

FINANCIAL SERVICES ALERT

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DEVELOPMENTS OF NOTE

Chambers USA: America's Leading Lawyers for Business [has recognized Goodwin Procter](#) for excellence in numerous practice area categories in its 2009 edition and 99 of the firm's attorneys have been named as leading lawyers. We are delighted to announce that many of these lawyers come from our integrated Financial Services practice, including Banking, Investment Management, Hedge Funds and Consumer Financial Services. The Financial Services practice was honored nationally in Investment Funds, including the sub-categories of Hedge Funds and Registered Funds, Financial Services Regulation, and Privacy & Data Security. On the state level, Goodwin Procter was selected for excellence in Massachusetts Banking & Finance: Corporate & Regulatory, as well as Hedge & Mutual Funds.

Treasury Proposes Executive Compensation Reforms; FRB General Counsel Testifies on Proposed Reforms

Executive Compensation Principles. Treasury Secretary Geithner last week released a statement regarding compensation reform that is intended to better align compensation practices with sound risk-management, long-term growth and value creation. His statement outlined a set of broad-based principles that he expects to evolve over time:

- Compensation plans should properly measure and reward performance;
- Compensation should be structured to account for the time horizon of risks;
- Compensation practices should be aligned with sound risk management;
- Golden parachutes and supplemental retirement packages should be reexamined to determine if they align the interests of executives and shareholders; and

- Transparency and accountability in the process of setting compensation should be promoted.

Secretary Geithner also stated that the Obama Administration intends to work with Congress to pass legislation in two specific areas. First, the Administration supports efforts in Congress to pass so-called “say on pay” legislation, which would give the SEC authority to require public companies to provide for a non-binding shareholder vote on executive compensation packages. Under this proposed legislation, all public companies would be required to include in their annual proxy statements a non-binding shareholder resolution requesting approval or disapproval of the compensation for the top five named executive officers disclosed in the proxy. With respect to proxy materials related to a merger or other change in control transaction, shareholders would have the right to cast a non-binding vote to approve or disapprove golden parachute payments disclosed in the proxy materials. Although the shareholder votes under the proposed legislation would not be binding on the board, it is believed that the mere prospect of the vote would cause directors to consider more carefully shareholder interests when setting executive compensation.

Second, the Administration intends to propose legislation giving the SEC the power to ensure that compensation committees are more independent, adhering to standards similar to those put in place for audit committees as part of the Sarbanes-Oxley Act. Compensation committees would also be given the authority and the financial resources to hire their own independent compensation consultants and outside legal counsel. Compensation committees would be directly responsible for the appointment, compensation, retention and oversight of any compensation consultants it retained, and the compensation consultants would report directly to the compensation committee. Additionally, the proposed legislation would direct the SEC to establish standards to ensure the independence of compensation consultants and outside legal counsel used by the compensation committee.

Interim Final Rule for TARP Recipients. The Treasury also released an interim final rule on compensation and corporate governance standards for TARP recipients (the “Interim Final Rule”). The Interim Final Rule implements the executive compensation restrictions of the American Recovery and Reinvestment Act of 2009 and completely revises 31 CFR part 30, which contains the current executive compensation rules for TARP recipients. Next week’s edition of the *Alert* will have further discussion of the Interim Final Rule.

FRB Testimony. In conjunction with the Treasury’s proposals, Scott Alvarez, General Counsel of the FRB, testified before the House Financial Services Committee on executive compensation in banking and financial services. Mr. Alvarez stated that compensation arrangements at many financial institutions created incentives to take excessive risk and that in some cases these incentives were powerful enough to overcome regulatory risk control processes. He said that correcting these weaknesses will require improvements in both corporate governance and risk management at financial institutions. These improvements will need to be implemented for both top management and business-line employees. Mr. Alvarez further stated that the FRB is working on enhanced guidance on compensation practices at U.S. banking organizations. Mr. Alvarez recommended that to better align compensation practices with safety and soundness financial institutions should conduct a broad review of compensation practice and make compensation more sensitive to risk. He asserted that risk controls are a necessary complement to prudent compensation systems and that an institution’s board should take a more informed and active hand in compensation.

