Katten
Katten Muchin Rosenman LLP

CORPORATE & FINANCIAL
WEEKLY DIGEST

February 7, 2014 Volume IX, Issue 6

SEC/CORPORATE

SEC Division of Corporation Finance Issues Guidance on Rule 506(c) Private Placements

On January 23, the Securities and Exchange Commission's Division of Corporation Finance issued new Compliance and Disclosure Interpretations (C&DIs) with respect to Rule 506 exemptions from registration under the Securities Act of 1933. These C&DIs relate to the rules adopted by the SEC in September 2013 pursuant to Section 201(a) of the JOBS Act, which required the SEC to eliminate the prohibition on general solicitation as long as all investors are accredited investors and the issuer takes reasonable steps to verify that purchasers are accredited investors. The new C&DIs include the following interpretive guidance:

C&DI 260.33 clarifies that an issuer that commenced an offering before September 23, 2013 (the effective date of the new Rule 506(c) exemption), is not required to take reasonable steps to verify the accredited investor status of purchasers of securities in the offering before September 23, 2013. Once the issuer begins to make sales in reliance on Rule 506(c), it must take reasonable steps to verify that purchasers of securities in the offering are accredited investors. The issuer must also amend any previously filed Form D to reflect that it is relying on the Rule 506(c) exemption.

C&DI 260.34 provides that an issuer that commenced an offering before September 23, 2013, in reliance on what is now the Rule 506(b) exemption, may switch from the Rule 506(b) exemption to the Rule 506(c) exemption even if Rule 506(b) sales were made after September 23 and included non-accredited investors, provided that all securities thereafter sold in reliance on the Rule 506(c) exemption are sold only to accredited investors and the issuer takes reasonable steps to verify that such purchasers are accredited investors.

The guidance suggests there are reasonable grounds for allowing Rule 506(b) issuers that have an existing marketing ability and the ability to implement Rule 506(c) compliance procedures to switch to the Rule 506(c) exemption. The Rule 506(c) exemption applies to operating companies as well as private funds. Nevertheless, the relative rarity of Rule 506(c) offerings to date suggests that compliance experts have not yet updated compliance policies and procedures to deal with Rule 506(c) publicly solicited private placements or that the Rule 506(c) verification requirements are onerous.

BROKER DEALER

SEC Issues No-action Relief Regarding Registration of M&A Brokers

The Securities and Exchange Commission Division of Trading and Markets (Division) issued no-action relief on January 31, in response to a request from attorneys on behalf of firms effecting securities transactions in connection with the transfer and control of a company to a buyer that will actively operate the company or its business (each, an M&A Broker). The no-action relief specifies that the Division would not recommend enforcement action to the SEC if an M&A Broker engages in certain activities in connection with the purchase or sale of privately held companies without registering as a broker-dealer pursuant to Section 15(b) of the Securities

Exchange Act of 1934 (Exchange Act). A "privately held company" for purposes of the no-action letter is generally an operating company that does not have any class of securities registered, or required to be registered, with the SEC.

Previously, the SEC and relevant court proceedings held that a person in the business of effecting the sale of operating businesses through the sale of securities was acting as a "broker," as such term is defined under Section 3(a)(4) of the Exchange Act. Accordingly, absent an exemption, such person would be required to register as a broker-dealer under Section 15(b) of the Exchange Act. The request letter distinguishes mergers, acquisitions, business sales and business combinations from traditional capital-raising securities transactions because, among other reasons, the buyer takes an active role in operating a company that is the subject of a merger or acquisition involving a change of control, as opposed to the passive investment objectives of an investor in an equity-raising transaction. The SEC's issuance of no-action relief to M&A Brokers that meet certain conditions (see below) represents a major shift in the SEC's position and a substantial change to the regulatory framework for M&A Brokers.

The SEC set a number of conditions in issuing the no-action relief, including, among other things, that (i) the buyer will control (e.g., own 25 percent or more of the company) and actively operate the company after the transaction, (ii) the M&A Broker will not provide financing and may not bind a party to the transaction, (iii) the M&A Broker may not assist in forming the group of buyers, (iv) the M&A Broker may not have custody of the funds or securities issued or exchanged in connection with the transaction and (v) the transaction will not involve a public offering.

The no-action letter only exempts M&A Brokers that meet the conditions of the letter from the registration requirement under the Exchange Act, but does not discuss any state registration requirements that may apply.

Click here to read the SEC's January 31, 2014 No-Action Letter.

