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SEC NEWS

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SEC's Advisory Committee on Small and Emerging Companies Discusses Exchange Act Registration Requirements, Regulation A and Crowd-Funding

The SEC's Advisory Committee on Small and Emerging Companies met on February 1, 2012, to consider proposed recommendations to the SEC concerning a relaxation of the registration requirements under the Securities Exchange Act of 1934 (Exchange Act), which would increase the amount of securities that can be sold pursuant to Regulation A and crowd-funding.

Under Section 12(g) of the Exchange Act and relevant SEC rules, a company must register a class of its equity securities and is subject to the reporting obligations under the Exchange Act if, at the end of the company's fiscal year, the securities are held of record by 500 or more persons and the company has total assets exceeding $10 million. Concerns have been raised that this registration threshold is too low and forces companies to become subject to public-reporting requirements prematurely and that companies are forced to adjust artificially their compensation and capital raising activities to avoid hitting the 500 shareholder cap.

The Committee discussed a number of issues, including whether beneficial owners or shareholders of record should be counted, the particular capital-raising needs of community banks, and whether employee-shareholders should be counted. After much discussion, the Committee determined to recommend to the SEC that (i) record holders, and not beneficial owners, continue to be counted for purposes of Section 12(g) of the Exchange Act, (ii) the threshold for registration and reporting under the Exchange Act be increased to 2,000 record holders (and to 1,200 to cease reporting under the Exchange Act) for banks and bank holding companies, (iii) the threshold for registration and reporting under the Exchange Act be increased to 1,000 record holders (and to 600 to cease reporting under the Exchange Act) for entities that are not banks or bank holding companies, and (iv) employees who are unable to trade their company securities be excluded from the number of shareholders counted for purposes of Section 12(g).

The Committee also discussed Regulation A, a rarely used provision of the federal securities laws that allows companies to offer and sell up to $10 million of securities without having to complete a "full-blown" S-1 registration statement. Sometimes called "registration lite," Regulation A is seldom used because the company is required to prepare an extensive offering document which is filed with and reviewed by the SEC and each state securities commission of the states in which the securities will be sold. The Committee voted to recommend to the SEC that the Regulation A threshold be increased to $50 million but recognized that the process of filing with and review by state securities commissions remains a significant barrier to the use of Regulation A. In general, members of the Committee did not expect that increasing the threshold to $50 million would increase the utilization of Regulation A.

(continued on page 2)

CONTENTS

SEC NEWS

SEC's Advisory Committee on Small and Emerging Companies Discusses Exchange Act Registration Requirements, Regulation A and Crowd-Funding (continued from page 1)

Interestingly, the Committee decided to make no recommendation with respect to crowd-funding. Members of the Committee expressed concern that by permitting crowd-funding, early-stage companies would significantly damage their ability to later raise needed funds from angel and institutional investors who, generally, are averse to investing in private companies with large numbers of shareholders. The Committee also expressed concerns about allowing such offerings with little, if any, regulatory oversight. ■

FINRA Revises Its Proposed Rule on Private Placements

On January 19, 2012, the Financial Industry Regulatory Authority, Inc. (FINRA) filed with the SEC a Partial Amendment No. 1 (Partial Amendment)[1] to proposed FINRA Rule 5123 (Private Placement of Securities) to address concerns raised in comments on the initial proposed rule filed with the SEC on October 5, 2011 (Proposed Rule). In response, on January 20, 2012, the SEC issued a Notice of Filing of Partial Amendment No. 1 and Order Instituting Proceedings to Determine Whether to Approve or Disapprove a Proposed Rule Change, as modified by Partial Amendment No. 1, to Adopt FINRA Rule 5123.[2]

The Proposed Rule would have required that members of FINRA and associated persons that offer or sell any applicable private placement (as described in the proposed rule change), or participate in the preparation of a private placement memorandum, term sheet or other disclosure documents in connection with any such private placement, provide relevant disclosures to each investor prior to sale describing the anticipated use of offering proceeds, and the amount and type of offering expenses and offering compensation.