FASB Amends Asset Transfer Rules; FRB and ABA React

FASB. The Financial Accounting Standards Board (“FASB”) finalized two Statements, Nos. 166 and 167, that will affect the ability of an institution to effectively transfer assets off of its balance sheet to a deconsolidated entity. In each case, the amendments will become effective as of the beginning of the reporting entity’s first annual reporting period that begins after November 15, 2009. Earlier application is not permitted.

Statement 167: Statement 167 amends FASB Interpretation No. 46(R), *Consolidation of Variable Interest Entities*. Historically, a reporting company had to consolidate a variable interest entity (“VIE”) if, from a quantitative perspective, it was the primary beneficiary of the VIE (*i.e.*, it absorbed a majority of the VIE’s losses, received a majority of its residual returns, or both). Statement 167 amends that standard by requiring the reporting entity to also perform a qualitative analysis that results in a VIE being consolidated if the reporting entity: (1) has the power to direct activities of the VIE that significantly impact the VIE’s financial performance, and (2) has an obligation to absorb losses or receive benefits that may be significant to the VIE. In making the first evaluation, the reporting entity must consider whether it has an implicit financial obligation to ensure that the VIE operates as intended.

Statement 167 also requires more ongoing reassessments as to whether a reporting entity must consolidate a VIE. Statement 167 further requires enhanced reporting, including of the reporting company’s significant judgments and assumptions as to whether a VIE must be consolidated, and how involvement with a VIE (*e.g.*, because of restrictions on a consolidated VIE’s assets) affects the reporting company’s financial statements. The disclosure requirements in Statement 167 replace (but generally are consistent with) those in FASB Staff Position FAS 140-4 and FIN 46(R)-8, *Disclosures by Public Entities (Enterprises) about Transfers of Financial Assets and Interests in Variable Interest Entities*.

Statement 166: Statement 166 principally amends FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*. Statement 166 eliminates the concept of a qualifying “special-purpose entity” (“SPE”), alters the requirements for transferring assets off of the reporting company’s balance sheet, requires additional disclosure about a transferor’s involvement in transferred assets, and eliminates special treatment of guaranteed mortgage securitizations.

As to SPEs, Statement 166 removes the SPE exemption from consolidation in FASB 46(R), which historically has enabled entities that transfer assets to a qualifying SPE to definitively remove these assets from their balance sheets. As to altering the derecognition of assets requirements, Statement 166 limits the circumstances under which an asset, or portion of an asset (referred to as a “participating interest” in Statement 166), can be derecognized when the transferor has not transferred the entire asset to a non-consolidated entity, or has a continuing involvement with the asset. For example, a transfer of part of a financial asset only can be derecognized only if, among other things, the transferred portion is a pro-rata portion of the whole asset, and no portion is subordinate to another.

As to disclosures, Statement 166 requires additional information to be presented about a variety of forms of continuing involvement by a transferor with an asset, including recourse arrangements, guarantee arrangements, and servicing arrangements. The transferor also must report gains and losses from asset transfers during each period. Finally, as to guaranteed mortgage securitizations, Statement 166 eliminates the special provisions

regarding such assets in Statement 140 and Statement No. 65, *Accounting for Certain Mortgage Banking Activities*, resulting in guaranteed mortgage securitizations being treated like any other asset for purposes of the derecognition provisions described above.

FRB. The FRB issued a release to bank holding companies (“BHCs”) and state member banks in which the FRB noted that the FASB’s publication of Statements 166 and 167, when they become effective in 2010, will have a material effect on BHCs’ and banks’ off-balance sheet vehicles, *e.g.*, those used in connection with securitization transactions. The FRB noted that Statements 166 and 167 are designed to address weaknesses in accounting and disclosure standards for off-balance sheet vehicles.

The FRB stated that it “is reviewing regulatory capital requirements associated with [Statements 166 and 167].” As part of that review, the FRB stated that it is considering a number of matters, including the maintenance of prudent capital levels, the performance of off-balance sheet vehicles during the recent economic downturn, and information garnered from the recent “stress tests” of certain major financial institutions concerning capital requirements and the performance of off-balance sheet vehicles. Finally, the FRB urged BHCs and banks to take into account the impact of Statements 166 and 167 in conducting their internal capital planning initiatives.