CFTC

CFTC Issues Guidance on New Filing Requirements

On February 5, the Division of Swap Dealer and Intermediary Oversight (DSIO) of the Commodity Futures Trading Commission issued guidance to futures commission merchants (FCMs) and depositories regarding procedures for complying with certain new filing requirements under the CFTC's enhanced customer protection rules, which were effective January 13. The guidance provides information to FCMs and depositories for filing (i) acknowledgement letters for accounts holding customer funds, (ii) "early warning" notices and (iii) certain financial and risk reports. Additionally, DSIO reminds FCMs to use the WinJammer Online Filing System when filing all letters, notices and reports covered in the guidance. A short summary of the new and amended regulations referenced by the guidance is available in the *Corporate and Financial Weekly Digest* edition of November 1, 2013.

The guidance is available here.

SEC Extends Exemptions for Security-based Swaps

On February 5, the Securities and Exchange Commission issued an extension of interim final rules that provide exemptions for security-based swaps from securities laws under the Securities Act of 1933, the Securities Exchange Act of 1934 and the Trust Indenture Act of 1939. Originally set to expire on February 11, 2014, the exemptions will now remain effective an additional three years until February 11, 2017. The exemptions allow market participants to continue trading security-based swaps without interruption while the SEC finishes its regulatory regime for security-based swaps and evaluates the implications of including security-based swaps in the definition of "security."

The interim final rule extension is available here.

INVESTMENT COMPANIES AND INVESTMENT ADVISERS

SEC Issues Risk Alert on Investment Advisers' Due Diligence Processes for Selecting Alternative Investments

The Securities and Exchange Commission's Office of Compliance Inspections and Examinations (OCIE) issued a risk alert on January 28 regarding the due diligence practices of investment advisers when they recommend or place clients' assets in alternative investments, including private funds such as hedge funds, private equity funds, venture capital funds, real estate funds and funds of private funds.

The risk alert was issued following OCIE staff examinations of the due diligence and related investment advisory processes of more than ten SEC-registered investment advisers that invested in or recommended private fund and fund of private fund investments. The staff evaluated how such advisers: (i) performed their due diligence; (ii) identified, disclosed and mitigated conflicts of interest (e.g., benefits to the adviser or its employees for allocations made to private funds) and (iii) utilized experienced investment teams when evaluating complex investment strategies and fund structures.

The risk alert reminds advisers that exercise discretion to purchase alternative investments on behalf of clients that they must determine whether such investments meet the clients' investment objectives and are consistent with the investment principles and strategies that were disclosed by the manager of the alternative investment to the adviser. With respect to the due diligence processes, the risk alert provides a roadmap of current industry trends and practices to comply with the Investment Advisers Act of 1940 and federal securities laws.

The risk alert cites certain deficiencies in the due diligence processes of several of the advisory firms examined, including: (i) omitting alternative investment due diligence policies and procedures from their annual reviews, even though these investments comprised a large portion of certain advisers' investments on behalf of clients; (ii) providing potentially misleading information in marketing materials about the scope and depth of due diligence conducted and (iii) having due diligence practices that differed from those described in the advisers' disclosures to clients.

Click here to read the SEC's January 28, 2014 Risk Alert.

LITIGATION

District Court Upholds SEC's Partial Win in Bank Fraud Suit

The US District Court for the Southern District of Florida recently refused to reconsider its earlier decision granting partial summary judgment in favor of the Securities and Exchange Commission in a securities fraud case against BankAtlantic Bancorp, Inc.

The SEC alleged that BankAtlantic Bancorp, Inc., now known as BBX Capital Corporation (BBX or Bank), failed to disclose problems with its commercial real estate portfolio. After the court granted summary judgment in favor of the SEC on the issue of falsity, BBX moved for reconsideration.

In finding that BBX had not met the high standard necessary for a motion to reconsider, the court noted that the Bank did not disclose—and in some cases affirmatively misrepresented—"the existing trend of crumbling creditworthiness evident in the entire Commercial Residential Portfolio." The court rejected BBX's argument that it made adequate disclosures, explaining that the Bank "cannot inoculate [itself] from liability by informing investors about potential problems that might arise based on what the market may do in the future … when, at the same time, they failed to disclose to investors current problematic trends [it] knew about."

The case is currently scheduled for trial in November.

SEC v. BankAtlantic Bancorp,. Inc. et al., Case No. 12-cv-60082 (S.D. Fla. Jan. 30, 2014).

SDNY Grants SEC's Final Summary Judgment Claim in Securities and Investment Advisor Fraud Case

The US District Court for the Southern District of New York granted the Securities and Exchange Commission summary judgment on its one outstanding securities fraud claim against Alberto Vilar and Gary Tanaka, co-founders of Amerindo Investment Advisors, Inc., after the US Court of Appeals for the Second Circuit clarified the meaning of a "domestic transaction in any security."

