31, 2012. In order to qualify for such relief, the SD must (i) be required to register by December 31, 2012; (ii) be regulated by a US prudential regulator or the Securities and Exchange Commission; and (iii) have a fiscal year-end of December 31. CFTC Letter No. 12-52 is available [here](#).
- **Swap Data Recordkeeping and Reporting Requirements.** In three separate no-action letters, DMO issued relief from certain swap data recordkeeping and reporting requirements. In CFTC Letter No. 12-50, DMO issued time-limited no-action relief from the timing

requirements for the reporting data relating to allocated swap transactions set forth in CFTC Regulation 45.3(e)(ii). The no-action letter acknowledges global time zone and legal holiday differences and provides extended post-allocation reporting deadlines for agents reporting cross-jurisdiction allocation swaps. CFTC Letter No. 12-50 is available [here](#).

In CFTC Letter No. 12-53, subject to specific criteria, DMO issued time-limited, no-action relief from Parts 43 and 45 for swap dealers entering into agreements that allow the allocation of swap reporting responsibilities between prime brokers and executing dealers in prime brokerage transactions. In addition, subject to certain conditions, the no-action relief extends to prime brokers' reporting of unique swap identifiers for such prime brokerage transactions. CFTC Letter No. 12-53 is available [here](#).

In CFTC Letter No. 12-55, DMO issued a no-action letter providing time-limited relief to SDs and MSPs from the obligation to report valuation data for cleared swaps to a swap data repository pursuant to CFTC Regulation 45.4(b)(2)(ii). The no-action relief applies to: SDs and MSPs that are reporting counterparties for which the SD or MSP has the obligation to report valuation data under Regulation 45.4(b)(2)(ii). CFTC Letter No. 12-55 is available [here](#).

The no-action relief provided by CFTC Letters 12-50, 12-53 and 12-55 expires on June 30, 2013.

- **Relief for Japan Securities Clearing Corporation and Natural Gas Exchange Participants.** In two separate no-action letters, the CFTC's Division of Clearing and Risk (DCR) and DSIO provided relief to JSCC and to certain JSCC and NGX participants. In CFTC Letter No. 12-56, DCR issued relief to JSCC from derivatives clearing organization (DCO) registration requirements. In addition, qualified JSCC clearing participants are exempt from the requirement to clear certain credit default swaps (CDS) and yen-denominated interest rate swaps through a registered DCO. Such relief is available until the earlier of December 31, 2013, or the date on which JSCC registers as a DCO with respect to its interest rate swap clearing. CFTC Letter No. 12-56 is available [here](#).

In CFTC Letter No. 12-57, DSIO indicated that a person trading swaps executed on NGX will not be required to include such swaps for purposes of the SD *de minimis* exception under CFTC Regulation 1.3(ggg)(4). Such relief is available until the earlier of March 31, 2013, or the date in which NGX's registration application as a foreign board of trade is accepted or denied. CFTC Letter No. 12-57 is available [here](#).

- **Relief for SDs and MSPs from Certain Pre-Trade Mid-Market Mark Reporting Obligations.** Pursuant to CFTC Letter No. 12-58, DSIO granted relief to SDs and MSPs from pre-trade mid-market mark reporting obligations to a counterparty in a transaction involving certain CDS and interest rate swaps. Such relief is available until final CFTC regulations governing the registration of swap execution facilities (SEFs) have been issued, provided that real-time tradeable bid and offer prices are available for such swaps, and the counterparty agrees that the SD or MSP does not need to disclose the pre-trade mid-market mark. Such counterparty agreement must be in writing before the transaction occurs.

Upon issuance of the final SEF regulations, the relief provided in this letter will continue to be available for transactions in which the bid and offer prices for such transactions are available on a designated contract market or SEF, and the counterparty agrees in writing, before the transaction occurs, that the SD or MSP does not need to disclose the pre-trade mid-market mark. CFTC Letter No. 12-58 is available [here](#).

Exemption from NFA Assessment Fee for Proprietary Trading Firms that Register as CPOs

The National Futures Association (NFA) has issued a notice temporarily exempting certain proprietary trading firms that may be required to be registered as commodity pool operators (CPOs) as of December 31, 2012, from the assessment fees that CPOs are otherwise required to pay. NFA Bylaw 1301 generally exempts exchange members from paying assessment fees with respect to transactions effected on that exchange. However, the exemption does not apply to exchange members that are commodity pools operated by CPOs. Because the

Commodity Futures Trading Commission has rescinded exemptions from CPO registration effective December 31, 2012, the CFTC could view certain proprietary trading firms as commodity pools subject to CPO registration. NFA's Board of Directors will consider the application of the NFA assessment fee to such firms. Until the Board of Directors resolves the issue, any proprietary trading firm that becomes registered as a CPO will remain exempt from the assessment fee if its trading account was exempt from the NFA assessment fee as of December 31, 2012, until further notice from NFA.

