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DEVELOPMENTS OF NOTE

Federal District Court Grants in Part and Denies in Part Motion to Dismiss ERISA Class Action Claims Challenging Bank's Inclusion of Company Stock in its Retirement Plans

In *Wilson v. Venture Fin'l Group, Inc., et al.*, Case No. 09-5768, 2010 WL 2028088 (W.D. Wash. May 18, 2010), the U.S. District Court for the Western District of Washington granted in part and denied in part a motion to dismiss ERISA breach of fiduciary duty claims involving a bank's inclusion of a company stock fund in its retirement plans.

Plaintiffs, former employee participants in employee stock ownership plans sponsored by their employer bank, filed a class action suit seeking to hold plan fiduciaries liable for alleged losses incurred when the bank's share value fell as a result of alleged unsound banking practices. Plaintiffs in their complaint alleged, among other things, that plan fiduciaries breached their duties of loyalty and prudence under ERISA by (1) continuing to offer the bank's stock given known financial challenges facing the bank, and (2) failing to divest the plans of their holdings in the stock. The complaint named as defendants the bank, its board of directors, and the plans' administrators and trustees.

DIVESTITURE

Plaintiffs in their complaint alleged that defendants had a responsibility to divest the plans of company stock if it became or remained imprudent. Defendants moved to dismiss this claim on the ground that the divestiture was impossible because the bank's stock was not publicly traded, and there was no readily available market for the bank's stock. The court granted defendants' motion to dismiss on the divestiture issue on the ground that plaintiffs failed to allege facts sufficient to establish that defendants could have divested the stock held by the plans even if they wanted to. The court also rejected plaintiffs' assertion that defendants had a "heightened" responsibility to divest where the plans were

overwhelmingly invested in company stock, noting that such a claim was nothing more than a claim for diversification, and that ERISA § 404(a)(2) exempts investments in qualifying employer stock from ERISA's duty to diversify.

CONTINUING TO HOLD AND OFFER STOCK

The court denied defendants' motion to dismiss plaintiffs' claim that it was a breach of duty for plan fiduciaries to permit the plans to continue to hold bank stock where an FDIC investigation of the bank allegedly revealed unsound banking practices. The court held that, while divestiture was not an option under the allegations as pleaded, continuing to hold and purchase stock may have been imprudent if, as plaintiffs alleged, plan fiduciaries were aware that the bank faced the alleged financial crisis. In short, this decision held that under plaintiffs' allegations, while defendants did not have the ability to divest, they did have the choice not to offer more of the stock to the plans.

OTHER CLAIMS

The court also denied the motions to dismiss plaintiffs' claims based on the alleged failure to monitor the performance of appointed fiduciaries and failure to disclose information regarding the soundness of investment in the bank stock, as well as claims for alleged co-fiduciary liability.

CESR Issues Guidelines Relating to a Common Definition of a Money Market Fund

The Committee of European Securities Regulators ("CESR") recently issued guidelines (the "Guidelines") relating to any European fund that calls itself or markets itself as a "money market fund." The Guidelines cover both a UCITS fund (a fund that complies with the requirements of the European directives relating to "Undertakings for Collective Investment in Transferrable Securities") and a non-UCITS fund regulated under a national law of a European Union member state. Currently, there is no commonly accepted definition in Europe of what constitutes a money market fund. Commission Directive 2006/73/EC (commonly known as the "MiFID Level 2 Directive") provides for a "qualifying money market fund." Under that directive an investment firm may deposit client funds in a qualifying money market fund for the purpose of safeguarding those funds. The Guidelines on the other hand are intended to ensure that money market funds meet investor expectations. As a result, the adoption by CESR of the Guidelines is roughly equivalent to the SEC's adoption in 1983 of Rule 2a-7 under the Investment Company Act of 1940. Although CESR guidance does not have legal status, as a practical matter, all European securities regulators apply CESR guidance.

