CTC Investor Relations

Market News

October 2016

A monthly review of IR developments for our clients and friends. . .

Just before Wells Fargo disclosures, Court affirmed SEC's claw-back powers

Wells Fargo's issues regarding the return of incentive compensation based on improper acts by the bank's lower-level managers arose within weeks of a related U.S. Appeals Court ruling that affirmed the SEC's powers on claw-backs of performance-based executive comp. In SEC v. Jensen, the Ninth Circuit affirmed that the Commission's claw-back powers under Sarbanes-Oxley aren't limited to misconduct by CEOs and CFOs directly. Top-executive pay is vulnerable to financial restatements, the court ruled, even if underlings are to blame for the restatements. Defendants had argued that claw-backs of incentive pay based on the prior financial reports were warranted only if the execs receiving the pay were involved in the misdeeds. The ruling affirms several district court rulings that had also sided with the SEC's view. The appellate-level ruling could mean the SEC will pursue claw-backs more often, including in cases driven by whistleblower-driven restatements.

Romances trigger 'lack of independence' action against E&Y

The SEC fined Ernest & Young $9.3 million to settle charges that three former auditors got "too close to clients on a personal level." In citing the first action against an auditing firm for failing to remain independent, the SEC said the firm ignored red flags that signaled their partners' inappropriate actions. This is a major breach for independent auditors whose job it is to examine a public company's financial statements and certify their accuracy, assuring investors they can rely on their review as independent financial experts. The action was against three Ernest & Young senior partners. One of the partners was romantically involved with the chief financial executive of a client firm, while the second with a chief accounting officer. The SEC did not disclose the title of the third employee in the case or the title of the corporate officer involved.

Sausage making: How your earnings release becomes a news story

PR Newswire's Brad Smith posted recently about how quarterly earnings releases turn into Associated Press news stories. More volume and budget cuts means this quarterly process is now more automated, increasing the chance of errors. Smith discovered that the AP's earnings news starts with real humans at Zacks Investment Research, who pore through earnings releases to extract key data points and enter them into an application called Wordsmith, which generates the news-story text in a form-letter approach. Smith advises that the Zacks personnel look first for GAAP Net Income, EPS and Total Revenue. The deeper those numbers and others are buried, the longer it takes AP to issue its report.

Check out your road-show chauffeur to avoid problems

A leading supplier of limos for investor road-show teams says that problems can be avoided by taking a few preliminary steps. DPV Transportation says that given the tightly scheduled, multi-stop trips within large cities, they recommend confirming the drivers' experience, licensing, knowledge of your routes, and advice about potential delays over those routes. Also, make sure that the limo firm has assigned a special coordinator to the meetings, especially if multiple vehicles are required. Chauffeurs should also be specifically covered by non-disclosure agreements with the limo firm.

SEC promises to crack down on third-quarter non-GAAP offenders

The SEC has set up a task force to closely monitor non-GAAP numbers in third-quarter financial reports to ensure they are in compliance. The Commission is acting under its May 17, 2016 guidance to companies to give equal prominence to GAAP and non-GAAP metrics, and explain how they are reconciled. Most violators will receive a comment letter directed toward the offense. Earlier last month the Department of Justice, in conjunction with a SEC civil complaint, criminally charged a financial professional at a public company with using non-GAAP metrics fraudulently.

NYSE implements new volatility procedures

In response to the record 558 drop in the Dow Jones Industrial Average on August 24, 2015, the NYSE last month eliminated Rule 48, allowing market makers to delay opening a stock when the markets are volatile. Under the change, approved by the SEC in early July, parameters governing pre-open price indications and automated openings would be simplified and would adjust for market volatility. In addition, under all market conditions exchange indications will be published to both proprietary and other feeds. This is an appropriate change for the NYSE, which has market makers on the trading floor opening the trading of stocks each day, unlike the other exchanges which are fully automated. The exchange claims the human factor gives it greater stability because people can intervene in ways that trading algorithms cannot.

Whistleblower regulation hailed a big success, despite missing its numbers by a mile

Over the first five years of its Dodd-Frank enhanced whistleblower program, the SEC received 14,000 tips, including 4,000 last year alone. Those numbers fall well short of the estimated 30,000 tips a year projected when the program started in 2011. Despite the shortfall, experts sees the program as a great success, pointing to results such as the tips that led to discovery of the Madoff Ponzi scheme, a $30 million award given to a Siemens staffer in September 2014, or the latest award of $22 million given to a whistleblower at Monsanto several weeks ago. Awards vary from 10 to 30 percent of the monetary sanction recovered.

Activists are honing in on smaller companies

At the end of August, 66 percent of the 575 companies targeted by activists have been either small or micro-cap companies, up 6.7 percent from the same period last year. An increase in activist funds is causing a shortage of target companies, fueling the trend with no end in sight: There were 64 activist campaigns in August, compared with 47 in August last year. Experts suggest that companies pro-actively assess their vulnerabilities, come up with strategies to resolve them, and communicate that strategy. They also suggest to regularly check the investor register to see whether an activist appears.

Study shows directors who lean left are stingy on exec pay

Corporate directors who have left-leaning political views are ironically conservative when it comes to compensating chief executive officers. A recent study conducted by the University of Washington and the University of Notre Dame examined political contributions by directors from 4,000 different public companies between 1998 and 2013 to determine whether they were liberal or conservative. Boards with more conservatives compensated top management better than those with more liberal directors. Considering corporate boards are supposed to base their decisions on what is best for the shareholders, pay by performance makes sense. But the research suggests that political preference has a larger influence. This may be why a *Wall Street Journal* analysis of S&P 500 companies found that of the companies with the 10 highest-paid CEOs, only three delivered top-10% shareholder returns.

♦ ♦ ♦ ♦ ♦ ♦ ♦

For investor relations or market questions, or to discuss our consulting services, please contact us at (937) 434-2700, or e-mail ctc@irbyctc.com