NFA Notice I-12-33 is available [here](#).

INVESTMENT COMPANIES AND INVESTMENT ADVISERS

NFA Provides Bylaw 1101 Guidance to Commodity Pool Operators of Investment Companies

Under amended Commodity Futures Trading Commission Regulation 4.5, registered investment advisers (RIAs) to registered investment companies engaging in more than minimal commodity trading activities will be required to register as commodity pool operators (CPOs) and become members of the National Futures Association (NFA). NFA Bylaw 1101 requires that CPOs determine if any participants in their commodity pools are required to be registered with the NFA.

Until further notice, the NFA has determined that CPOs to investment companies will not be required to perform due diligence on pool participants (*i.e.*, fund shareholders) pursuant to NFA Bylaw 1101. These CPOs still need to fulfill their Bylaw 1101 obligations to ensure that any futures commissions merchant through which they transact commodity transactions and any sub-adviser to their investment company is properly registered in the appropriate capacity and is a member of the NFA, or is exempted from commodity trading adviser registration. The NFA is to provide additional guidance regarding due diligence obligations under NFA Bylaw 1101 that will eventually supersede the current interpretation of Bylaw 1101.

[Read more.](#)

SEC Charges Eight Mutual Fund Directors for Failure on Valuations

On December 10, the Securities and Exchange Commission announced charges against eight former member of the boards of directors overseeing five mutual funds for violating their asset pricing responsibilities under the federal securities laws. The funds are alleged to have overstated the values of portfolio securities during the housing market crisis in 2007.

The SEC alleges that the respective boards of directors, which delegated the responsibility for fair valuation of securities to a valuation committee, failed to provide meaningful substantive guidance on how fair valuation determinations should be made. Additionally, the SEC alleges that the directors failed to take meaningful efforts to learn how fair values were being determined and obtained insufficient information regarding how valuation committee determinations were made.

Investment company directors must adopt and implement meaningful fair valuation methodologies and procedures and maintain internal controls over financial reporting. Where such obligations are delegated to a valuation committee, directors must, at a minimum, "determine the method, understand the process and continuously evaluate the appropriateness of the [valuation] method used."

[Read more.](#)

LITIGATION

Head of SEC Enforcement Division's Asset Management Unit Addresses Hedge Fund Enforcement Priorities

Bruce Karpati, Chief of the Securities Exchange Commission Enforcement Division's Asset Management Unit (AMU), spoke before the Regulatory Compliance Association earlier this week to address the AMU's current

enforcement priorities. By way of background, the AMU is a specialized unit established by the Enforcement Division to focus on investment advisers, investment companies, hedge funds, mutual funds and private equity funds. The AMU employs industry professionals and experts (including fund managers, private equity analysts and due diligence professionals) to help identify and investigate emerging issues.

According to Mr. Karpati, “it is clear that even the sophisticated class of investors who invest in hedge funds are themselves unable to effectively monitor the industry.” This difficulty exists because, Mr. Karpati argued, the basic hedge fund business model creates incentives for potential abuse and misconduct, including that: (i) payment of both management and performance fees may cause managers to “overprioritize” compensation; (ii) managers are under pressure to show consistent or improving performance metrics; (iii) managers may seek to gain an informational edge that may result in improper insider trading; (iv) by controlling all aspects of the business, managers may be subject to conflicts of interest; and (v) competitive pressure may cause managers to give “favored treatment” to preferred investors.

Mr. Karpati emphasized his view that the hedge fund operating model may be in tension with the manager’s role as a fiduciary. He noted that “[a]s a fiduciary, a hedge fund manager must guard against conscious and unconscious incentives that might cause him or her to provide less than disinterested advice since an investment adviser may be faulted even when he or she does not intend to injure a client or even if a client does not suffer a monetary loss.” Mr. Karpati concluded that the anti-fraud provisions of the Investment Advisers Act enable the AMU to pursue “breaches of fiduciary duty and other forms of misconduct.”