The SEC alleged that Vilar and Tanaka diverted millions from investors to their own businesses. In a related criminal proceeding, a jury found the pair guilty of securities fraud and investment advisor fraud in 2008. While the criminal case was pending on appeal, the district court granted the SEC's motion for summary judgment on all claims except one, finding that the criminal convictions had conclusively established three out of four elements for securities fraud, and thus the doctrine of issue preclusion barred Vilar and Tanaka from disputing those elements in the SEC's case. The court held that the final element—a "domestic transaction"—had not been conclusively established in the criminal case, and conducted its own analysis, ultimately concluding that all investors except one (the Mayer Family) had engaged in a "domestic transaction."

After the summary judgment decision, the Second Circuit issued its judgment and opinion for the appeal in the criminal case. In a footnote, the Second Circuit expressly disagreed with the district court's interpretation of "domestic transaction" as applied to the Mayer Family, and explained that the domestic nature of a transaction "concerns where, physically, the purchaser or seller" committed to buying or selling a security.

In light of the Second Circuit's opinion, both the SEC and Vilar and Tanaka moved for reconsideration of the district court's summary judgment decision. On that motion, the district court found that the Second Circuit's ruling in the criminal case was controlling, intervening law, and thus the court was required to reconsider its prior decision. Analyzing each of the investors, including the Mayer Family, the court concluded that all had engaged in domestic transactions because a preponderance of the evidence showed that each was physically present in the United States. Thus, the court reaffirmed its grant of summary judgment for earlier investors and granted summary judgment for the Mayer Family claims.

SEC v. Amerindo Inv. Advisors, Inc. et al., Case No. 05-cv-5231 (RJS) (S.D.N.Y. Jan. 31, 2014).

For more information, contact:

FINANCIAL SERVICES

Janet M. Angstadt	+1.312.902.5494	janet.angstadt@kattenlaw.com
Henry Bregstein	+1.212.940.6615	henry.bregstein@kattenlaw.com
Wendy E. Cohen	+1.212.940.3846	wendy.cohen@kattenlaw.com
Guy C. Dempsey Jr.	+1.212.940.8593	guy.dempsey@kattenlaw.com
Kevin M. Foley	+1.312.902.5372	kevin.foley@kattenlaw.com
Jack P. Governale	+1.212.940.8525	jack.governale@kattenlaw.com
Arthur W. Hahn	+1.312.902.5241	arthur.hahn@kattenlaw.com
Carolyn H. Jackson	+44.20.7776.7625	carolyn.jackson@kattenlaw.co.uk
Kathleen H. Moriarty	+1.212.940.6304	kathleen.moriarty@kattenlaw.com
Ross Pazzol	+1.312.902.5554	ross.pazzol@kattenlaw.com
Kenneth M. Rosenzweig	+1.312.902.5381	kenneth.rosenzweig@kattenlaw.com
Fred M. Santo	+1.212.940.8720	fred.santo@kattenlaw.com
Christopher T. Shannon	+1.312.902.5322	chris.shannon@kattenlaw.com
Peter J. Shea	+1.212.940.6447	peter.shea@kattenlaw.com
James Van De Graaff	+1.312.902.5227	james.vandegraaff@kattenlaw.com
Robert Weiss	+1.212.940.8584	robert.weiss@kattenlaw.com
Gregory E. Xethalis	+1.212.940.8587	gregory.xethalis@kattenlaw.com
Lance A. Zinman	+1.312.902.5212	lance.zinman@kattenlaw.com
Krassimira Zourkova	+1.312.902.5334	krassimira.zourkova@kattenlaw.com

LITIGATION

William M. Regan	+1.212.940.6541	william.regan@kattenlaw.com
Tenley Mochizuki	+1.212.940.8568	tenley.mochizuki@kattenlaw.com

* Click here to access the *Corporate and Financial Weekly Digest* archive.

Katten

Katten Muchin Rosenman LLP www.kattenlaw.com

AUSTIN | CENTURY CITY | CHARLOTTE | CHICAGO | HOUSTON | IRVING | LONDON | LOS ANGELES | NEW YORK | ORANGE COUNTY | SAN FRANCISCO BAY AREA | SHANGHAI | WASHINGTON, DC

Katten Muchin Rosenman LLP is an Illinois limited liability partnership including professional corporations that has elected to be governed by the Illinois Uniform Partnership Act (1997).

London: Katten Muchin Rosenman UK LLP.