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SEC I: U.S. Chamber of Commerce Files Suit to Overturn SEC Rule Requiring Mutual Fund Boards to Have an Independent Chairperson

U.S. Chamber of Commerce, [U.S. Chamber Files Suit Against New Mutual Fund Rules - Charges SEC Overstepped Authority in Independent Boards](#) (Sept. 2, 2004).

Chamber of Commerce of the United States of America v. U.S. Securities and Exchange Commission, [Complaint](#) (D.D.C., filed Sept. 2, 2004).

On September 2, the U.S. Chamber of Commerce commenced a lawsuit against the SEC in the United States District Court for the District of Columbia under the

Administrative Procedure Act challenging two provisions of the SEC's new mutual fund governance rule. The first provision requires funds to restructure their boards so that the chairperson is not affiliated with the firm that provides advisory services to the fund. The second provision requires that at least 75% of a fund's directors be independent of the fund adviser (or, in the case of funds with three-member boards, that two of the three directors be independent). According to the Chamber of Commerce's announcement of the action: "The SEC has over-reached its authority, resulting in a rule that is bad for investors and contrary to the intent of Congress". The Chamber of Commerce alleges that the "SEC failed to satisfy basic rulemaking requirements by not giving serious consideration to public comments during the rulemaking; ignoring important information about the costs -- and the consequences -- of the rule; and failing to consider evidence that an independent chair is likely to harm rather than help fund performance."

SEC II: SEC Warning Shot - First Action Against Insurers for Permitting Market Timing of Mutual Funds Through Variable Annuities

U.S. Securities and Exchange Commission, [SEC Brings First Enforcement Action Against Insurance Companies for Permitting Market Timing of Mutual Funds Through Variable Annuities - Insurance Companies to Pay \\$20 Million in Settlement](#), News Release 2004-109 (Aug. 9, 2004).

On August 9, the SEC fired its first warning shot over the bow of the variable annuity industry. It announced that it has brought the first enforcement action charging insurance companies with securities fraud for facilitating market timing of mutual funds through the sale of variable annuities. According to the Commission's announcement, the companies involved are subsidiaries of Conseco, Inc. (CIHC, Inc., Conseco Services, LLC, and Conseco Equity Sales, Inc.) and the company to which Conseco sold its variable annuity business in

2002, Inviva, Inc., and its subsidiary, Jefferson National Life Insurance Company.

In its announcement the SEC emphasized that it found that:

"the prospectuses through which the insurance companies sold the variable annuities misleadingly represented, among other things, that the annuities were 'not designed for professional market timing organizations.' In fact, the insurance companies affirmatively marketed and sold the annuities to professional market timers. Eventually, market timing assets constituted the majority of assets invested in the variable annuity products. The insurance companies profited by the fees earned from the sales of the annuities to the market timers."

The companies reportedly have agreed, while neither admitting nor denying the Commission's findings, to settlements that include a total payment of \$20 million in disgorgement and penalties as well as undertakings of compliance reforms. Members of the Commission have been saying for months that the Commission is engaged in a careful review of the variable annuity industry.

SEC III: SEC Proposes to Postpone the Final Phase-In Period for Acceleration of Periodic Report Filing Dates

U.S. Securities and Exchange Commission, [Temporary Postponement of the Final Phase-In Period for Acceleration of Periodic Report Filing Dates](#), Release No. 33-8477 (Aug. 25, 2004).

On August 25 the SEC proposed to postpone for one year the final phase-in period for acceleration of the due dates of quarterly and annual reports required to be filed under the Securities Exchange Act of 1934 by accelerated filers that have a public float of at least \$75 million, that have been subject to the Exchange

Act's reporting requirements for at least 12 calendar months, that previously have filed at least one annual report, and that are not eligible to file their quarterly and annual reports on Forms 10-QSB and 10-KSB.

In its release, the Commission states candidly that the postponement is being proposed "to allow additional time and opportunity for accelerated filers and their auditors to focus their efforts on complying with our new requirements regarding internal control over financial reporting."

For excellent analyses of the SEC's proposal, RealCorporateLawyer.com is pleased to make the following available via its Web site:

[Putting the Brakes on Accelerated Disclosure from Fried, Frank, Harris, Shriver & Jacobson](#) (08/30/2004).

[SEC Proposes One Year Delay in Acceleration of Form 10-K and Form 10-Q Filing Deadlines from Bryan Cave LLP](#) (08/26/2004).

