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**FINANCIAL SERVICES REGULATORY REFORM UPDATE**

November 19<sup>th</sup>, 2010

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**SEC PROPOSES INVESTMENT-ADVISER OVERSIGHT RULES**

On November 19<sup>th</sup>, as part of its implementation of one of its Dodd-Frank mandates, by a 3-2 vote the SEC proposed new rules to strengthen the SEC's oversight of investment advisers. The new rules would:

1. Facilitate registration of advisers to hedge funds and other private funds with the SEC,
2. Implement the Dodd-Frank mandate requiring reporting by certain advisers that are exempt from SEC registration,
3. Increase the asset threshold for advisers to register with the SEC, and
4. Define "venture capital fund" and provide clarity regarding certain exemptions to investment adviser registration.

The full press release and more information are available [here](#).

**FED PROPOSES RULE ON VOLCKER COMPLIANCE EXTENSION**

Under Dodd-Frank, the Federal Reserve has the sole responsibility to determine the conformance period during which banks can act to reach full compliance with the Volcker rule. Dodd-Frank provides banking entities 2-years to reach this compliance, but the Fed may extend this period by up to three additional one-year periods, which banks must apply for by submitting a compliance plan to the Fed. On Wednesday, the Fed [proposed a rule](#) that would give bank two years to comply with the Volcker restrictions, once they are in place, on proprietary trading. The proposals would also allow the Fed to impose conditions on any compliance extensions, and would require non-banking entities that become banks in the future to comply with the Volcker rule within 2 years. Comments about the proposal are due within 45 days of the publication of the proposal in the Federal Register, which is anticipated soon.

**DEFICIT COMMISSION CO-CHAIRS MAKE CHANGES TO DRAFT PROPOSAL**

The co-chairs of the National Commission on Fiscal Responsibility and Reform, Erskine Bowles and Alan Simpson, will be making changes to their first draft, released on November 10<sup>th</sup>, in order to win support from the rest of the Commission before the two public meetings at the end of the month. Bowles noted they will *not* be diluting their proposal in order to win votes, but rather the end result will be an "honest approach" and "not milksop."

Senate Budget Committee Chairman Conrad (D-ND), also one of the commissioners, stated in the past that the final proposal should be comprehensive in nature, rather than piecemeal (which realistically would be easier to garner the necessary 14 votes). Many are still skeptical that the Commission will be able to reach an agreement – the initial reaction to the co-chairs’ proposal was not positive from Democrats or Republicans. Right now the plan is weighted towards spending cuts, but also would have federal revenues rising to the equivalent of 21% of the economy.

The Commission met three times this past week, behind closed doors, and discussed health care and Social Security, among other things. Commissioners Alice Rivlin and Rep Ryan (R-WI) proposed turning Medicare into a “premium support” program that would give recipients the option of buying private insurance. Although the measure would effectively cut costs, it was not received well by many commissioners.

#### SEC CHAIR MEETS WITH UK COUNTERPARTS – AS CONCERNS ABOUT THE GLOBAL HARMONIZATION ABOUT FINANCIAL REGULATORY REFORM CONTINUE TO GROW

On Monday, SEC Chair Schapiro met separately with UK Financial Services Authority (FSA) Chair Adair Turner and UK Financial Reporting Council (FRC) Chair Stephen Haddrill to share the two countries’ views on regulatory reform and other financial matters of common concern. All agencies stated their commitment to working together, particularly regarding regulated, multi-national firms with a presence in the U.S. and UK. Schapiro specifically talked with Turner about OTC derivatives trading, high-frequency trading and the “flash crash,” credit rating agencies and cross-border enforcement sharing between the SEC and FSA. She spoke with Haddrill about reg reform efforts in the U.S. and EU, as well as oversight of cross-border audit firms, issuer disclosure rules and investor access to corporate proxy rules.

#### SEC’S PROPOSED ABS REGULATIONS DRAW FIRE

On Monday, 14 groups representing municipal securities issuers, broker-dealers and financial advisers sent a [joint comment letter](#) to the SEC, arguing that the SEC’s proposals on regulating the ABS market use too broad a definition for ABS. The groups, which included the Securities Industry and Financial Markets Association and the Bond Dealers of America, stated that most municipal securities are not securitized, and the intent of Dodd-Frank was only to reform the market for securities collateralized by loans.

The proposals in question would have ABS issuers review the assets underlying the security being issued, and disclose the findings of that review in the security’s registration statement. ABS issuers and underwriters would also have to disclose the findings of any third-party due diligence report.

On the opposite end of the spectrum, Sen. Levin (D-MI) submitted his own [comment letter](#) to the SEC, in which he argued that the SEC proposals actually fall short of congressional intent behind the relevant Dodd-Frank sections. He asked the SEC to specify review standards for ABS issuers, and added that the Dodd-Frank provision was intended to allow investors to have access to material information about assets underlying asset-backed securities.

#### SEC/TREASURY PERSONNEL CHANGES

SEC Chair Mary Schapiro named Jennifer B. McHugh as Acting Director of the Division of Investment Management today, to replace outgoing Director Andrew “Buddy” Donahue. McHugh was previously a

senior advisor in the Office of the Chairman and will hold the position until a new Director is named. Please find the press release [here](#). Around the same time, Henry T. C. Hu, the inaugural Director of the Division of Risk, Strategy, and Financial Innovation (which was created in 2009), announced that he will be leaving his position at the SEC to return to the University of Texas in January. Please find the press release [here](#).