The comment letters received by the SEC contained a broad range of concerns, including, among others, that the proposed rule change:

- contained a definition of private placement that was overbroad and could be interpreted to apply to any offer or sale of securities for which an exemption from registration is claimed under the Securities Act of 1933 (Securities Act) or could be interpreted to require a FINRA member to have primary responsibility for preparing disclosure documents for sales in the event that an issuer does not prepare them;

(continued on page 3)

PRACTICE TIPS

Form 10-K and Proxy Season—Checklist of Action Items

1. ***Review SEC Guidelines for Form 10-K Disclosures.*** At the end of 2011 and beginning of 2012, the SEC issued two disclosure guidelines affecting companies' Form 10-K disclosures: guidance on cybersecurity risks[3] and exposures to European sovereign debt.[4] Each public company should evaluate whether its business is materially affected by cybersecurity risks or exposure to European debt. These issues can affect a company's disclosures in its Form 10-K "Business," "Risk Factors" and "Management's Discussion and Analysis of Financial Condition and Results of Operations" sections, as well as its notes to financial statements and disclosure controls and procedures.

2. **Use Correct Headings in Form 10-K and Comply with Mine Safety Disclosure Rules.** Effective January 27, 2012,[5] Form 10-K includes a new Item 4 in Part I:

   "Item 4. Mine Safety Disclosures

   If applicable, provide a statement that the information concerning mine safety violations or other regulatory matters required by Section 1503(a) of the Dodd-Frank Wall Street Reform and Consumer Protection Act and Item 104 of Regulation S-K (17 CFR 229.104) is included in exhibit 95 to the annual report."

   Although the new mine safety disclosure applies only to a "registrant that is the operator, or that has a subsidiary that is an operator, of a coal or other mine" and may not apply to your company, check the table of contents of Form 10-K to make sure that Item 4 states "Mine Safety Disclosures," not "(Removed and Reserved)."

(continued on page 3)

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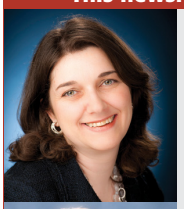

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FINRA Revises Its Proposed Rule on Private Placements (continued from page 2)

- may be contrary to the intent of Congress and/or the federal securities laws, which do not otherwise prescribe these disclosures for many types of private placements;
- could significantly affect the ability of many issuers to raise capital; and
- should broaden or provide for additional exemptions, such as in connection with a merger or acquisition.

To respond to these concerns, FINRA proposed the Partial Amendment which would narrow the proposed definition of "private placement" to mean only a non-public offering of securities conducted in reliance on an available exemption from registration under the Securities Act. The Proposed Rule, as amended by the Partial Amendment, would not apply to securities offered pursuant to the following provisions:

- Securities Act Sections 4(1), 4(3) and 4(4) (which generally exempt secondary transactions);
- Securities Act Sections 3(a)(2) (offerings by banks), 3(a)(9) (exchange transactions with an existing holder, where no one is paid to solicit the exchange), 3(a)(10) (securities subject to a fairness hearing), or 3(a)(12) (securities issued by a bank or bank holding company pursuant to reorganization or similar transactions); or
- Section 1145 of the Bankruptcy Code (securities issued in a court-approved reorganization plan that are not otherwise entitled to the exemption from registration afforded by Securities Act Section 3(a)(10)).

FINRA proposed amending the filing and disclosure requirements of the proposed rule change for those private placements for which a disclosure document includes a description

of the anticipated use of offering proceeds, the amount and type of offering expenses, and the amount and type of compensation provided or to be provided to sponsors, finders, consultants, and members and their associated persons in connection with the offering. Prior to any sale, members would be required to provide the disclosure document to each investor, other than those investors in a private placement that would be subject to an exemption. Each member participating in the offering or a member designated to make the filing on behalf of all members identified in the filing would be required to file such document with FINRA no later than 15 calendar days after the date of first sale.

In addition, FINRA proposed amending the filing and disclosure requirements for private placements for which there is no disclosure document. If no disclosure document is used, the participating member or a designated member acting on behalf of the member would be required to make a notice filing with FINRA no later than 15 calendar days after the date of first sale, identifying the private placement and the participating members and stating that no disclosure document was used.

Further, FINRA proposed to add supplementary material to the proposed rule change that would clarify that the rule would not require delivery of multiple copies of a disclosure document to a single customer. The proposed rule change would require an affected member to deliver disclosure documents only to persons to whom it sells shares in the private placement.