SEC IV: SEC Final Rule Regarding Portfolio Manager Disclosures by Registered Management Investment Companies

U.S. Securities and Exchange Commission, [Disclosure Regarding Portfolio Managers of Registered Management Investment Companies](#), Release Nos. 33-8458, 34-50227, IC-26533 (Aug. 23, 2004).

On August 23, the SEC issued a final rule release entitled "Disclosure Regarding Portfolio Managers of Registered Management Investment Companies". The release was prompted by the Commission's decision to adopt amendments to its forms to expand disclosure provided by registered management investment companies regarding their portfolio managers. According to the Commission, the "amendments extend the existing requirement that a registered management investment company provide basic information in its prospectus regarding its

portfolio managers to include the members of management teams. The amendments also require a registered management investment company to disclose additional information about its portfolio managers, including other accounts that they manage, compensation structure, and ownership of securities in the investment company." The amendments address disclosures regarding:

- identification of portfolio management team members;
- other accounts managed and potential conflicts of interest;
- portfolio manager compensation structure; and
- securities ownership of portfolio managers.

SEC V: SEC Adopts Amendments to Rule 12b-1 to Prohibit Fund Brokerage from Being Used to Compensate Broker-Dealers for Selling Fund Shares

U.S. Securities and Exchange Commission, [Prohibition on the Use of Brokerage Commissions to Finance Distribution](#), Release No. IC-26591 (Sept. 2, 2004).

At an open meeting held on August 18, the Commission adopted amendments to rule 12b-1 to prohibit fund brokerage from being used to compensate broker-dealers for selling fund shares. The Commission concluded that in recent years the practice of directing fund brokerage to broker-dealers as compensation for distribution of fund shares had begun to present "opportunities for abuse that are identical to those that arise when the fund makes direct payments for distribution." The problem, according to the Commission, is further compounded by "the difficulty of making effective disclosure to shareholders about the cost of the practice."

Funds will still be permitted to use selling brokers to execute portfolio transactions under this rule, but the funds will now be required to have policies and procedures in place to preclude "quid pro quo" arrangements relative to the sale of fund shares.

SRO I: SEC Solicits Comments on Proposed Amendments to NYSE Governance Listing Standards

U.S. Securities and Exchange Commission, [Self-Regulatory Organizations: Notice of Filing of a Proposed Rule Change and Amendment No. 1 Thereto by the New York Stock Exchange, Inc. to Amend Section 303A of the NYSE Listed Company Manual Relating to Corporate Governance](#), Release No. 34-50298 (Aug. 31, 2004).

New York Stock Exchange, Inc., [Proposed Amendments to Section 303A Corporate Governance Rules](#) (Aug. 3, 2004).

On August 3, the New York Stock Exchange filed with the SEC a proposed rule change to amend Section 303A of the NYSE Listed Company Manual Relating to Corporate Governance. The Exchange requested expedited approval by the SEC. Following communications with Commission staffers, however, the NYSE filed an amendment to the proposal on August 30 withdrawing its request for expedited approval. The following day, the Commission issued a Notice of Filing and request for public comments on the NYSE proposal.

The NYSE proposal notes that the amendments are intended to make "(i) clarifying language changes consistent with interpretations that have been provided by the Exchange in response to questions and published Frequently Asked Questions . . . and (ii) changes to Section 303A.02(b)(iii) to align it more closely with the similar standard in place at the other listing markets." The Exchange proposes amendments including the following:

To add a definition of the term "executive officer", to make minor changes throughout Section 303A to provide consistency when using this term, and to clarify that service as an interim executive officer will not trigger certain look-back provisions.

To reformulate the wording of the bright line independence tests to reflect more accurately how the applicable look-back periods should be applied.

To clarify that, under Section 303A.02(b)(ii) of the Listed Company Manual, which precludes independence where a director or family member receives more than \$100,000 in direct compensation, the look-back period should not be longer than 36 months.

To clarify that for purposes of Section 303A.02(b)(v) of the Listed Company Manual, the exception for certain charitable contributions is only intended to apply to "contributions" -- not payments for business relationships such as a vendor who is paid for performing services for a charity -- and, thus the independence standard applies to such business-related payments.

To revise the independence standard set forth in Section 303A.02(b)(iii) of the Listed Company Manual so that it would "cover any director or immediate family member who is a current partner of the audit firm, any director who is a current employee of the audit firm, any immediate family member who is a current employee of the audit firm participating in the firm's audit, assurance or tax compliance (but not tax planning) practice, and any former partner or employee of the audit firm who personally worked on the listed company's audit during the past three years."