In surveying recent cases, Mr. Karpati observed that, since 2010, the Enforcement Division has pursued over 100 cases against hedge fund managers, “a significant majority of which involved conflicts of interest, valuation, performance, and compliance and controls.” To identify potential cases, Mr. Karpati emphasized that the AMU is relying in part on new risk-analytic initiatives and data analyses, including the “Aberrational Performance Inquiry,” which looks for funds with suspicious or improbable performance returns. In addition, Mr. Karpati noted that the AMU is using its new methods with an eye toward “zombie funds,” which may be improperly delaying the liquidation of their holdings because the income from those assets is the manager’s only revenue source.

Mr. Karpati concluded his presentation by identifying “best practices” that fund managers might engage in to help fulfill their fiduciary obligations. According to Mr. Karpati, fund managers should: (i) set the “tone at the top and create a culture of compliance;” (ii) establish internal controls and checks and balances where employees have overlapping and potentially conflicting positions (e.g., a portfolio manager valuing the fund’s assets); (iii) check and monitor traders; (iv) periodically review and test compliance procedures; and (v) cooperate with exam staff and promptly implement any remedial measures identified during an examination.

Mr. Karpati’s speech is available [here](#).

District Court Rules that Individual LLC Member Is Third-Party Beneficiary and Bound by Arbitration Agreement

The US District Court for the Southern District of Florida confirmed that third-party beneficiaries of a contract containing an arbitration clause may be compelled to arbitrate their claims notwithstanding that the third-party beneficiary is not technically a party to the agreement.

Plaintiff Great Lakes Reinsurance brought claims in federal court, as subrogee for its policyholder, for negligence, gross negligence and bailment against Sunset Harbor Yacht Club, Inc. and Sunset Harbor Marina, Inc. The defendants moved to compel arbitration.

In 2009, David Trafton reported his boat stolen from the Marina and, following an insurance investigation, had his loss paid by Great Lakes. Trafton’s father, who originally purchased the boat and sold it to his son in 2006, had the boat docked at the Marina since 2003. David Trafton signed a dockage agreement at the Marina giving the Traftons temporary access to a slip for the boat until they could set up a membership with the Yacht Club and get a permanent slip. Consistent with the terms of the membership plan, the Traftons set up a limited liability company to purchase an equity membership in the Yacht Club. The company completed the purchase in 2003. Although David Trafton was a member of the company, only his father and his father’s wife signed the purchase agreement.

The parties did not dispute that the limited liability company was a member of the Yacht Club and bound by the Yacht Club’s Bylaws, which mandate that all disputes be decided by mediation, and, if necessary, arbitration. The

only dispute was over whether David Trafton, as an individual, was a member and thus bound by the arbitration provision of the bylaws.

Although David Trafton was not a signatory to the arbitration agreement, defendants contended that he was an intended third-party beneficiary of the company's membership. Plaintiff maintained that David Trafton was never an intended beneficiary and that his father was the "designated user" and therefore the intended beneficiary.

The court, applying Florida law, concluded that David Trafton was an intended beneficiary because he availed himself of the membership benefits whenever he chose. David Trafton testified that he was the member of the company who most frequented the Yacht Club and that he always had a means of entry to the private facility. The fact that he was arguably a step removed from the arbitration agreement did not mean, according to the court, that he should be able to enjoy the benefits of the company's membership without being bound by the arbitration agreement.

Great Lakes Reinsurance (UK) PLC v. Sunset Harbor Marina, Inc., No. 10-CV-24469 (S.D.Fla. Dec. 12, 2012).

EXECUTIVE COMPENSATION AND ERISA

Significant New Fees for Group Health Plans in 2014–2016

The Department of Health and Human Services (HHS) issued proposed regulations in the *Federal Register* on December 7 which provide guidance regarding the Transitional Reinsurance Program (the Program). The Program will be effective for three years: 2014–16. It will impose heavy fees upon employer-sponsored health care plans, whether insured or self-insured.

HHS estimates that the fee will be equal to \$63 per year for each person covered under an employer-sponsored health care plan (including dependents in addition to employees and retirees). However, the fee does not apply to retirees and dependents for whom Medicare is the primary payer. It is estimated that the fee will be reduced to \$42 per year in 2015 and \$24 per year in 2016. The rules for determining the number of persons covered under the plan are similar to the rules required for determining the number of covered lives for purposes of the Patient Centered Outcomes Research (PCOR) fee, which became effective in 2012, and is due to be paid on July 31, 2013, in the amount of \$1 per covered life. Those rules provide several alternative permissible methods of counting covered lives. (This subject is discussed in detail in the April 20, 2012, edition of [Corporate and Financial Weekly Digest](#).)

