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CORPORATE & FINANCIAL
WEEKLY DIGEST

March 9, 2012

## SEC/CORPORATE

Please see "SEC and CFTC Propose Rules on Identity Theft Detection and Prevention" in **CFTC** below.

## BROKER DEALER

### FINRA Best Execution and Interpositioning Rule Effective May 31, 2012

As reported in the October 21, 2011 edition of *Corporate & Financial Weekly Digest*, the Financial Industry Regulatory Authority (FINRA) proposed a rule change to adopt NASD Rule 2320 (Best Execution and Interpositioning) and Interpretive Material 2320 (Interpretive Guidance with Respect to Best Execution Requirements) as FINRA Rule 5310 in the consolidated FINRA rulebook. Subsequently, the Securities and Exchange Commission issued an order granting approval of the proposed rule change. FINRA has issued a Regulatory Notice announcing that FINRA Rule 5310 will become effective on May 31, 2012. The Regulatory Notice also states that FINRA Rule 6438 (Displaying Priced Quotations in Multiple Quotation Mediums) will become effective on May 31, 2012.

## CFTC

### SEC and CFTC Propose Rules on Identity Theft Detection and Prevention

On February 28, the Securities and Exchange Commission (SEC) and the Commodity Futures Trading Commission (CFTC) jointly issued proposed rules and guidelines intended to help protect investors from identity theft by ensuring that certain SEC- and CFTC-regulated entities create programs to detect and respond to identity theft red flags. The proposal, if implemented, will affect broker-dealers, investment advisors, investment companies, futures commission merchants, commodity pool operators, commodity trading advisors, retail foreign exchange dealers, introducing brokers, swap dealers and major swap participants. The Dodd-Frank Wall Street Reform and Consumer Protection Act amended section 615(e) of the Fair Credit Reporting Act, transferring from the Federal Trade Commission to the SEC and CFTC authority over identity theft guidelines for financial institutions and creditors. The proposed rules cover two areas to address identity theft. First, the proposed rules and guidelines would require financial institutions and creditors to develop and implement a written identity theft prevention program that is designed to detect, prevent, and mitigate identity theft in connection with certain existing accounts or the opening of new accounts. Second, the proposed rules would establish special requirements for any credit and debit card issuers to assess the validity of notifications of changes of address under certain circumstances. The SEC and CFTC are seeking comment from the public on or before May 7.

To view the SEC Proposing Release, click here.
To view the CFTC Proposing Release, click here.

# LITIGATION

### Member of LLC Not an Employer Under the Fair Labor Standards Act

In the first Federal appellate decision to address the issue head on, the U.S. Court of Appeals for the Fifth Circuit last week held that an individual is not personally liable as an "employer" under the Fair Labor Standards Act (FLSA) merely by their status as an LLC member. The plaintiff was a bartender at a bar owned by Pasha Entertainment Group, LLC, and alleged that he was not paid an hourly wage in violation of the FLSA. The LLC being out of business, the plaintiff sued the defendant, a member of the LLC, in his individual capacity. If an individual has exerted "actual operational control," that individual can be personally liable for FLSA violations committed by a company.

The District Court for the Southern District of Texas granted summary judgment in favor of the defendant, and the Fifth Circuit affirmed. The Fifth Circuit applied the "economic reality" test to determine whether the defendant had operational control. This involves examining the hiring, firing, supervisory, and payment powers the defendant specifically exercised. Because the defendant did not hire the plaintiff, did not sign the plaintiff's checks, and did not supervise the plaintiff's day-to-day work, as a matter of economic reality, no control existed. Accordingly, the Fifth Circuit refused to impose liability on the member of the LLC. The court explained: "We decline to adopt a rule that would potentially impose individual liability on all shareholders, members and officers of entities that are employers under the FLSA based on their position rather than the economic reality of their involvement in the company."

*Gray v. Powers*, No. 10-20808 (5th Cir. Feb. 29, 2012).