To revise the definition of "immediate family member" for purposes of Section 303A.02(b)(iii) of the Manual to make it parallel to the Commission's definition set forth in Exchange Act Rule 10A-3(e)(8).

To revise Section 303A.05(b) of the Manual to clarify that a non-management director must preside over each executive session of the non-management directors, although the same director is not required to preside at all executive sessions of the non-management directors.

To clarify that under Section 303A.05(b) of the Manual, the non-CEO compensation on which the committee should focus is that of the executive officers and to make clear that the board has the ability to delegate its authority to approve non-CEO executive officer compensation to the compensation

committee.

To clarify that the audit committee must meet to review and discuss the company's financial statements and must review the company's specific Management's Discussion and Analysis disclosures.

To amend Sections 303A.09 and .10 of the Manual to specify that the disclosure must be in the annual proxy statement (or, if the company does not file a proxy statement, then in the Form 10-K).

To clarify that foreign private issuers are required to provide disclosure of the significant differences between Section 303A requirements and the actual corporate governance practices of the foreign private issuer, as opposed to the general corporate governance practice of the foreign private issuer's home country.

To clarify that qualifications to the annual CEO certification must be specific and disclosed.

SRO II: PCAOB Releases Reports on 2003 Limited Inspections of Big Four Accounting Firms

Public Company Accounting Oversight Board, [Board Releases Reports on 2003 Limited Inspections of Big Four Accounting Firms](#) (Aug. 26, 2004).

Public Company Accounting Oversight Board, [Statement Concerning the Issuance of Inspection Reports](#), PCAOB Release No. 104-2004-001 (Aug. 26, 2004).

[Report on 2003 Limited Inspection of Deloitte & Touche LLP](#) (Aug. 26, 2004).

[Report on 2003 Limited Inspection of Ernst & Young LLP](#) (Aug. 26,

2004).

[Report on 2003 Limited Inspection of KPMG LLP](#) (Aug. 26, 2004).

[Report on 2003 Limited Inspection of PricewaterhouseCoopers LLP](#)
(Aug. 26, 2004).

On August 26, the Public Company Accounting Oversight Board issued reports on the Board's 2003 limited inspections of the four largest public accounting firms. The inspections, according to the announcement, "examined compliance, quality control and selected public-company audits in the national and regional practice offices of Deloitte & Touche LLP, Ernst & Young LLP, KPMG LLP and PricewaterhouseCoopers LLP. At the time the reports were issued, the PCAOB also issued a "Statement Concerning the Issuance of Inspection Reports" that detailed the nature of the inspections and the authority that underlies the inspection process.

Each of the reports includes a detailed description of the types of matters on which the PCAOB focused its inspection procedures and the procedures that the PCAOB staff used to examine those matters. Additionally, the reports include descriptions of issues identified by the PCAOB staff in the course of reviewing the firms' performance on selected audit engagements. As the PCAOB puts it, the reports detail "apparent departures from auditing standards, related attestation standards, ethical standards, independence standards, and the firm's own quality control policies and procedures."

PRACTICAL GUIDANCE: Courtesy of RealCorporateLawyer.com

RealCorporateLawyer.com provides its readers with free access to a very large collection of law firm memoranda providing practical guidance on current hot topics. Readers are encouraged to visit the frequently-updated "Special Features" area of the home page for such current memoranda, as well as the [SEC Reform Portal](#) containing hundreds of other such memoranda. Recent

additions include:

U.S. Court of Appeals Limits Safe Harbor Protection from Gibson, Dunn & Crutcher (08/30/2004)	New Form 8-K Requirements Effective August 23, 2004 from Coudert Brothers LLP (08/23/2004)
Putting the Brakes on Accelerated Disclosure from Fried, Frank, Harris, Shriver & Jacobson LLP (08/30/2004)	SEC Proposes Rule and Rule Amendments Requiring Registration of Certain Hedge Fund Managers from Fried, Frank, Harris, Shriver & Jacobson LLP (08/13/2004)
Update: New Form 8-K Requirements and Executive Compensation Requirements from Bryan Cave LLP (08/30/2004)	SEC Proposes To Require Hedge Fund Adviser Registration from Covington & Burling (08/06/2004)
SEC Proposes One Year Delay in Acceleration of Form 10-K and Form 10-Q Filing Deadlines from Bryan Cave LLP (08/30/2004)	Protection for Whistleblowers Under the Sarbanes-Oxley Act from Covington & Burling (08/04/2004)
The SEC's New Form 8-K Rules Are Now Effective from Fried, Frank, Harris, Shriver & Jacobson LLP (08/30/2004)	

