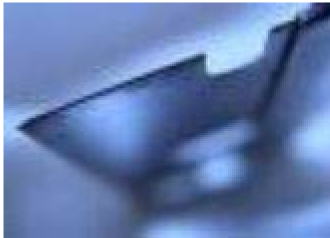
Razor Alert



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Financial Services Update

This Razor Alert incorporates recent developments in the financial services area:

- Short Sales in the EU and US
- US Financial Services Legislative Proposals
- Regulation of Consumer Credit
- Investment Advice
- Securitization
- Compensation

Short Sales in the EU and US

SEC Approves Short Selling Restrictions

The SEC adopted a new rule to restrict short selling when a stock is experiencing significant downward price pressure to promote market stability and preserve investor confidence. This alternative uptick rule is designed to restrict short selling from further driving down the price of a stock that has dropped more than 10 percent in one day. It will enable long sellers to stand in the front of the line and sell their shares before any short sellers once the circuit breaker is triggered.

Once the stock has triggered a circuit breaker by experiencing a price decline of at least 10 percent in one day, short selling would be permitted if the price of the security is above the current national best bid.

New Regulatory Approaches to Short Selling in the EU

Changes in the regulatory approach to the short selling of listed securities have recently been announced in the EU. In the EU, a new regulatory proposal would (to the extent adopted by the EU member states) require private disclosure of net short positions above a 0.2% threshold to the applicable regulator, and public disclosure to the market of such positions above a 0.5% threshold.

US Financial Services Legislative Proposals

Treasury Proposes "Volcker Rule" Legislative Text

The Department of the Treasury released proposed legislative text to implement the "Volcker Rule" announced by the Obama Administration on January 21st. Treasury's proposal, which takes the form of new sections 13 and 13a of the Bank Holding Company Act of 1956, includes: (1) a Prohibition on Proprietary Trading; (2) a Prohibition on Sponsoring or Investing in Private Equity or Hedge Funds; (3) Limitations on Transactions or Relationships with "Advised" Private Equity or Hedge Funds; (4) Capital and Quantitative Limitations for Certain Nonbank Financial Companies; (5) a Concentration Limit on Large Financial Firms; and (6) Rulemaking Authority to Carry-out Entire Section granted to the appropriate Federal banking agencies.

New "PROP Trading Act" Would Expand "Volcker" Prohibitions

Senators Merkley (D-OR) and Levin (D-MI) proposed a bill that would expand the prohibitions on proprietary trading and certain asset management activities recently proposed by the Administration. Aspects of the bill include: (1) expanded coverage including (i) no express exemption for customer-related trading, market-making, or hedging and (ii) exemptions must be granted by the Fed and FDIC; (2) could extend to broker-dealers and private equity or hedge fund managers that are not affiliated with banks; (3) self-executing; (4) potentially destabilizing in that it requires covered financial companies to shed prohibited businesses within two years of the bill's enactment; (5) no size limits on financial institutions; and (6) provides new limits on securitizations.

Restoring American Financial Stability bill summary

Highlights of the new bill proposed by Senator Dodd include: (1) consumer protections with authority and independence by creating a new independent watchdog tasked with ensuring consumer protections; (2) ending too big to fail by: (i) creating a safe way to liquidate failed financial firms; (ii) imposing new capital and leverage requirements that make it undesirable to get too big; (iii) updating the Fed's authority to allow system-wide support but no longer prop up individual firms; and (iv) establishing rigorous standards and supervision to protect the economy and consumers, investors, and businesses; (3) advanced warning system by creating a council to identify and address systemic risks posed by complex companies, products, and activities; (4) exotic instrument transparency and accountability by eliminating exceptions that allow certain practices to go on unnoticed and unregulated - including exceptions for over-the-counter derivatives, asset-backed securities, hedge funds, mortgage brokers and payday lenders; (5) streamlining federal bank supervision; (6) providing shareholders with a non-binding vote on executive compensation and new input with a say on pay and corporate affairs; (7) providing new rules for credit rating agencies; and (8) strengthening rules on oversight by empowering regulators to enforce existing regulations.

The Restoring American Financial Stability Act introduced by Senator Dodd includes: institutional arrangements; systemic regulation; bank holding company act amendments; resolution (orderly liquidation) authority; emergency financial stabilization powers; federal reserve governance; bureau of consumer financial protection; derivatives; credit retention requirements; payment, clearance, and settlement; changes in broker-dealer regulation and investor protection; corporate governance; executive compensation; insurance; hedge fund registration; and credit rating agencies.