Insurance companies are responsible for paying the fees in the case of insured plans. In the case of self-insured plans, though the plan is liable, a third-party administrator or other third party may make the payments with respect to the plan. These entities will be required to submit enrollment information by November 15, 2014. HHS will notify the entities within a month thereafter of any contributions due, which must be paid within 30 days of the notification. The fee is generally applicable with regard to plans which provide major medical coverage and health reimbursement accounts, though a health reimbursement account that is integrated with a group health plan is excluded from the fee. Health savings accounts and flexible spending accounts are also excluded. Wellness programs and employee assistance programs that do not provide major medical coverage are also excluded, as are group health plans that provide only "excepted benefits."

The Program was enacted as part of the Patient Protection and Affordable Care Act. Its principal purpose is to collect \$20 billion to cover reinsurance payments to insurers in the individual market who are expected to have higher-cost enrollees. It is intended that this will stabilize premiums for coverage in the individual market. Reinsurance programs are to be established in every state, either by the State or by HHS in those states that do not do so. Presumably many people buying insurance through the exchanges are expected to have previously been uninsured and perhaps are bad risks, and/or unable to secure coverage through their employers (such as part-time or seasonal employees). This is expected to result in increased costs for insurers, at least a portion of which can be offset by payments from the Program.

The proposed regulations can be found [here](#).

EU DEVELOPMENTS

European Commission Adopts AIFMD Level 2 Regulation

On December 19, the European Commission adopted a Delegated (Level 2) Regulation (Delegated Regulation) implementing certain aspects of the Alternative Investment Fund Managers Directive (2011/61/EU) (AIFMD).

The Delegated Regulation contains rules supplementing the AIFMD in a number of key areas including:

- Conditions and procedure for the authorization of Alternative Investment Fund Managers (AIFMs);
- Calculation of leverage;
- Operating conditions for AIFMs, including rules on conflicts of interest, risk management, liquidity management, organizational requirements, valuation and delegation of AIFM functions;
- Depositary tasks and liabilities;
- Transparency requirements towards investors and regulators; and
- Cooperation agreements with third countries.

The Delegated Regulation is subject to a three-month scrutiny period by the European Parliament and the European Council of Ministers. Provided no objections are raised, the Delegated Regulation will enter into force 20 days after its publication in the *Official Journal of the European Union*, and will apply from July 22, 2013.

[Read more.](#)

European Commission Adopts EMIR Technical Standards on OTC Derivatives

On December 19, the European Commission adopted nine technical standards which clarify certain aspects of Regulation 648/2012 on OTC derivatives, central counterparties (CCPs) and trade repositories (generally known as the European Markets Infrastructure Regulation or EMIR). The technical standards provide clarity in regard to the European rules for the mandatory clearing and reporting of OTC derivatives transactions.

The technical standards that have been adopted relate to:

- Indirect clearing arrangements;
- The clearing obligation procedure;
- The public register;
- Access to a trading venue;
- Non-financial counterparties;
- Risk mitigation techniques for OTC derivatives contracts not cleared by a central counterparty (CCP);
- The specification of the provisions in legislation that relate to the requirements for CCPs;
- The capital, retained earnings and reserves of a CCP;
- The format of the records to be maintained by a CCP;

- The specification of the provisions in legislation that related to the minimum details of the data to be reported to trade repositories;
- The details of the application for registration as a trade repository;
- Data to be published and made available by trade repositories;
- Operational standards for aggregating, comparing and accessing the data published by trade repositories;
- The specification of the format and frequency of trade reports to trade repositories; and
- The format of applications for registration of trade repositories.

The standards will come into force 20 days after their publication in the *Official Journal of the European Union*. It is likely that this will be in early February 2013.

The proposed technical standard dealing with colleges of supervisors for CCPs has not been adopted. This will be redrafted by the European Securities and Markets Authority for adoption by the European Commission at a later stage.

[Read more.](#)

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

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
Kevin M. Foley	312.902.5372	kevin.foley@kattenlaw.com
Jack P. Governale	212.940.8525	jack.governale@kattenlaw.com
Arthur W. Hahn	312.902.5241	arthur.hahn@kattenlaw.com
Joseph Iskovitz	212.940.6351	joseph.iskovitz@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

EXECUTIVE COMPENSATION AND ERISA

Russell E. Greenblatt	312.902.5222	russell.greenblatt@kattenlaw.com
Christopher K. Buch	312.902.5509	christopher.buch@kattenlaw.com

EU DEVELOPMENTS

Edward Black	44.20.7776.7624	edward.black@kattenlaw.co.uk
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