Don't forget the upcoming SEC "Hot Topics" Seminar, Fall 2004. The schedule is Dallas - Sept. 29, Atlanta - Oct. 26, Cleveland - Nov. 16, Boston - Nov. 18 and London - Oct. 7. Each is a free full day briefing presented by RR Donnelley and Glasser legalWorks where attendees can hear from SEC officials, corporate counsel, law firm partners and accounting experts on a host of important hot topics. MCLE Credit is available. [For more information, please click here.](#)

Also, don't forget the [RealFundCompliance.com](#) Web site. [The site's August E-Zine is available here.](#) The free site includes a [monthly E-Zine](#) on fund compliance as well as [breaking news](#) on fund compliance issues. There are [daily regulatory developments listings](#) on the home page as well as hot topic sections on such topics as [compliance](#), [disclosure](#), [fund governance](#), [soft dollars](#), [revenue sharing](#), [frequent trading](#) and [legislative initiatives](#). The site includes a new [FAQ section](#) as well as special features on topics including the following: [anti-money laundering](#), [bank/trust companies](#), [broker-dealers](#), [CFTC](#), [ERISA / fiduciary](#), [inspection / enforcement](#), [insurance products](#), [investment advisers](#), [litigation](#), [private funds / hedge funds](#), [registered funds](#), [retirement / 529 plans](#), and [Sarbanes-Oxley](#).

COMINGS AND GOINGS: Who's Doing and Saying What and Where?

On August 25, the Commission announced that it has named **Mark A. Adler** Deputy Chief Litigation Counsel of the Commission's Division of Enforcement. He succeeds **Peter H. Bresnan** who was named as an Associate Director of the Division of Enforcement in April. *See* U.S. Securities and Exchange Commission, [Mark A. Adler Named Deputy Chief Litigation Counsel of SEC's Division of Enforcement](#), Release No. 2004-118 (Aug. 25, 2004).

On August 20, the SEC announced the selection of H. David Sherman as the academic accounting fellow for a one-year term beginning August 2004. An associate professor at Northeastern University in Boston, he teaches accounting and control course in executive and high technology MBA programs and graduate and undergraduate business programs. He is also an adjunct associate professor at Tufts Medical School and co-director of the MD-MBA program. *See* U.S. Securities and Exchange Commission, [H. David Sherman Named Academic Accounting Fellow for SEC Division of Corporation Finance](#), Release No. 2004-115 (Aug. 20, 2004).

On August 19, the SEC announced that **Cynthia M. Fornelli**, Deputy Director of the Division of Investment Management, will be leaving the Commission to join Bank of America in Charlotte, North Carolina. *See* U.S. Securities and Exchange Commission, [Cynthia Fornelli, Deputy Director of the Division of Investment Management, to Leave Commission](#), News Release 2004-114 (Aug. 19, 2004).

On August 26, the New York Stock Exchange announced that **Edgar S. Woolard, Jr.**, who retired as Chairman of the Board of DuPont in October 1997, has been elected to the NYSE board of directors to take the seat vacated by **D. Euan Baird** who resigned April 23rd. *See* New York Stock Exchange, [NYSE Names Edgar S. Woolard, Jr. to Board of Directors](#) (Aug. 26, 2004).

On August 11, the New York Stock Exchange announced that it has appointed **Linda Dallas Rich** as Senior Vice President, Government Relations. She served most recently as Senior Counsel for the U.S. House of Representatives Committee on Financial Services. *See* New York Stock Exchange, [NYSE Appoints Linda Dallas Rich as Senior Vice President, Government Relations](#)

(Aug. 11, 2004).

What Are the Commissioners Saying? SEC Chairman William H. Donaldson delivered a Statement on [Portfolio Manager Disclosure](#), a [Statement on Final Amendments to Rule 12b-1](#), and a [Closing Statement](#) during the August 18 open Commission meeting.

What Are the Commission Staffers Saying? On August 26, Donald T. Nicolaisen (SEC Chief Accountant) issued a "[Press Statement on PCAOB Inspection Reports](#)". On August 10, Donald T. Nicolaisen spoke at the annual meeting of the American Accounting Association regarding "[The Future of Standards Setting for Public Companies](#)".

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