Meanwhile at the Treasury, Kim Wallace, the top legislative affairs official there, brought on two new deputies this week: Charles Yi from Sen. Dodd's Banking Committee staff, and Kathleen Mellody from Rep. Kanjorski's House Financial Services Committee staff. Both new deputies are known for their bipartisan working relationships, and are expected to have a busy start to their new jobs.

#### TREASURY'S WOLIN SPEAKS AT LONDON STOCK EXCHANGE

*Wolin speaks about Dodd-Frank at London Stock Exchange.* On Wednesday, Deputy Treasury Secretary Neil Wolin spoke before the London Stock Exchange about the need for the U.S. and EU to join forces in overseeing derivatives oversight. Dodd-Frank calls for derivatives to be reported to trade repositories and traded on standardized exchanges in most cases, and the U.S. wants to ensure that international firms won't "shop around" for less restrictive regulatory environments. Wolin endorsed the European Commission's proposals on a central clearinghouse for derivatives, but called on other countries to establish mechanisms for dismantling banks. He highlighted the importance of international coordination as a means of preventing future crises. His full speech is available [here](#).

#### FCIC REPORT ON FINANCIAL CRISIS CAUSES DELAYED

On Wednesday, the Financial Crisis Inquiry Commission voted 6-4 to delay publishing its final report on the causes of the financial crisis. The report will now be released on January 13, 2011. Originally, Congress has mandated that the FCIC complete its investigation by December 15, 2010, but the majority of the organization believes that this is not enough time, as they stated in a letter to President Obama and Congress after voting on the matter. The 4 minority voters (all Republican) stated that the FCIC should honor the statutory requirement and that the deadline can in fact be met. According to a FCIC spokesperson, the FCIC has completed most of its research on the financial crisis, but many "investigative items... still need to be pursued."

#### MSRB OPENS REGISTRATION SYSTEM FOR MUNICIPAL ADVISERS

Under Dodd-Frank, the Municipal Securities Rulemaking Board's authority was expanded to include municipal advisers – those who advise state and local governments on municipal bonds and other investment-related matters, and who solicit municipal bond business on behalf of others. On Monday, the MSRB [announced](#) the opening of its registration system for municipal advisers, who must now register first with the SEC and then with the MSRB.

#### REPUBLICANS RESPOND TO FEDERAL RESERVE ACTIONS

In response to the Fed's recent announcement to inject \$600 billion into the economy, two Republicans – Rep. Pense (R-IN) and Sen. Corker (R-TN) - are proposing or considering legislation that would dramatically change the mission of the Federal Reserve. The current "dual mandate" of the Fed, developed by Congress in 1977, requires the Fed to develop monetary policy with the goals of promoting

price stability and maximum employment. Pense's bill would only have the Fed ensure a low, stable rate of inflation, thereby leaving job growth policy to Congress and the administration. Corker is coming from a slightly different perspective, and hasn't introduced a bill yet – he stated that it would likely take 3-5 years to determine accurately whether the Fed made the right decision.

#### DODD ASKS FSOC TO WEIGH IN ON FORECLOSURE “ROBO-SIGNING”

At Tuesday's Senate Banking Committee hearing on the foreclosure documentation problems, Chairman Dodd (D-CT) asked the Financial Stability Oversight Council to weigh in on the mortgage documentation problems, or “robo-signing” that occurred last month. Specifically, he asked the FSOC to “drill down and find out the scope of the problem and determine the steps that need to be taken to prevent systemic problems, if they conclude that there are systemic implications.” Dodd was skeptical of the Congressional Oversight Panel report that found foreclosure paperwork errors to be no threat to the overall financial system, and also criticized the financial services industry for labeling the problems as merely “technical.”

#### FINANCIAL STABILITY BOARD MAKES “TOO BIG TO FAIL” PROPOSAL

Late last week, the Financial Stability Board (the group charged by the G-20 with addressing weaknesses in the financial system in light of the 2008 financial crisis) released its proposed framework to handle the “too big to fail” problem. (The proposal was finalized on October 20<sup>th</sup>, but only released last week). Notably, the framework calls on national authorities to require systemically important financial institutions (SIFIs) to “have higher loss absorbency capacity to reflect the greater risks that these institutions pose to the global financial system.” The proposal also asks national authorities to adopt measures that would enable SIFIs to be wound up “without disruption to the financial system and without taxpayer support.” The full proposed framework is available [here](#).

#### PRACTICING LAW INSTITUTE DISCUSSES SAY-ON-PAY

Last week, the Practicing Law Institute held a panel on shareholder-director relations and voting. One of the panelists, the executive director of the Council of Institutional Investors (Ann Yerger), stated that institutional investors will be very focused on executive compensation in the upcoming proxy season, and are starting to look at how they will handle the new say-on-pay voting power. Because the frequency of say-on-pay votes has not yet been determined, Yerger believes this will be a divisive point – some investors want an annual vote, while many companies want the vote to be every three years. Another panelist, a partner at Edwards Angell Palmer and Dodge, believes that many companies will end up with a one-year say-on-pay vote “so as to communicate with their shareholders.”

#### UPCOMING HEARINGS

*The Senate and House of Representatives will be in Thanksgiving recess during the week of November 22<sup>nd</sup>, and will return for a second lame duck session on Monday, November 29<sup>th</sup>. It is still undetermined how many weeks the second session of the lame duck will last.*