Regulation of Consumer Credit

FED Proposes Clarifications to its final rules under Regulation E and Regulation DD

The Federal Reserve Board proposed clarifications to its Regulation E (Electronic Fund Transfers) and Regulation DD (Truth in Savings) pertaining to overdraft services to clarify that the prohibition in Regulation E on assessing overdraft fees without the consumer's affirmative consent applies to all institutions, including those with a policy and practice of declining automated teller machine (ATM) and one-time debit card transactions when an account has insufficient funds.

Sweeping New Credit CARD Act Rules to Protect Consumers Took Effect

Recently, new credit card protections came into place when major provisions of Credit CARD Act took effect. These provisions will stop unfair interest rate hikes and changes in terms, prohibit exorbitant and unnecessary fees, defend the rights of responsible credit card users, and protect young consumers against aggressive credit card solicitations. They include new rules on: (1) timing of interest rate hikes; (2) clarity of billing and change of terms statements; (3) bill delivery and payment allocation; (4) fee amounts; and (5) applicants under 21.

Fed Proposes Rule Amendment for Regulation Z (Truth in Lending)

The Fed proposed a rule amending Regulation Z (Truth in Lending) to protect credit card users from unreasonable late payment and other penalty fees and to require credit card issuers to reconsider increases in interest rates. The proposed rule would: (1) prohibit credit card issuers from charging penalty fees that exceed the dollar amount associated with the consumer's violation of the account terms; (2) ban inactivity fees, such as fees based on the consumer's failure to use the account to make new purchases; (3) prevent issuers from charging multiple penalty fees based on a single violation of the account terms; (4) require credit card issuers to inform consumers of the reasons for increases in rates; and (5) require issuers that have increased rates since January 1, 2009 to re-evaluate such increases.

Investment Advice

Proposed Regulation to Increase Workers' Access to High Quality Investment Advice

The Pension Protection Act of 2006 (PPA) amended the Employee Retirement Income Security Act of 1974 (ERISA) to create a new statutory exemption from the prohibited transaction rules to expand the availability of investment advice to participants in 401(k)-type plans and individual retirement accounts (IRAs). The Department of Labor has published a proposed rule that allows investment advice to be given under the statutory exemption in two ways: (1) through the use of a computer model pre-certified as unbiased and (2) through an adviser compensated on a "level-fee" basis (i.e., fees do not vary based on investments selected by the participant). Several other requirements also must be satisfied, including disclosure of fees the adviser is to receive. The proposed rule will implement the PPA provisions and make investment advice more accessible for millions of Americans in 401(k) type plans and individual retirement arrangements (IRAs).

Securitization

FDIC Approves an Extension Regarding the Safe Harbor Protection for Securitizations

The FDIC approved an extension through September 30, 2010 of the Safe Harbor Protection for Treatment by the FDIC as Conservator or Receiver of Financial Assets Transferred by an Insured Depository Institution in Connection With a Securitization or Participation. Under this safe harbor, all securitizations or participations in process through September 30, 2010 are permanently grandfathered under the existing terms of 12 C.F.R. Part 360.6. When a safe harbor was initially adopted in 2000 for securitizations and participations, the FDIC provided important protections for securitizations and participations by confirming that in the event of a bank failure, the FDIC would not try to reclaim loans transferred into such transactions so long as an accounting sale had occurred. However, on June 12, 2009, the Financial Accounting Standards Board ("FASB") finalized modifications to the accounting treatment for such transactions through Statement of Financial Accounting Standards No. 166, *Accounting for Transfers of Financial Assets, an Amendment of FASB Statement No. 140* ("FAS 166") and Statement of Financial Accounting Standards No. 167, *Amendments to FASB Interpretation No. 46(R)* ("FAS 167"). Following the November 15, 2009 effective date of these changes, most securitizations no longer meet the off-balance sheet standards for sale accounting treatment and, as a result, no longer comply with the preconditions for the application of the original FDIC safe harbor.

Compensation

Draft UK Rules on Pay Disclosure for Top Earners at Banks

The UK published draft new rules that will require the annual public disclosure by large banks and building societies of an "executives' remuneration report." The new rules would, amongst other things, require the annual disclosure of the number of employees within pay bands starting at £500,000 to £1,000,000. They would only apply to a bank (including any associated company providing services to the bank) with more than 1000 employees provided that the bank (either alone or together with its corporate group members where most of the group's activities are financial services activities) also has more than £100 billion of assets on its balance sheet. The draft rules implement proposals to give shareholders more power and information to shape remuneration policies at banks. The rules would require an annual executives' remuneration report to be posted on the internet, with a copy sent to each shareholder. In addition, any bank on the main market of the London Stock Exchange would need to seek shareholder approval of the report by majority vote at its annual general meeting.