### Enron Auditors May Still Face Disciplinary Actions

Whether former Arthur Andersen accountants violated professional standards and should be subject to sanctions for their audits of Enron more than 15 years ago has been a subject of protracted litigation. In the latest round, last week, three accountants were rebuffed by a Texas state appeals court which held that state regulators followed appropriate procedures in sanctioning the accountants in connection with audits of Enron completed in 1997 and 1998. The plaintiff accountants had their professional licenses revoked or suspended after the Texas State Board of Public Accountancy (the Board) reviewed the accountants' approval of Enron's off-balance sheet treatment of two entities, which resulted in artificially increasing the company's income. The Board had overruled decisions of an administrative law judge, who had recommended far less severe sanctions. The plaintiffs sought judicial review of the administrative ruling, claiming that the Board reach its decision in illegal closed-door sessions.

At the first stage of judicial review, the trial court agreed with the accountants and held that the Board violated Texas' Open Meetings Act, reversed the sanctions, and barred the Board from taking any further disciplinary action against the accountants. That ruling, however, was reversed by the appellate court last week. The court held that there were extensive, substantive public deliberations, the hearing of oral arguments, and an ultimate vote made in a public meeting, which satisfied the Board's responsibilities under the Open Meetings Act. Although the Board also had closed executive sessions, the court held that the Board's public votes met the legal requirements. The case was remanded for further proceedings, so the litigation still has not come to a close.

*Texas State Board of Public Accountancy v. Bass*, No. 03-10-002777-CV (Tex. App. Feb. 24, 2012).

# BANKING

### Federal Reserve Extends Comment Deadline For Enhanced Prudential Standards and Remediation Proposed Regulations

On March 2, the Federal Reserve announced that it has extended until April 30 the deadline for submitting comments on proposed rulemaking for public comment to implement the enhanced prudential standards required to be established under section 165 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) and the early remediation requirements established under section 166 of the Act. This follows action taken by the Federal Reserve on January 5, when it published in the *Federal Register* a notice of the request for comments to be due on March 31.  The enhanced standards include risk-based capital and leverage requirements, liquidity standards, requirements for overall risk management (including establishing a risk committee), single-counterparty credit limits, stress test requirements, and a debt-to-equity limit for companies that the Financial Stability Oversight Council has determined pose a grave threat to financial stability.

The Federal Reserve release stated that "due to the range and complexity of the issues addressed in the rulemaking, the Board has determined that an extension of the end of the public comment period from March 31, 2012, until April 30, 2012, is appropriate."

For more information, click here.

### Federal Reserve Issues Guidance On Upgrades for Supervisory Ratings

On March 2, the Federal Reserve Board's Division of Supervision and Regulation issued  SR 12-4, which contains guidance "to ensure that supervisors apply consistent standards as they evaluate whether banking organizations … are eligible for upgrades of supervisory ratings."  The guidance was issued "to ensure that upgrades occur in a timely manner when the banking organizations have made the requisite progress in addressing any supervisory concerns that had prompted lower ratings."  To be eligible for an upgrade, institutions "are expected to demonstrate, among other things, improvement in financial condition and risk management, as well as show that such improvement is likely to continue."  This guidance applies to all institutions supervised by the Federal Reserve with total consolidated assets of $10 billion or less, including state member banks and bank holding companies. In so stating, the Federal Reserve explained that "while the factors discussed below are particularly relevant for state member community banks with consolidated assets of $10 billion or less and address situations encountered recently, they can be applied to other types of community institutions supervised by the Federal Reserve."  The timing of the release is interesting, particularly given the legislation presently before Congress that would require modification of certain practices employed by bank examiners.

For more information, click here.

### FDIC Issues Guide for Consumers

On March 5, the Federal Deposit Insurance Corporation issued a short guide to help consumers understand the differences between debit, credit and prepaid cards.  The guide is intended "to help consumers, who routinely use cards to pay for goods and services but who don't always understand the differences in how these cards work or the applicable consumer protections."

For more information, click here.

### Volcker Rule Will Not Be Ready On Time

The Volcker Rule is required by the Dodd-Frank Wall Street Reform and Consumer Protection Act to be effective by July 21.  In response to questions regarding the Volcker Rule from the House Financial Services Committee Federal Reserve Chairman Ben Bernanke stated, “I don’t think it will be ready for July.”  The Federal Rule has received thousands of comments on the proposed rule, from individuals, banks, financial organizations, trade associations, and sovereign entities, and consumer groups.