It remains uncertain whether the Proposed Rule, as amended by the Partial Amendment, will be approved by the SEC. Comments on the Proposed Rule, as modified by the Partial Amendment, were due on February 27, 2012. ■

PRACTICE TIPS

Form 10-K and Proxy Season—Checklist of Action Items (continued from page 2)

3. ***Stay Up to Date on Shareholder Proposal Developments.*** Although the "proxy access" rule,[6] which required a public company to include nominees for director proposed by a shareholder in its proxy materials, is not in force, the private ordering rule (i.e., amendments to Rule 14a-8(i)(8)) became effective in September 2011. The private ordering rule gave shareholders an opportunity to propose amendments to a company's governing documents that would establish procedures for the inclusion of one or more shareholder nominees for director in company proxy materials. In addition, the SEC issued Staff Legal Bulletin No. 14F on Shareholder Proposals[7] in October 2011. The Staff Legal Bulletin addressed, among other things, (i) brokers and banks that constitute "record" holders under Rule 14a-8(b)(2)(i) for purposes of verifying whether a beneficial owner is eligible to submit a proposal under Rule 14a-8; (ii) common errors shareholders can avoid when submitting proof of ownership; and (iii) the SEC's new process for transmitting Rule 14a-8 no-action responses by email.

4. ***Prepare "Bullet-Proof" Compensation Disclosure.*** Shareholder advisory votes to approve company executive compensation (the say-on-pay vote) have prompted public companies[8] to enhance their executive compensation disclosures, especially in the Compensation Discussion and Analysis (CD&A) section of the proxy statement in order to obtain shareholder approval of say-on-pay proposals. If the say-on-pay proposal is on the ballot for a company's coming annual meeting, and especially if shareholders did not approve the executive compensation last year, the company should carefully prepare compensation disclosures in its proxy statement to withstand the increased public scrutiny of the executive compensation information and to avoid public relations issues if its compensation practices are not approved by shareholders.[9] Additionally, one of the mandatory principles-based topics to be discussed in the CD&A focuses on whether, and if so, how the public company has considered the results of the most recent say-on-pay vote in determining compensation policies and decisions, and how that consideration has affected the company's executive compensation policies and decisions. Such disclosure becomes especially important in the case of a company that did not get its executive compensation approved by shareholders during the 2011 proxy season.

(continued on page 4)

ISS Issues FAQs

On January 25, 2012, Institutional Shareholder Services Inc. (ISS) issued Frequently Asked Questions (FAQs)[10] on a few executive compensation issues, including pay for performance and management say-on-pay responsiveness. These FAQs clarify certain ISS views expressed in its 2012 updates to proxy voting guidelines and white paper focused on ISS' new methodology of evaluating pay for performance alignment.

For example, one of the FAQs explains the impact an adverse pay-for-performance recommendation might have on equity plan proposals. ISS may recommend a vote AGAINST the equity plan if a significant portion of the CEO's misaligned pay is attributed to non-performance-based equity awards, and the CEO is one of the participants in the plan. In addition, the recommendation of a vote AGAINST the equity plan may depend on factors such as:

- magnitude of pay misalignment;
- contribution of non-performance-based equity grants to overall pay; and
- the proportion of equity awards granted in the last three fiscal years concentrated at the named executive officer level.

One of the FAQs states that in the case of a low or negative vote on a prior year's management say-on-pay (MSOP) proposal, ISS plans to give a negative voting recommendation on the election of directors comprising the compensation committee (and/or full board in rare cases) under two conditions: (i) if an issue is deemed sufficiently egregious to warrant that; and (ii) if ISS determines that the board has failed to respond adequately to issues that led to high opposition to the prior MSOP proposal. ■

NYSE Restricts Broker Voting on Corporate Governance Proxy Proposals

On January 15, 2012, the NYSE issued an Information Memo[11] setting forth further restrictions on brokers voting client shares without specific client instructions. According to the Information Memo, the following matters will now be treated as matters on which a broker may not vote absent client instructions:

- proposals to de-stagger the board of directors;
- proposals to implement majority voting in the election of directors;
- proposals to eliminate supermajority voting requirements;
- proposals providing for the use of written consents;
- proposals providing rights to call a special meeting; and
- proposals pertaining to certain types of anti-takeover provision overrides.