ABA. Separately, in a letter to the FRB and other federal bank regulatory agencies (the “Agencies”), the American Bankers Association urged the Agencies to soften the regulatory capital impact of Statements 166 and 167 by, among other things, adopting a three-year transition period for changes to the regulatory rules related to Statements 166 and 167 and imposing no changes to the regulatory requirements for the first year.

SEC Issues Release for Proxy Rule Amendments Relating to Shareholder Nomination of Directors

The SEC voted to propose amendments to the proxy rules under the Securities Exchange Act of 1934 (the “1934 Act”) that would facilitate shareholder nomination of directors. The proposed amendments would also revise Rule 14a-8 under the 1934 Act, principally to require an issuer’s proxy materials to include a shareholder proposal that would amend, or request an amendment to, an issuer’s governing documents regarding nomination procedures or disclosures related to shareholder nominations. This article describes the main features of the SEC’s proposal, which includes several features specific to registered investment companies.

Shareholder Nominations. Proposed Rule 14a-11 under the 1934 Act would require an issuer to include a shareholder nominee or nominees for director in an issuer’s proxy materials and form of proxy (collectively, “proxy materials”) if certain conditions were met. The proposed rule would apply to all issuers subject to the proxy rules, including investment companies, except for issuers subject to the proxy rules solely because they have a class of debt registered under Section 12 of the 1934 Act.

Shareholder Nominations Prohibited by State Law/Governing Documents. Proposed Rule 14a-11 would not apply if state law or an issuer’s governing documents prohibit shareholders from nominating directors. (The release proposing the amendments (the “Proposing Release”) notes that the SEC is unaware of any such law. If an issuer’s governing documents prohibited shareholder nominations, under the proposed amendments to Rule 14a-8, discussed below, a

shareholder could submit a proposal for inclusion in the issuer's proxy materials to remove the prohibition.) State law or an issuer's governing documents could provide for rights in addition to those proposed, *i.e.*, they could allow an issuer to include in its proxy materials nominees put forward by shareholders who would not be eligible to rely on proposed Rule 14a-11.

Shareholder Eligibility – Share Ownership. Under Proposed Rule 14a-11, a shareholder wishing to nominate a director or directors for inclusion in an issuer's proxy materials would need to meet a minimum ownership threshold. A shareholder would also have to meet requirements relating to period and purpose of ownership. Shareholders would be eligible to have their nominee included in the proxy materials if:

- They own at least 1 percent of the voting securities of a “large accelerated filer” (generally, a company with a worldwide market value of \$700 million or more) or of a registered investment company with net assets of \$700 million or more.
- They own at least 3 percent of the voting securities of an “accelerated filer” (generally, a company with a worldwide market value of \$75 million or more but less than \$700 million), or of a registered investment company with net assets of \$75 million or more but less than \$700 million.
- They own at least 5 percent of the voting securities of a non-accelerated filer (generally, a company with a worldwide market value of less than \$75 million) or of a registered investment company with net assets of less than \$75 million.

In addition,

- Shareholders would be able to aggregate holdings to meet applicable thresholds if acting as a shareholder group. (As a consequence, when this article refers to a nominating shareholder, it should also generally be read to refer to a nominating shareholder group.)
- Shareholders would be required to have held their shares for at least one year.
- Shareholders would be required to sign a statement declaring their intent to continue to own their shares through the shareholder meeting at which directors are to be elected.
- Shareholders would be required to certify that they are not holding their stock for the purpose of changing control of the issuer, or to gain more than minority representation on the board of directors.

