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SEC/CORPORATE

OTC Markets Proposes Amendments to OTCQX Rules and New Rules for US Banks

On February 13, OTC Markets Group (OTC) proposed amendments to the OTCQX Rules for both US and international companies. The OTCQX is the highest market tier for over-the-counter trading on the OTC Markets. These proposed amendments include changes to, among other things, the roles market professionals designated by OTCQX companies are required to serve for such companies, initial eligibility standards and requirements as to the dissemination of material information. The OTC will be accepting comments on the proposed amendments through March 16, 2014. The proposed amendments will become effective on March 17, 2014 (other than the amendment regarding disclosure of material information, which will become effective on May 17, 2014).

To read the full text of the proposed amendments to the OTCQX Rules for US companies, click here.

To read the full text of the proposed amendments to the OTCQX Rules for international companies, click here.

Also on February 13, the OTC announced the publication of a new set of OTCQX Rules for US banks in connection with a new OTCQX banks marketplace that the OTC plans to launch in spring 2014. These rules establish the application, eligibility, disclosure and continued qualification requirements for US banks admitted to the OTCQX.

To read the full text of the OTCQX Rules for US banks, click here.

BROKER DEALER

SEC Approves Changes to FINRA BrokerCheck Disclosure Rule 8312

The Securities and Exchange Commission approved two changes to Financial Industry Regulatory Authority Rule 8312 relating to FINRA BrokerCheck Disclosure (BrokerCheck Rule). The first change to the BrokerCheck Rule requires FINRA's BrokerCheck system to make publicly available on a permanent basis information about former associated persons of a FINRA member firm who were registered on or after August 16, 1999, if such persons were the subject of an investment-related civil action brought by a state or foreign financial regulatory authority that was dismissed pursuant to a settlement agreement. The second change to the BrokerCheck Rule expands the breadth of the information included in FINRA's BrokerCheck system by including information about current or former FINRA member firms or current or former members of any registered national securities exchange that uses FINRA's Central Registration Depository for registration purposes (collectively, BrokerCheck Firms) and each of such BrokerCheck Firms' current or former associated persons. Both amendments to the BrokerCheck Rule become effective on June 23.

FINRA Regulatory Notice 14-08 is available here.

INVESTMENT COMPANIES AND INVESTMENT ADVISERS

SEC to Examine Never-Before Examined Registered Investment Advisers

The Securities and Exchange Commission's Office of Compliance Inspections and Examinations (OCIE) announced that it is launching an initiative, as part of its existing National Exam Program, to examine investment advisers who have never-before been examined and who have been registered for three or more years (the Target Firms). The SEC press release on this initiative stated, "[a]s part of the initiative, OCIE will conduct examinations of a significant percentage of advisers that have not been examined since they registered with the SEC." A letter directed at the target firms of this new initiative (Initiative Letter) outlines two distinct approaches that the SEC may take with respect to an exam of a Target Firm. The first approach is a "risk-assessment" approach, which is designed to allow OCIE to obtain a better understanding of the Target Firm. An exam under this approach may include a high-level overview of a Target Firm's overall business activities with particular focus on the Target Firm's compliance program and other documents essential to assess the representations in the Target Firm's disclosure documents. The second approach is a "focused review." Under this approach, the OCIE may conduct a comprehensive, risk-based examination of one or more of the following higher-risk areas of a Target Firm's business and operations: compliance program, filings/disclosure, marketing, portfolio management and safety of client assets.

This initiative does not cover investment advisers to private funds, as such advisers are subject to the "Presence Exam" initiative that was launched in October 2012. Additionally, OCIE notes in the Initiative Letter that the fact that an adviser receives the letter from OCIE does not necessarily mean that it will be examined.

The Initiative Letter is available here.

LITIGATION

DC Circuit Upholds Ruling That IRS Cannot Regulate Tax-return Preparers

The US Court of Appeals for the District of Columbia Circuit recently held that the Internal Revenue Service did not have the statutory authority to regulate tax-return preparers.

In 2011, the IRS issued new regulations that, among other things, required paid tax-return preparers to pass a certification exam, pay annual fees and complete fifteen hours of continuing education each year. The IRS relied on 31 USC § 330 as its authority for the new regulations, which authorizes the IRS to "regulate the practice of representatives of persons before the Department of the Treasury." The District Court ruled against the IRS and in favor of three independent tax-return preparers who challenged the new regulations as exceeding the agency's authority. The IRS appealed.

The court of appeals held that the regulation exceeded the IRS's statutory authority. Among other reasons, the court found that tax-return preparers did not "represent" the taxpayer before the Treasury because the tax-return preparers do not act as agents with legal authority to act on behalf of their clients. Further, the court found that tax-return preparers do not "practice before the Treasury," which describes an appearance in an adversarial or adjudicative process, not merely the preparation of tax returns. Accordingly, the court of appeals affirmed, enjoining the enforcement of these regulations.

Loving v. Internal Revenue Service, et al., No. 13-5061 (D.C. Cir. Feb. 11, 2014).

Federal Reserve Approves Final Rule Regulating Bank Holding Companies and Foreign Banking Organizations

On February 18, the Federal Reserve Board (Federal Reserve) approved a Final Rule to enhance supervision over the largest US bank holding companies (BHCs) and the largest foreign banking organizations (FBOs) with operations in the United States. The Final Rule was adopted pursuant to Section 165 of the Dodd-Frank Wall Street Reform and Consumer Protection Act. The Final Rule applies primarily to BHCs with $50 billion or more in total assets (Large BHCs), but it also creates some requirements for certain BHCs with total assets from $10 billion to $50 billion.

Federal Reserve Chair Janet Yellen stated that the Final Rule addressed the destabilizing effect on the financial system and economy caused by the failure of large financial institutions. Although nonbank financial companies designated for oversight by the Financial Stability Oversight Council are not subject to the Final Rule, the Federal Reserve stated that it would implement rules for such entities at a later date.

Under the Final Rule, a US Large BHC will be subject to capital planning and stress testing requirements previously issued under the Dodd-Frank Act. A Large BHC must also comply with enhanced risk-management and liquidity standards, conduct liquidity stress tests and hold a buffer of highly liquid assets based on projected funding needs during a 30-day stress event. Any publicly traded US BHC with $10 billion or more in total assets is also required to establish an enterprise-wide risk committee.

The Final Rule also covers an FBO with a US presence. An FBO with $50 billion or more of US non-branch assets (i.e., the sum of the consolidated assets of each top-tier US subsidiary of the foreign banking organization) must establish a US holding company, is subject to the same capital planning and stress testing requirements as a US BHC, and must also establish a US risk committee and hire a US chief risk officer. A publicly traded FBO with more than $10 billion in total assets must establish a US risk committee and conduct stress testing. An FBO with more than $50 billion in total assets but less than $50 billion in US assets is subject to additional capital, liquidity and risk-management requirements. The Federal Reserve estimates that the holding company requirement in the Final Rule will apply to 15-20 FBOs while the Final Rule will apply to approximately 100 foreign banks in the United States overall.

US BHCs must comply with the Final Rule by January 1, 2015. FBOs must submit their plans to comply with the rule by January 1, 2015, but they will have until July 1, 2016, to implement their plans.

The 415-page final rule can be found here.

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