

# Market News

**July 2010**

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

## **Sarbanes-Oxley seems here to stay, and some companies don't mind**

Save for limiting the job security of members of the Public Company Accounting Oversight Board (PCAOB), the Supreme Court has chosen not to tamper with the fundamental principles of the 2002 Sarbanes-Oxley Act (SOX). The Court ruled that the PCAOB members must be directly subject to the SEC, but with their powers and purview intact, disappointing those who had hoped the Court would seize the PCAOB flaw as reason to void the entire statute. Having survived Supreme Court review, SOX is now gaining the respect and appreciation of more public companies, according to a survey by global risk and business consultant Proviti. Ironically, most of the survey respondents said SOX doesn't go far enough in its risk-assessment requirements. Proviti's fourth annual SOX survey found most companies have completed or nearly completed their SOX-mandated changes, and spending less time on compliance. More than a third reported better traditional internal audits, and 25 percent report more appropriate coverage of risk. Other benefits cited were increased objectivity within their internal audit department, and increased effectiveness and efficiency of operations.

## **SEC's swaps suit lacked 'materiality,' judge rules**

A Deutsche Bank salesman and hedge-fund trader may have talked about details of a debt restructuring and then traded swaps on the deal afterward, but a federal judge said the SEC couldn't prove that inside information was behind the trades. U.S. District Judge John Koeltl's 122-page opinion in the SEC's first-ever attempt to police insider trading in the derivatives world said that the government didn't prove that the information that the salesman and trader exchanged in phone calls was non-public. The judge found the SEC's insider trading authority does extend into the private world of swaps and derivatives trading, but that the SEC's case was weak. The parties admitted that they talked by phone about a \$1.6 billion bond offering for the TV-ratings unit Nielsen Co. and that the trader bought related credit-default swaps, selling them later for a \$1.2 million profit.

## **SEC's get-tough policies not yet affecting corporate filings reviews**

So the new, chastened SEC is scrutinizing every corporate filing for evidence of fraud — right? Maybe not. Cases in point are filings for nine public offerings by companies from the Ukraine or Russia, all with virtually no revenues or assets, and minimal if any operations. The SEC cleared all nine, most without asking even a single question of the filers. One that cleared the Commission in eight days, no questions asked, was for Ukragro Corp. of Zhitomir, Ukraine. It listed a 79-year-old massage therapist as its only employee, no revenue, \$100 in assets and a plan to open health spas. The SEC cleared eight similar filings by companies with similarly thin portfolios and plans, all filed by Dean Law Corp. of Seattle. Meredith Cross, head of the SEC's corporation-finance division, says her staff of 300 reviewers now look at every filing, unlike before, but adds that they don't judge whether a proposed offering is worthwhile, but only whether all risks are adequately disclosed. If fraud is suspected, she said, filings are routed to the enforcement division for further review.

## **Shareholders get more auditor votes, for all the wrong reasons**

More shareholders are voicing their opinions on outside auditing firms this year. According to proxy-advisory firm RiskMetrics Group, 66 percent of the top 3,000 public companies are voting on auditor-ratification proposals in 2010, versus 53 percent in 2009. It's not because shareholders are taking more interest in outside audit firms, but due to the SEC's change this year in the broker-vote regulation, prohibiting brokers from voting in director elections without their customers' direction. Afraid they would not reach a quorum, companies added routine matters to their ballots so that brokers could cast ballots for their customers on non-director issues, circumventing the purpose of the regulation. Ironically, the ratification of an outside audit firm by shareholders is not binding.

## **Was Mylan's prescription effective but unsafe?**

The SEC wants to know whether drugmaker Mylan Inc. violated Regulation FD during a September 2009 investor event at a company plant in West Virginia. At the event, Mylan CEO Robert Coury and President Heather Bresch may have signaled good results for the current quarter, judging from a 7 percent jump in Mylan's shares the next day. A month later, Mylan reported great results for the quarter, and a brighter outlook for the year. The SEC is looking into what the attending investors say that Mylan told them at the meeting, as well as giving weight to Coury and Bresch's assertions that everything they said at the meeting was appropriate.

## **Another move to prevent another "flash crash"**

NASDAQ's proposal to protect investors and listed companies from a repeat of the May 6 "flash crash" is a single stock circuit breaker — the NASDAQ Volatility Guard<sup>SM</sup> — which will pause trading based on predetermined thresholds across all NASDAQ listed securities. The program supplements the coordinated efforts by the SEC and U.S. exchanges for an initial pilot program ending December 10<sup>th</sup> establishing a trading pause for stocks in the Standard & Poor's 500 Stock Index that experience a change of 10 percent or more within a trading day. The program will go into effect this month.

## **FASB/IASB propose single revenue recognition standard for U.S. GAAP and IFRS**

A proposed standard to streamline accounting for revenue across industries, and correct inconsistencies in existing standards and practices, was announced June 24. The core principle of the new U.S. GAAP and IFRS proposed revenue recognition standard is that companies should recognize revenue when it transfers goods and services to a customer, and in the amount of consideration the company expects to receive from the customer, according to a release by both boards. The boards have not decided on an effective date for the standard.

## **SEC says Reg FD limits also apply to directors**

The SEC occasionally issues what it calls Compliance and Disclosure Interpretations in Q&A format on Reg FD and other regulations, reflecting questions it gets from outside parties. On June 4, it noted that Regulation FD doesn't bar directors from talking privately with shareholders, but FD's limits apply: directors can't selectively disclose material, non-public information when "it is reasonably foreseeable that the shareholder will purchase or sell the company's securities on the basis of that information." The SEC suggests that companies adopt or extend their disclosure policies to address such director communications with investors. It also notes that Reg FD permits private disclosures of material non-public information to those who promise to keep it in confidence and not act upon it.



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