In the case of a registered investment company, other than a series company, the ownership threshold would be calculated based on the company's net assets as of the end of the second fiscal quarter in the fiscal year immediately preceding the fiscal year of the shareholder meeting, as disclosed in Form N-CSR. Because their series may not share the same fiscal year end, series investment companies would provide information for determining the share ownership threshold by filing Form 8-K within four business days after determining the anticipated shareholder meeting date. The Form 8-K filing would disclose a series investment company's net assets

as of June 30 of the calendar year immediately preceding the calendar year of the meeting and the total number of shares entitled to vote for the election of directors at the meeting as of the end of the most recent calendar quarter. A nominating shareholder would have to meet the share ownership requirements of proposed Rule 14a-11 at the time the shareholder files the notice on Schedule 14N required under the proposed rule, as discussed below.

Schedule 14N. A shareholder would have to provide the issuer and the SEC with a notice on proposed Schedule 14N in order to nominate a director in reliance on Rule 14a-11. The Schedule 14N filing would include disclosure about the amount and percentage of securities owned by the nominating shareholder and length of ownership, and the nominating shareholder would have to certify, among other things, that the nominating shareholder (a) intended to continue to hold the securities through the date of the meeting and (b) was not seeking to change the control of the company or to gain more than a limited number of seats on the board of directors. The nominating shareholder would have to make a statement in Schedule 14N regarding its intent with respect to continued ownership after the election. The Schedule 14N would also have to provide disclosure for use in the issuer's proxy materials similar to that currently required under the proxy rules for contested elections. A nominating shareholder could provide a statement in support of its nominee(s). A nominating shareholder would have to promptly amend its Schedule 14N for any material change in the facts set forth in a prior notice.

As is the case when directors nominate candidates, a nominating shareholder would be liable for any false or misleading statements in information provided to the company that is then included in the company's proxy materials. The proposed amendments would provide that an issuer would not be responsible for information provided by a nominating shareholder, unless the issuer knows or has reason to know the information is false. Information provided by a nominating shareholder in its notice on Schedule 14N and then included by an issuer in its proxy materials would not be incorporated by reference into any filing by the issuer under the Securities Act of 1933, the 1934 Act or the Investment Company Act of 1940 unless the issuer determined specifically to do so.

A nominating shareholder would have to file Schedule 14N with the issuer and the SEC by the date specified in the issuer's advance notice provision or, if the issuer does not have an advance notice provision, no later than 120 calendar days before the date that the issuer mailed its proxy materials for the prior year's annual meeting. If the issuer did not hold an annual meeting during the prior year, or if the date of the meeting changed by more than 30 days from the prior year, then the nominating shareholder would have to provide its notice on Schedule 14N by the deadline specified by the issuer in a Form 8-K filed within four business days after the issuer determines the anticipated meeting date. The issuer would specify a deadline that was a reasonable time before the issuer intended to mail its proxy materials for the meeting.

Shareholder Nominees. An issuer would not be required to include a shareholder nominee in its proxy materials if the nominee's candidacy or, if elected, board membership would violate applicable state law, federal law or the applicable rules of a national securities exchange or national securities association, and the violation could not be cured. An issuer would not be able to opt out of Rule 14a-11 by

adopting alternate requirements for inclusion of shareholder nominees in its proxy materials. In addition, the required compliance of a shareholder nominee with independence standards of a national securities exchange or securities association would be limited to objective standards in the independence requirements that apply to directors generally and not to any particular definition of independence applicable to audit committee members. In the case of a registered investment company or a business development company, the independence standard would be met if a director nominee was not an “interested person” of the issuer within the meaning of the Investment Company Act of 1940.

A nominating shareholder could have no direct or indirect agreement with the company regarding the nomination of the nominee. The SEC specifically determined not to propose any limitations on the relationships between a nominating shareholder and its director nominee(s). Proposed Rule 14a-11 expressly provides that a nominating shareholder will not be deemed an “affiliate” of the company under the Securities Act of 1933 or the 1934 Act solely as a result of nominating a director or soliciting for the election of a director nominee or against a company nominee pursuant to Rule 14a-11. In addition, the proposed amendments provide that if a shareholder nominee is elected, and the nominating shareholder or group does not have an agreement or relationship with that director, other than relating to the nomination, the nominating shareholder or group would not be deemed an affiliate solely by virtue of having nominated that director.