These changes may make it more challenging for companies to adopt the above-listed corporate governance proposals. ■

PRACTICE TIPS

Form 10-K and Proxy Season—Checklist of Action Items (continued from page 3)

5. ***Become Familiar with Proxy Advisor Positions.*** Companies need to closely monitor recommendations and general policy statements of proxy advisors, including Institutional Shareholder Services Inc. (ISS), to avoid possible negative recommendations on company proposals at the annual meeting of shareholders. The say-on-pay proposal may have increased the influence of vote recommendations given by proxy advisors due to the special attention paid to various compensation issues faced by pubic companies. For example, ISS issued its 2012 updates to proxy voting guidelines[12] and white paper[13] highlighting ISS' new methodology of evaluating pay for performance alignment.

6. ***Monitor SEC Rulemaking Timeline.*** The SEC's current estimated timeline for January – June 2012 includes the adoption of exchange listing standards regarding compensation committee independence and factors affecting compensation adviser independence, as well as the adoption of disclosure rules regarding compensation consultant conflicts under Section 952 of the Dodd-Frank Act. (The SEC proposed such rules in March 2011). Although these new rules may not affect companies' 2012 proxy statements, companies should review the composition of the compensation committee and evaluate the independence of committee members to identify potential issues. In addition, companies should review their relationships with compensation consultants and identify any existing or potential conflicts of interest in such relationships. In January – June 2012, the SEC also expects to propose rules regarding:
   - disclosure of pay-for-performance, pay ratios, and hedging by employees and directors (under Sections 953 and 955 of the Dodd-Frank Act); and
   - recovery of executive compensation (under Section 954 of the Dodd-Frank Act).

   The SEC plans to adopt final rules regarding these matters in July – December 2012. ■

Changes to the Deadline for Filing Annual Report on Form 20-F

Amendments[14] to the Form 20-F deadline go into effect this year. For companies with the fiscal year ended December 31, 2011, instead of filing an annual report within six months after December 31, 2011, foreign private issuers are required to file Form 20-F within four months after December 31, 2011. However, if a foreign private issuer filed a registration statement on Form F-3 and relies on the incorporation of 2011 financial statements by reference into the Form F-3, such issuer must file a Form 6-K or Form 20-F by March 31, 2012, including 2011 financial statements and notes to such statements, to prevent the financial statements in its Form F-3 from becoming stale. ■

SEC Amends Advisory Performance Fee Rules

The Investment Advisers Act of 1940 (Advisers Act) generally prohibits a registered investment adviser from charging performance-based fees to clients. However, Rule 205-3 under the Advisers Act permits registered investment advisers to charge a performance-based fee to "qualified clients." On February 15, 2012, the SEC adopted amendments to Rule 205-3.[15]

INCREASE IN DOLLAR AMOUNT THRESHOLDS

Under the rule, a qualified client includes a client whose net worth or assets under management by the adviser meet certain dollar thresholds. The amendments codify the order (Order) issued by the SEC on July 12, 2011.[16] Accordingly, the amended rules set the assets under management threshold to $1 million and the net worth test to $2 million. In addition, the SEC added a new provision to the rule which will require the SEC to issue an order every five years adjusting for inflation the dollar amount thresholds for the assets under management and net worth tests.

CALCULATION OF NET WORTH

A client's net worth is calculated only once, at the time the advisory contract is entered into. Under the new rules, consistent with changes that the SEC recently made under Regulation D,[17] the estimated fair market value of the person's primary residence is not included as an asset, and indebtedness secured by the primary residence up to such value is not included as a liability, in the calculation of a person's net worth. Therefore, the amount of any positive equity the person may have in his or her primary residence is not part of the net worth determination. However, the excess of debt secured by the primary residence over its estimated fair market value (i.e., "underwater mortgage") is included as a liability in the net worth calculation and reduces the person's net worth.