The Guidelines describe a two-tiered approach consisting of a "Short-Term Money Market Fund" and a "Money Market Fund." The critical distinction between a Short-Term Money Market Fund and a Money Market Fund is that a Short-Term Money Market Fund may purchase and sell its shares using a stable share price, but a Money Market Fund may not. This two-tier approach was recommended to the SEC by the Committee on Federal Regulation of Securities, Section of Business Law, American Bar Association (the "ABA") in its September 8, 2009 letter commenting on amendments to Rule 2a-7 proposed by the SEC in June 2009. ([John Hunt](#) of Goodwin Procter participated in drafting that comment letter.)

CRITERIA APPLICABLE TO SHORT-TERM MONEY MARKET FUNDS AND MONEY MARKET FUNDS

The Guidelines specify the following criteria for both types of money market funds:

- A fund must have as its primary investment objective maintaining the fund's principal, and must aim to provide a return in line with money market rates.
- If the fund is a UCITS fund, it must invest in money market instruments, as described in the "UCITS IV" Directive (2009/65/EC), or deposits with credit institutions. (Under the UCITS IV Directive, money market instruments are defined as instruments normally dealt in on a money market, that are liquid and which have a value that may be accurately determined at any time, and they typically would include treasury and local authority bills, certificates of deposit, commercial paper, medium-term notes and bankers' acceptances.) If the fund is a non-UCITS fund, the portfolio must meet equivalent liquidity and valuation standards.
- A fund must invest in instruments that are "of high quality," as determined by the fund's management company, with such determination to consider, among other things, (a) the credit quality of the instrument (generally, it must be rated in one of the two highest ratings categories by each recognized credit rating agency that has rated the security, or if unrated be of equivalent quality), (b) the nature of the asset class represented by the instrument, (c) for structured financial instruments, the operational and counterparty risk inherent in the structured financial transaction, and (d) the liquidity profile.
- A fund must provide daily net asset value and share prices calculations.
- A fund must not take any direct exposure to equity securities or commodities, including by the use of derivatives, and the fund only may use derivatives in line with its investment strategy or for currency hedging with respect to non-base currency securities.
- A fund must disclose in its prospectus and, in the case of a UCITS fund, its "key information document," whether the fund is a Short-Term Money Market Fund or a Money Market Fund.
- A fund must provide appropriate information to investors on its risk-reward profile so investors can identify specific risks that are linked to the fund's investment strategy.

SHORT-TERM MONEY MARKET FUND CRITERIA

To qualify as a Short-Term Money Market Fund, a fund generally must:

- Limit its investments in securities to those with a residual maturity until the legal redemption date (*i.e.*, the date when the fund's management company may be assured that full payment will have been received) of no more than 397 days; and
- Ensure that its portfolio weighted average maturity is no more than sixty days, and its portfolio weighted average maturity life is no more than 120 days.

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MONEY MARKET FUND CRITERIA

To qualify as a Money Market Fund, a fund generally must:

- Limit its investment in securities to those with a residual maturity until the legal redemption date of no more than two years, provided that the time remaining until the next interest rate reset date is no more than 397 days, and any floating rate securities should reset to a money market rate or index; and
- Ensure that its portfolio weighted average maturity is no more than six months, and its portfolio weighted average maturity life is no more than twelve months.

In addition, a Money Market Fund may acquire any “sovereign issuance” (*i.e.*, any money market instrument issued or guaranteed by a central, regional or local authority or central bank of a member state, the European Central Bank, the European Union or the European Investment Bank) if the sovereign issuance is at least investment grade quality, notwithstanding the general requirement that a fund’s investments must be of high quality.

COMPLIANCE DATES

The Guidelines take effect on July 1, 2011. A money market fund created after July 1, 2011 will have to comply with the Guidelines immediately. A money market fund created on or before July 1, 2011 generally must comply with the Guidelines’ prospectus and, if applicable, the Guidelines’ key information document disclosure requirements, by that date, and is allowed a six-month transitional period with respect to investments acquired on or before July 1, 2011.

OTHER ITEM OF NOTE

Client Alert Regarding Changes to House “Carried Interest” Legislation Proposed in Senate Deliberations

Goodwin Procter’s Tax Practice has issued a [Client Alert](#) discussing an amendment introduced in the Senate during its consideration of H.R. 4213, the House bill containing changes to the taxation of “carried interest.” The proposed amendment offers more favorable treatment of carried interest than the House bill.