Number of Shareholder Nominees. Under the proposed amendments, an issuer would be required to include in its proxy materials no more than one shareholder nominee, or the number of nominees that represents up to 25 percent of the issuer’s board of directors, whichever is greater. Any currently serving directors elected through the Rule 14a-11 mechanism whose term extends past the election in question would be counted towards the limit. If an issuer received multiple shareholder nominations meeting the proposed amendments’ requirements, the issuer would determine which to include in its proxy materials based on order of receipt.

Inclusion/Exclusion of Shareholder Nominees in Issuer Proxy Materials. Under the proposed amendments, in the absence of any grounds for excluding a shareholder nomination, an issuer would have to include in its proxy materials disclosure regarding the nominee and if any were provided by the nominating shareholder, a statement in support of the nominee. In its form of proxy, an issuer could identify any shareholder nominees as such and recommend on the form of proxy how shareholders should vote on those nominees and on management nominees, but would otherwise be required to present the nominees in an impartial manner in accordance with Rule 14a-4 under the 1934 Act. An issuer could not allow shareholders to vote for, or withholding authority to vote for, its nominees as a group, but would instead have to require that each nominee be voted on separately.

The proposed amendments include the following grounds for exclusion of a shareholder nominee:

- Proposed Rule 14a-11 is not applicable to the issuer;
- The nominating shareholder has not complied with the requirements of Rule 14a-11;
- The nominee does not meet the requirements of Rule 14a-11;
- Any representation required to be included in the notice on Schedule 14N to the company is false or misleading in any material respect; or
- The issuer has reached the maximum number of nominees from prior shareholder nominations.

The proposed amendments set forth processes regarding the eligibility determination for a shareholder nomination and various notifications to be provided to and by issuers and nominating shareholders, all according to prescribed timeframes. As provided for under Rule 14a-8 for shareholder proposals, an issuer would be able to seek no-action guidance from the SEC staff regarding exclusion of a shareholder nomination. With some exceptions, the burden would generally be on the issuer to demonstrate that it may exclude a shareholder nominee.

Communications Related to Shareholder Nominations. The proposed amendments include additional exemptions from the proxy rules' prohibition against solicitations prior to the filing and dissemination of a proxy statement. In order to facilitate the use of proposed Rule 14a-11 and remove concerns regarding communications among shareholders regarding the submission of a nomination, the SEC is proposing an exemption that would apply to communications meeting specific content limitations. The SEC is also proposing an exemption for solicitations by or on behalf of a nominating shareholder in support of a nominee included in an issuer's proxy materials. The exemption includes limitations on the content of the solicitation and provides that the soliciting party may not directly or indirectly seek the power to act as proxy. Communications pursuant to these proposed exemptions would have to be filed with the SEC no later than the date of first publication.

Shareholder Proposals. Rule 14a-8 under the 1934 Act provides shareholders with an opportunity to place a proposal in an issuer's proxy materials for consideration at an annual or special meeting of shareholders. A shareholder proposal that meets certain procedural requirements and does not fall within one of the categories of proposals that the Rule allows an issuer to exclude, must appear alongside management's proposals in the issuer's proxy materials. Currently, Rule 14a-8(i)(8) under the 1934 Act permits an issuer to exclude a shareholder proposal that relates to a nomination or an election for membership on the issuer's board of directors or analogous governing body or a procedure for such nomination or election. In addition to amending Rule 14a-8(i)(8) to permit shareholder nominations in accordance with Rule 14a-11, the SEC is proposing to allow shareholder proposals by qualifying shareholders that would amend, or that request an amendment to, provisions of an issuer's governing documents concerning the issuer's nomination procedures or other director nomination disclosure provisions so long as those disclosure provisions do not conflict with proposed Rule 14a-11. In addition, the proposed amendments would codify a

number of prior staff interpretations. In sum, under the proposed amendments, an issuer would be able to exclude a proposal under Rule 14a-8(i)(8) if the proposal:

- would disqualify a nominee who is standing for election;
- would remove a director from office before his or her term expired;
- questions the competence, business judgment, or character of one or more nominees or directors;
- nominates a specific individual for election to the board of directors, other than pursuant to Rule 14a-11, an applicable state law provision, or a company's governing documents; or
- otherwise could affect the outcome of the upcoming election of directors.