The new rules provide that if the amount of debt secured by the primary residence outstanding at the time the advisory contract is entered into exceeds the amount of such debt outstanding during the prior 60 days, the amount of the excess will be included as a liability reducing the net worth, even if the estimated value of the primary residence still exceeds the aggregate amount of debt secured by such primary residence. This provision aims to prevent the artificial inflation of the net worth by converting the home equity, which cannot be included in the net worth calculation, into other assets that can be added to the assets owned by the investor (for example, cash or other assets). The rule provides an exception to the 60-day look back provision, exempting debt that results from the acquisition of the primary residence from being viewed as a liability in the calculation of net worth.

The new rules related to the calculation of the net worth test will take effect on May 22, 2012.

TRANSITION RULES

Pursuant to the amended rules, the restrictions on performance fees apply only to new contractual arrangements and not to new investments by clients who previously met the definition of qualified client at the time they entered into an advisory contract with the investment adviser. Therefore, a client who met the $1.5 million net worth test in effect before the effective date of the Order and entered into an advisory contract with a registered investment adviser before that date, could continue to maintain and invest additional assets with the adviser.

Additionally, the amended rule provides that the Advisers Act provisions which generally prohibit a registered investment adviser from charging performance-based fees to clients, other than qualified clients, will not apply to contractual arrangements into which the registered investment adviser entered prior to registering with the SEC.

Finally, the rules allow for limited transfers from a qualified client to a non-qualified client. Specifically, the rules provide that an owner of an interest in a private investment company can transfer an interest by gift or bequest, or pursuant to an agreement related to legal separation or divorce to a non-qualified client. ■

SEC Issues Guidance on Registration of Affiliates of Investment Advisers

Recently, the SEC's Division of Investment Management staff (Staff) issued a no-action letter (2012 Letter) clarifying its views relating to the registration requirements of certain affiliates of registered investment advisers.[18] Specifically, the Staff addressed questions related to (i) registration of certain special purpose vehicles (SPVs) established by investment advisers, and (ii) multiple advisers conducting a single advisory business.

SPECIAL PURPOSE VEHICLES

The Staff reconfirmed its 2005[19] position that it would not recommend that the SEC take enforcement action against a registered adviser and a SPV created by such registered adviser if the SPV does not separately register as an investment adviser where the following conditions are met:

- the SPV is established by the investment adviser to a private fund to act as the private fund's general partner or managing member;
- the SPV's formation documents designate the investment adviser to manage the private fund's assets;
- all of the investment advisory activities of the SPV are subject to the Advisers Act, and the SPV is subject to examination by the SEC; and
- the registered adviser subjects the SPV, its employees, and persons acting on its behalf to the registered adviser's supervision and control such that each person is a person "associated with" the registered adviser, as defined by the Advisers Act.

The Staff also expanded its 2005 position in the 2012 Letter, explaining that its position was not limited to a registered adviser with a single SPV. Therefore an advisor with multiple SPVs can rely on the 2005 position. Additionally, the staff confirmed that an SPV with independent directors may rely on the 2005 position provided that those independent directors are the only persons acting on the SPV's behalf that the registered adviser does not supervise and control.

SINGLE ADVISORY BUSINESS

The 2012 Letter also addresses the circumstances under which it would be appropriate for multiple advisers to file a single registration application on Form ADV. Specifically, the Staff stated that an investment adviser may file a single Form ADV (filing adviser) on behalf of itself and each other adviser that is registering through such Form ADV and that is controlled by or under common control with the filing adviser (each, a relying adviser), if the filing adviser and the relying advisers collectively conduct a single advisory business.

(continued on page 6)

SEC Issues Guidance on Registration of Affiliates of Investment Advisers (continued from page 5)

The Staff further stated that, absent other facts suggesting that the advisers conduct different businesses, a single advisory business exists where:

- the advisers advise only private funds and separate accounts clients who are qualified clients under Rule 205-3 of the Advisers Act, and are otherwise eligible to invest in private funds advised by the advisers and whose accounts pursue investment objectives substantially similar or otherwise related to those private funds;
- each relying adviser, its employees, and the persons acting on its behalf are under the filing adviser's supervision and control such that each is a person "associated with" the filing adviser, as defined by Section 202(a)(17) of the Advisers Act;
- the filing advisers' principal office and place of business is in the United States, subjecting all advisers' client dealings to the Advisers Act, even dealings with non-U.S. clients;
- the advisory activities of each relying adviser are subject to the Advisers Act and its associated rules, and each relying adviser is subject to examination by the SEC;
- the filing adviser and each relying adviser operate under one code of ethics and a single set of written policies adopted pursuant to the Advisers Act, administered by a single chief compliance officer; and
- the filing adviser discloses in its Form ADV in the Miscellaneous Section of Schedule D that it and its relying advisers are filing a single Form ADV together in reliance on the Staff's guidance. The filing adviser must list each relying adviser in Section 1.B., Schedule D, of Form ADV, designating each a "relying advisor." ■

