Katten
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SEC / CORPORATE

US District Court Holds That Discretionary Tax Withholding is Exempt Under 16b-3

Several companies have received shareholder letters seeking to recover short-swing profits from insiders under Section 16(b) of the Securities Exchange Act of 1934, alleging that such insiders made non-exempt purchases of stock within six months of having shares withheld either for payment of the exercise price of employee stock options or to satisfy tax liabilities upon the vesting of restricted stock units (resulting in deemed dispositions of those shares). In each case, the shareholder has claimed that the Rule 16b-3(e) exemption (for transactions between an issuer and its officers and directors) is only available for such dispositions when the withholding is automatic, without an election by the insider or the company. On April 26, the United States District Court for the Southern District of Texas granted a motion to dismiss in *JD. Jordan v. Robert Flexton, et al*., No.4:16-CV03316, holding that dispositions of restricted stock units to cover tax withholding are compensation related transactions designed to be exempt under Section 16b-3(e) of the Securities Exchange Act of 1934.

This ruling is significant because it rejects the argument that Rule 16b-3 exempts withholding transactions only if "automatic." In this case the court allowed reliance on the exemption, when the company (Dynegy, Inc.) made the decision to withhold shares, not the insider. Note that, to rely upon this exemption, the tax withholding right must have been approved by the board of directors of the issuer, or a committee of the board of directors that is composed solely of two or more "non-employee directors" (typically, the compensation committee).

The full text of the order is available here.

Hinman Named Director of Division of Corporation Finance

On May 9, the Securities and Exchange Commission announced that William H. Hinman will be named the new director of the SEC's Division of Corporation Finance. Mr. Hinman was most recently a partner at Simpson Thacher & Bartlett LLP, where he advised public and private companies in corporate finance matters and boards of directors on public reporting, governance and other corporate matters. Newly sworn-in SEC Chairman Jay Clayton noted that, given Mr. Hinman's experience, "he understands the SEC's mission to promote capital formation, while ensuring that investors have the information necessary to make informed decisions."

The SEC's press release regarding Mr. Hinman's appointment is available here.

BROKER-DEALER

FINRA Proposed Rule Change to the Consolidated Audit Trail

In February, pursuant to Regulation NMS, the various national securities exchanges and the Financial Industry Regulatory Authority (each, a Participant) filed with the Securities and Exchange Commission a plan (Plan) to create, implement and maintain a consolidated audit trail (CAT) to capture information related to customers and order events for transactions in NMS securities and over-the-counter equity securities. The CAT will capture order information across all markets and throughout the life of an order (from inception to execution).

The Plan accomplishes this by creating CAT NMS, LLC (the Company), of which each Participant is a member, to operate the CAT. Under the Plan, the Operating Committee of the Company (Operating Committee) has discretion to establish funding for the Company to operate CAT, including establishing fees that the Participants will pay, and establishing fees to be implemented by Participants for their respective members (Industry Members) that are required to record and report information pursuant to the Plan (CAT Fees). The Participants are required to file with the SEC under Section 19(b) of the Securities Exchange Act of 1934any such CAT Fees applicable to Industry Members that the Operating Committee approves. Accordingly, FINRA submitted this filing to propose the Consolidated Audit Trail Funding Fees, which will require Industry Members that are FINRA members to pay the CAT Fees determined by the Operating Committee.

The proposed rule change, as well as more information, including with respect to the level of fees being contemplated in the fee schedule, is available here.

BANKING

CFPB's Prepaid Cards Rule Escapes Coverage Under the Congressional Review Act

Under the Congressional Review Act (CRA), Congress can review and overrule any federal regulations imposed during the final six months of the previous administration with a simple majority vote in each branch of Congress. However, Congress' power is limited under the CRA because it can only introduce and vote on a CRA resolution within 60 legislative days after the regulation was finalized. Once a rule is repealed, the CRA also prohibits the reissuing of the rule in the same form or the issuing of a new rule which is substantially the same as the repealed rule, unless the reissued or new rule is specifically authorized by a law enacted after the date of the joint resolution disapproving the original rule.

In February, joint resolutions were introduced in both the Senate and the House to repeal the final Consumer Financial Protection Bureau (CFPB) Prepaid Cards Rule under the CRA. The joint resolutions would nullify the rule finalized by the CFPB on November 22, 2016, relating to prepaid accounts under the Electronic Fund Transfer Act and the Truth in Lending Act. The rule establishes various consumer protections with respect to prepaid accounts. Neither the Senate nor the House voted on these resolutions, and the CRA voting deadline for this year passed on May 11.

UK DEVELOPMENTS

FCA Publishes Policy Statement on Remuneration for CRD IV Firms

On May 3, the UK Financial Conduct Authority (FCA) published a policy statement (PS17/10) to help firms subject to the Capital Requirements Directive (CRD IV) understand the rules applying to their remuneration policies and practices.

The FCA states that they have aligned the provision of PS17/20 with the European Banking Authority (EBA) Guidelines (Guidelines) on sound remuneration policies, which were published in December 2015 and came into force on January 1, 2017. The FCA states that the amendments their Handbook contained in PS17/10 are being made so that the Handbook complies with the Guidelines.

PS17/10 contains non-Handbook guidance designed to address some of the most frequently asked questions on how the FCA implements provisions under the EBA Guidelines. The frequently asked questions cover topics such as material risk takers, governance, groups, proportionality and variable remuneration.

PS17/10 is available here.

EU DEVELOPMENTS

FIA Calls for Transitional Period for Commodity Firms Under MiFID II

As originally reported by Risk.net (subscription required) on May 5, the Futures Industry Association (FIA) has asked HM Treasury to allow for a transitional period for commodity firms under the United Kingdom's implementation of the revised Markets in Financial Instruments Directive (MiFID II).

MiFID II will become effective in January 2018, at which point commodity firms are expected to be authorized for those parts of their business which require authorization or rely on an exemption. However, under MiFID II RTS 20, commodity firms will only be able to determine whether they can rely on an exemption by carrying out calculations, which require three years of trading data up to December 31 before the authorization is required.

The UK Financial Conduct Authority (FCA) has stated that in order to guarantee that applications for authorization are reviewed and granted before MiFID II comes into effect, firms need to have submitted their application by July 3. It is due to this mismatch in time scales, between the data timeframe and the FCA's deadline for guaranteed applications, that the FIA is pressing for a transitional regime.

For additional coverage on financial and regulatory news, visit *Bridging the Week*, authored by Katten's Gary DeWaal.

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