Shareholder Nominees Pursuant to State Law or an Issuer's Governing Documents.

Amended Rule 14a-8(i)(8) could result in amendments to an issuer's nomination procedures that would allow shareholder nominations without reliance on proposed Rule 14a-11. Similar changes could occur by action of state law, or through amendments to an issuer's governing documents other than by shareholder action. In view of these possibilities, the SEC is proposing to require that a nominating shareholder acting pursuant to procedures established by state law or under an issuer's governing documents file a notice on Schedule 14N with the issuer and the SEC including disclosure about the nominating shareholder and nominee similar to that required in an election contest.

Shareholder Groups. The proposed amendments address the potential ramifications under the share ownership reporting requirements of Section 13 of the 1934 Act of relying on proposed Rule 14a-11. The proposed amendments provide that a shareholder or shareholder group able to satisfy its Section 13 reporting obligations using Schedule 13G could continue to use Schedule 13G notwithstanding activities related to reliance on proposed Rule 14a-11, such as (a) the formation of a shareholder group solely for the purpose of nominating one or more directors pursuant to proposed Rule 14a-11, (b) the nomination of one or more directors pursuant to proposed Rule 14a-11, (c) soliciting activities in connection with such a nomination (including soliciting in opposition to an issuer's nominees), or (d) the election of a shareholder nominee through the mechanism provided by proposed Rule 14a-11. This exception would only be available with respect to a shareholder nomination. After the election of directors, a nominating shareholder or group would need to reassess its eligibility to continue to report on Schedule 13G. The proposed amendments expressly do not provide an exception addressing the reporting requirements of Section 16 of the 1934 Act.

Public Comment. In addition to general requests for comment, the proposing release requests comment on a number of specific issues. Comments on the proposed amendments are due by August 17, 2009.

SEC and Massachusetts Securities Division Settle Enforcement Action against Mutual Fund Investment Adviser and Distributor Relating to Pricing of Mutual Fund Holdings

The SEC and the Massachusetts Securities Division (the “Securities Division”) settled administrative enforcement proceedings against an investment adviser (the “Adviser”) and affiliated distributor (the “Distributor”) for a mutual fund (the “Fund”) relating to overstatement of the Fund’s net asset value (“NAV”). This article highlights some of the SEC’s principal findings as presented in the order issued in connection with the settlement (the “Order”) with respect to the Adviser and the Distributor; in each case, the party to the Order consented to the Order without admitting or denying its findings. The SEC’s investigation was conducted in conjunction with the Massachusetts Securities Division, which made similar findings and found similar conduct violative of Massachusetts securities laws.

The SEC found that the Adviser caused the Fund, which invested primarily in mortgage-backed securities, to overvalue certain of its assets in calculating NAV during the period February 2007 to June 2008. During a three week period prior to the Fund’s liquidation on June 18, 2008, the Fund revalued numerous securities it held downward, resulting in significant declines in NAV relative to normal fluctuations in the Fund’s share price. The Distributor communicated material, non-public information regarding the repricing selectively to Fund shareholders and financial intermediaries, including an affiliated broker-dealer, without issuing a press release or making any other public disclosure regarding the repricing.

The Order includes the following findings by the SEC:

- **Overstated NAV** - The Adviser violated Section 206(2) of the Investment Advisers Act of 1940 (the “Advisers Act”), which generally prohibits an investment adviser from engaging in any transaction, practice or course of business that operates as fraud or deceit on any client or prospective client, by causing the Fund to overstate its NAV from February 2007 until the Fund’s liquidation through the failure by the Fund’s portfolio management team “to factor readily-available negative information into its recommended valuations of certain [mortgage-backed] securities and its recommending valuations for a significant portion of the Fund’s holdings based on prices provided by [a] Florida broker-dealer, which in turn generated higher advisory fees paid by the Fund.” The Order noted that the Adviser had not performed adequate due diligence on the Florida broker-dealer, almost all of whose valuations were revised downward in the subsequent repricing of the Fund’s portfolio, with some valuations reduced by more than 90%. In addition, the Fund’s portfolio management team withheld information on new developments affecting the value of a Fund holding from the Fund’s valuation committee; when the committee later became aware of the development, the security’s value was reduced to zero. The Fund’s portfolio management team misrepresented a transaction by another mutual fund managed by the Adviser in a security held by the Fund to the Fund’s valuation committee as a “distressed sale” by the counterparty, which meant that the transaction could potentially be disregarded for valuation purposes. The Fund was then valuing the security at ten times the value