SEC Clarifies Large Trader Filing Requirement

Rule 13h-1 under the Exchange Act, which became effective October 3, 2011, requires all "large traders"[20] to file a Form 13H with the SEC promptly after effecting transactions that reach the prescribed trading activity level. Large traders are required to update their Form 13H on an annual basis within 45 days after the end of each full calendar year. The annual filing must show any changes to the information contained in Form 13H that have occurred during the applicable calendar year. The SEC staff has confirmed that large traders are not required to submit an annual filing for calendar year 2011. Therefore, large traders will need to submit their first annual filings for calendar year 2012 on or before February 14, 2013. ■

SEC COMMENT LETTER TRENDS

Are Your SEC Filings Being Monitored by the Office of Global Security Risk?

The Office of Global Security Risk[21] is an office under the SEC's Division of Corporation Finance that monitors companies' SEC filings and other available information to determine whether public companies are making appropriate disclosures about their activities relating to countries that have been designated as "State Sponsors of Terrorism."[22] This office has been active recently, issuing numerous comment letters in the last few months of 2011 alone.

In addition to specific inquiries regarding particular business operations, the comment letters also request a discussion of "the materiality of your contacts with Iran, Syria, Sudan and Cuba… and whether those contacts constitute a material investment risk… Various state and municipal governments, universities, and other investors have proposed or adopted divestment or similar initiatives regarding investment in companies that do business with U.S. designated state sponsors of terrorism. Your materiality analysis should address the potential impact of the investor sentiment evidenced by such actions toward companies that have operations associated with Iran, Syria, Sudan and Cuba." As there is no particular rule requiring public companies to disclose operations associated with identified state sponsors of terrorism, these requests for additional information seem to hinge on a liberal reading of the general duty to disclose material information that is necessary to make statements made in SEC filings, in the light of the circumstances under which they were made, not misleading.

Some of the comment letters appear to result not from a review of SEC filings, but from the SEC's independent review of websites. For example, one response letter stated "we understand from our discussions with the Commission that the SEC [comment] Letter was prompted by a statement on a website ("buyturkey.com"), which is operated by a third party with no affiliation to the Company…." In one comment letter, the SEC noted the company's website "includes Iran and Syria in its drop down menu for making a booking or getting a quote."

To the extent your company has any business operations associated with Iran, Syria, Sudan or Cuba, you should regularly review those operations and evaluate whether additional disclosure in your SEC filings is warranted. If you determine that additional disclosure is not warranted, it would be prudent to keep a record of your analysis and determination to facilitate a response to an inquiry from the Office of Global Security Risk. Furthermore, you may want to review your company's websites to remove outdated or extraneous references to Iran, Syria, Sudan and Cuba to avoid an unwarranted comment letter from the Office of Global Security Risk. ■

Senate and House Pass Bill Banning Insider Trading by Members of Congress

On February 2, 2012, and February 9, 2012, the Senate and House of Representatives, respectively, passed separate versions of the "Stop Trading on Congressional Knowledge Act" (STOCK Act) which addresses, among other matters, insider trading among certain members and employees of the federal government and the political intelligence community.[23]

Insider trading occurs when a person trades stocks or other securities on the basis of material, nonpublic information about the security or the issuer of the security in breach of a duty of trust or confidence, such as a duty to keep the information confidential.[24] With respect to information that a member of the federal government gains in the course of his or her official duties, it has been difficult to show that the member has a duty to keep that information confidential or other duty of trust or confidence that would preclude trading on the basis of the confidential information. The STOCK Act provides a framework for prohibiting specified members and employees of the federal government from trading on the basis of material, nonpublic information acquired in the course of their official duties. Under both the Senate and House bills, if enacted, the new law would:

- affirm that specified members and employees of the federal government are not exempt from insider trading prohibitions;
- require that various ethics committees and offices issue rules clarifying that specified members and employees of the federal government may not use nonpublic information derived from their positions with the federal government as a means of making a profit;
- provide that specified members and employees of the federal government owe an affirmative duty of trust and confidence to U.S. citizens, among others, regarding material, nonpublic information derived from the performance of their official responsibilities;
- require members and employees of Congress, as well as certain members and employees of the executive branch, including the President and Vice-President, to report to the appropriate ethics office the purchase, sale, or exchange of any stocks, bonds, commodities futures or other securities within 30 days after the transaction in the Senate bill, and within 30 days after learning of the transaction but in no case more than 45 days after the transaction in the House bill. The reporting requirements do not apply to transactions involving "widely held investment funds," such as mutual funds;
- require the creation of publicly accessible, searchable online systems for disclosed financial reports; and
- require the Comptroller General to submit a report within one year on the sale of political intelligence (i.e. information derived from certain executive or legislative branch officials for use in analyzing securities or commodities markets).

The Senate bill includes additional provisions addressing political intelligence consultants,[25] requiring organizations dealing in political intelligence to:

- register with the federal government upon making one or more political intelligence contacts. The provision is more stringent than similar provisions in the Lobbying Disclosure Act which require registration only if an employee makes more than one federal lobbying contact for a client and devotes 20% or more of his or her time to federal lobbying activities for the client in a 3-month period; and
- submit semiannual reports identifying their clients and the issues for which they engaged in political intelligence activities.

The bills will be sent to conference for reconciliation. If enacted, the STOCK Act should affirmatively establish the basis for prohibiting members of Congress and other high level federal employees from profiting based on material, nonpublic information during the course of their official duties under generally applicable securities laws. In addition, it should lead to enhanced disclosure of the activities of the political intelligence community. ■