### FinCEN Seeks To Strengthen Customer Due Diligence Requirements

On February 29, the Financial Crimes Enforcement Network (FinCEN) issued an advance notice of proposed rulemaking (ANPRM) to solicit public comment on a wide range of questions pertaining to the possible application of an explicit customer due diligence (CDD) obligation on financial institutions, including a requirement for financial institutions to identify beneficial ownership of their accountholders.

The agency stated that "[d]espite efforts to highlight and clarify CDD and beneficial ownership expectations over this time, FinCEN is concerned that there is a lack of uniformity and consistency in the way financial institutions address these implicit CDD obligations and collect beneficial ownership information within and across industries."  In addition to expanding CDD requirements, the proposal would "establish a categorical requirement for financial institutions to identify beneficial ownership of their accountholders, subject to risk-based verification and pursuant to an alternative definition of beneficial ownership…"

While the scope of the ANPRM includes all of the industries that have anti-money laundering (AML) program requirements under FinCEN's regulations, "at this time, and as an initial matter, FinCEN is considering developing a CDD rule to cover banks, brokers or dealers in securities, mutual funds, futures commission merchants, and introducing brokers in commodities."

Comments on the ANPRM will be accepted for 60 days from the date of publication in the *Federal Register*.

For more information, click here.

### Federal Reserve Releases Action Plans To Correct Bank Mortgage Lending Deficiencies

On February 27, the Federal Reserve Board released action plans for supervised financial institutions to correct deficiencies in residential mortgage loan servicing and foreclosure processing. It also released engagement letters between supervised financial institutions and independent consultants retained by the firms to review foreclosures that were in process in 2009 and 2010.

The action plans are required by formal enforcement actions issued by the Federal Reserve last year. The enforcement actions direct mortgage loan servicers regulated by the Federal Reserve to submit acceptable plans that describe, among other things, how the institutions will strengthen communications with borrowers by providing each borrower the name of a primary point of contact at the servicer; establish limits on foreclosures where loan modifications have been approved; establish robust, third-party vendor controls; and strengthen compliance programs. The Federal Reserve enforcement actions also require the parent holding companies of mortgage servicers to submit acceptable plans that describe, among other things, how the companies will improve oversight of servicing and foreclosure processing conducted by bank and nonbank subsidiaries. Finally, the enforcement actions further require the mortgage servicing subsidiaries to provide appropriate remediation to borrowers who suffered financial injury as a result of errors by the servicers. The engagement letters describe the procedures that will be followed by the independent consultants in reviewing servicers' foreclosure files to determine whether borrowers suffered financial injury as a result of servicer error.

For more information, click here.

## EXECUTIVE COMPENSATION AND ERISA

### EEOC Issues ADA Guidance for Employers on the Rights of Veterans with Disabilities

Each year, veterans leave the armed services and enter or re-enter the job market. The U.S. Equal Employment Opportunity Commission (the EEOC) estimates that 25% of veterans returning from the Middle East conflicts will have a service-connected disability. Recognizing the importance of assuring returning veterans a level playing field at home, on February 28, the EEOC issued Q&A guides for employers and for veterans, serving as reminders that veterans with disabilities are covered by the Americans with Disabilities Act (the ADA), and the Americans with Disabilities Act Amendments Act of 2008.

The employers' guide offers employers a practical guide to the recruitment, hire, and accommodation of veterans with disabilities. For example, the guide answers questions such as: what does the ADA require, and when is it applicable? It further answers questions such as: can an employer can ask if an applicant is a disabled veteran; and can an employer give preferential treatment to a veteran with a disability? The guide outlines actions employers can take to prevent employment-based discrimination against veterans from occurring, how to provide reasonable accommodations, specific steps to take if an employer desires to recruit and hire veterans with disabilities, and finally, supplies information on laws and regulations that employers may find helpful if they intend to recruit and hire veterans with disabilities.

While the guide does not have the force of law, the EEOC guidance expresses the agency's view on the subjects stated. Employers therefore have a strong interest in understanding the policy.

The EEOC guidance can be found here.

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LITIGATION

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BANKING

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