at which it was purchased by the other fund, but subsequently adopted the latter value when the Fund was repriced.

By virtue of the foregoing conduct, the SEC also found that the Adviser willfully aided and abetted and caused the Fund to sell and redeem its shares at a price other than its current NAV in violation of Rule 22c-1(a) under the Investment Company Act of 1940 (the "1940 Act"). The Distributor was found to have willfully violated Rule 22c-1(a) because while acting as the Fund's principal underwriter, it sold and redeemed shares of the Fund at a price that was not based on current NAV.

- Selective Disclosure Regarding Repricing - The Adviser and the Distributor violated Section 206(2) of the Advisers Act by disclosing information regarding the repricing of certain Fund holdings to select shareholders and financial intermediaries, specifically including shareholders who were customers of an affiliated broker-dealer, while failing to inform the Fund's Board of Trustees about these disclosures. The Order indicates that the Adviser knew or should have known that the selective disclosures would lead to substantial redemptions by shareholders at an inaccurately high NAV, thereby diluting the Fund. The Order notes that the Distributor violated Section 206(2) in willfully aiding and abetting the Adviser's violations by providing substantial assistance to the Adviser by making the selective disclosures to certain shareholders of the Fund. The SEC found related violations of Section 204A of the Advisers Act and Section 15(f) of the Securities Exchange Act of 1934 by the Adviser and Distributor, respectively, for failure to supervise their respective personnel to prevent the misuse of non-public information.
- Affiliated Transactions - The Adviser violated Section 17(a)(2) of the 1940 Act by willfully aiding and abetting the purchase of securities from the Fund by other funds advised by the Adviser in violation of Rule 17a-7 under the 1940 Act, which allows transactions between a mutual fund and certain of its affiliates subject to specified conditions. The Fund's portfolio management team caused certain other funds managed by the Adviser to purchase securities from the Fund at prices other than those required by the Rule and effected the trades through broker-dealers who received remuneration, contrary to the Rule's conditions.
- Best Execution - The Adviser willfully violated Section 206(2) of the Advisers Act when a trader for the Adviser refused to consider the prospect of an offer from a broker-dealer to pay a higher price for a particular security held by the Fund on the condition that the broker-dealer be allowed to purchase the security outright rather than being required to immediately re-sell the security to another mutual fund advised by the Adviser. The SEC found that as a result of this conduct, the Adviser failed to seek to obtain best execution of the trade for the Fund and favored another client over the Fund in breach of its fiduciary duty.

Sanctions. Under the terms of the settlement, the Adviser and the Distributor will, among other things, pay \$33 million to a Fair Fund to compensate shareholders. The Adviser will also pay disgorgement of approximately \$3 million. The Adviser and Distributor each agreed to a civil penalty of \$2 million. The Adviser also agreed to review for any NAV errors related to pricing other funds it advises that held the same securities as the Fund or securities for which the Fund's portfolio management team was responsible for recommending valuations. To the extent that a fund's NAV was materially overstated as a

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result of valuation errors, the Adviser will compensate shareholders for any resulting harm in the same manner as Fund shareholders. To the extent that a fund's NAV was not materially overstated as a result of valuation errors, the Adviser will compensate that fund for any harm caused by processing transactions at an incorrect NAV. The Adviser also agreed to retain an Independent Compliance Consultant to review the Adviser's procedures for valuing portfolio securities and preventing prohibited cross trades, and to review the Adviser and Distributor's procedures for preventing the misuse of material, nonpublic information.