ENDNOTES

1. Partial Amendment No. 1 and FINRA's Response Letter are available at http://www.finra.org/Industry/Regulation/RuleFilings/2011/P124600.
2. *See* Notice of Filing of Partial Amendment No. 1 and Order Instituting Proceedings to Determine Whether to Approve or Disapprove a Proposed Rule Change, as modified by Partial Amendment No. 1, to Adopt FINRA Rule 5123 (Private Placements of Securities), Exchange Act Release No. 66203 (Jan. 20, 2012), *available at* http://www.sec.gov/rules/sro/finra/2012/34-66203.pdf.
3. *See Cybersecurity Risk Disclosure,* Up to Date: Current Developments in Securities Laws (Oct. 2011), *available at* http://www.blankrome.com/index.cfm?contentID=37&itemID=2610.
4. *See SEC Staff Provides Guidance on Disclosures Regarding European Sovereign Debt Exposures,* Up to Date: Current Developments in Securities Laws (Jan. 2012), *available at* http://www.blankrome.com/index.cfm?contentID=37&itemID=2716.
5. *See SEC Adopts Mine Safety Disclosure Rules,* Up to Date: Current Developments in Securities Laws (Jan. 2012), *available at* http://www.blankrome.com/index.cfm?contentID=37&itemID=2716.
6. *See The Status of Proxy Access,* Up to Date: Current Developments in Securities Laws (Sept. 2011), *available at* http://www.blankrome.com/index.cfm?contentID=37&itemID=2590.
7. *See SEC Staff Issues Staff Legal Bulletin on Shareholder Proposals,* Up to Date: Current Developments in Securities Laws (Nov./Dec. 2011), *available at* http://www.blankrome.com/index.cfm?contentID=37&itemID=2674.
8. Companies that qualified as "smaller reporting companies" as of January 21, 2011, and newly public companies that qualify as smaller reporting companies after January 21, 2011, will not be subject to "say-on-pay" and "frequency of say-on-pay" votes until the first meeting of shareholders at which directors will be elected occurring on or after January 21, 2013.
9. *See Get Ready, Get Set – What Public Companies Can Do to Prepare for the 2011 Proxy Season* by Jane Storero and Yelena Barychev, The M&A Lawyer, November/December 2010, Volume 14, Issue 10.
10. *See* ISS, *2012 US Compensation Policy,* Frequently Asked Questions (Jan. 25, 2012), *available at* http://www.issgovernance.com/policy/2012/USCompensationFAQ.
11. NYSE Information Memo 12-4, *available at* http://www.nyse.com/nysenotices/nyse/information-memos/detail;jsessionid=7FBEDD0436D23D437A8E761210DD5D65?memo_id=12-4.
12. *See ISS Updates Its Proxy Voting Guidelines,* Up to Date: Current Developments in Securities Laws (Nov./Dec. 2011), *available at* http://www.blankrome.com/index.cfm?contentID=37&itemID=2674.
13. *See ISS Issues White Paper on Pay for Performance Alignment,* Up to Date: Current Developments in Securities Laws (Jan. 2012), *available at* http://www.blankrome.com/index.cfm?contentID=37&itemID=2716.
14. *See Foreign Issuer Reporting Enhancements,* SEC Release No. 33-8959 (Sept. 23, 2008), *available at* http://www.sec.gov/rules/final/2008/33-8959.pdf.
15. Investment Adviser Performance Compensation (Release No. IA-3372), *available at* http://www.sec.gov/rules/final/2012/ia-3372.pdf.
16. Since 1998, qualified clients under Rule 205-3 have included clients who have assets under management with the adviser of $750,000 or more, and clients who have a net worth of $1.5 million or more. Dodd-Frank, signed into law on July 21, 2010, directed the SEC to adjust the dollar thresholds included in the qualified client definition for inflation within one year of the date of enactment, and every five years thereafter. Accordingly, on July 12, 2011, the SEC issued an order approving adjustments to the dollar thresholds in Rule 205-3 under the Advisers Act. Pursuant to such order, the $750,000 million assets under management test was increased to $1 million and the $1.5 million net worth test was increased to $2 million. The order was effective as of September 19, 2011.
17. *See SEC Adopts Amendments to Net Worth Standard for Accredited Investors,* Up to Date: SEC News (Jan. 2012), *available at* http://www.blankrome.com/index.cfm?contentID=37&itemID=2716.
18. *See* American Bar Association, Business Law Section, No-Action Letter (Jan. 18, 2012), *available at* http://www.sec.gov/divisions/investment/noaction/2012/aba011812.htm.
19. *See* American Bar Association Subcommittee on Private Investment Entities, No-Action Letter (Dec. 8, 2005), *available at* http://www.sec.gov/divisions/investment/noaction/aba120805.htm.
20. Rule 13h-1 defines a "large trader" as any person that (i) directly or indirectly, including through other persons controlled by such person, exercises investment discretion over one or more accounts and effects transactions for the purchase or sale of any NMS security for or on behalf of such accounts, by or through one or more registered broker-dealers, in an aggregate amount equal to or greater than 2 million shares or shares with a fair market value of $20 million during any calendar day, or 20 million shares or shares with a fair market value of $200 million during any calendar month; or (ii) voluntarily registers as a large trader with the SEC.
21. The genesis of the Office of Global Security Risk is in the Conference Report accompanying the Consolidated Appropriations Act, 2004, Pub. L. 108-199.
22. The Secretary of State has the power to designate "State Sponsors of Terrorism." Currently, Iran, Sudan, Syria and Cuba are so designated.
23. *See* S. 2038, 112th Cong. (as passed by Senate, Feb. 2, 2012), *available at* http://www.gpo.gov/fdsys/pkg/BILLS-112s2038es/pdf/BILLS-112s2038es.pdf; S. 2038, 112th Cong. (as amended and passed by the House of Representatives, Feb. 9, 2012), *available at* http://www.gpo.gov/fdsys/pkg/BILLS-112s2038eah/pdf/BILLS-112s2038eah.pdf.
24. *See* 17 C.F.R. §240.10b5-2(b)(1). The insider trading laws can also be breached in other ways, such as by providing confidential information to another so that person may trade on the basis of the information.
25. Political intelligence is defined by the Act as information derived by a person from direct communication with an executive branch employee, a member of Congress, or an employee of Congress and provided in exchange for financial compensation to a client who intends, and who is known to intend, to use the information to inform investment decisions.

QUESTIONS: If you have a question regarding the issues raised in this newsletter, you may obtain additional guidance from the authors and other members of our Public Companies Group.

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