
Investment Management Industry News Summary - August 2006

AUGUST 30, 2006

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NASD/NYSE Notice Announces Measure Against Latvian Bank

August 25, 2006 3:21 PM

On August 14, 2006, the NASD and NYSE jointly issued a release concerning a special measure imposed by the Financial Crimes Enforcement Network ("FinCEN") against a Latvian bank, VEB Banka, and its subsidiaries. FinCEN took this action after finding that the entities are financial institutions of primary money laundering concern. Consequently, covered financial institutions, including broker-dealers, are prohibited from opening or maintaining correspondent accounts in the United States for, or on behalf of, these entities. Covered financial institutions must review their account records to ensure that they maintain no correspondent accounts directly for, or on behalf of, the entities, and must undertake due diligence measures to ensure that correspondent accounts are not indirectly used by the entities. Due diligence measures must include notification to correspondent account holders that the account may not be used to provide the bank or its subsidiaries with access to the covered financial institution. Notification may be transmitted by mail, fax, or email. Each covered financial institution must document its compliance with the notification requirement. Covered financial institutions must also take reasonable steps to identify any indirect use of their correspondent accounts by the

entities.

NASD and NYSE Joint Release on Section 311 of the USA Patriot Act, NTM 06-41 (August 2006), available at http://www.nasd.com/RulesRegulation/NoticestoMembers/2006NoticestoMembers/NASDW_017182

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NASD Notice Responds to Questions on Outsourcing

August 25, 2006 3:15 PM

On August 15, 2006, the NASD issued a memorandum responding to questions about a Notice to Members, Outsourcing: Members' Responsibilities When Outsourcing Activities to Third-Party Service Providers, NTM 05-48 (July 2005) ("NTM 05-48"). The memorandum states that NTM 05-48 was issued solely to clarify members' responsibilities when outsourcing certain activities, and not as a guide to whether particular activities are appropriately outsourced to third-party service providers. The memorandum described NTM 05-48 as taking the position that if a member organization outsources activities or functions that, if performed directly by members, would be required to be the subject of the member's supervisory system and written supervisory procedures under NASD Rule 3010, then the member must ensure that its supervisory system and written supervisory procedures includes procedures for outsourced "covered activities." to ensure compliance with applicable securities laws and regulations and NASD regulations. Further, the Notice clarifies that under certain circumstances a function outsourced to a third-party renders the person performing that function an associated person of the member by virtue of performing the function, and that the ultimate responsibility for oversight and supervision of the provider lies with the member. Thus, a member cannot contract its supervisory and compliance activities away from its direct control, although it may outsource certain activities that support the performance of those responsibilities.

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MSRB Publishes Request for Comments on Advertising Rules

August 25, 2006 8:28 AM

On August 11, 2006, the Municipal Securities Rulemaking Board ("MSRB") published a request for comments on draft amendments relating to Rule G-21 on advertisements relating to municipal fund securities, including interests in Section 529 college savings plans. MSRB stated that Rule G-21(e) was modeled in part on Rule 482 under the Securities Act of 1933, and codified previous MSRB interpretive guidance on advertisements of municipal fund securities. The MSRB published further interpretive guidance in May 2006 on certain elements of Rule G-21 as they apply to 529 advertisements.

The present request seeks guidance on draft amendments intended to further harmonize the MSRB's advertising rule with SEC and NASD rules. Among other issues, the draft amendments would modify the definition of "advertisement" to more closely align it with the definitions used by the NASD in connection with advertising and sales materials, and more clearly define, and set forth content standards for, "professional advertisement" and "product advertisement." The draft amendments would adopt provisions for generic advertisements of municipal fund securities, and provisions requiring advertisements and correspondence containing performance data to also include disclosure of sales charges and annual operating expenses. The draft amendments also address disclosure requirements applicable to broadcast advertisements, promotional materials and form letters, and home state tax benefits.

Request for Comments on Draft Amendments Relating to Rule G-21, On Advertising, MSRB 2006-26 (August 11,

2006), available at <http://www.msrb.org/msrb1/whatsnew/2006-26.asp>.

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Advisory Opinion on Payment of 12b-1 Fees to Unrelated Brokers

August 25, 2006 8:21 AM

On July 26, 2006, the U.S. Department of Labor ("DOL") issued an advisory opinion expressing the view that when a plan covering employees of a mutual fund, the fund's investment adviser, principal underwriter and certain affiliates invests in that fund pursuant to Prohibited Transaction Exemption ("PTE") 77-3, a broker that is not affiliated with the fund, the investment adviser, distributor or any fiduciary of the plan may receive 12b-1 fees from the fund, provided the principal underwriter does not retain any part of those 12b-1 fees. PTE 77-3 conditionally exempts from certain ERISA and Internal Revenue Code prohibitions the purchase or sale of shares of a proprietary mutual fund by a plan covering only employees of the fund, its investment adviser and principal underwriter, and affiliates of the adviser or principal underwriter. One of the conditions is that the plan may not pay a commission in connection with purchases or sales of the fund's shares. DOL had previously stated that a similar condition in PTE 77-4 would prohibit a broker that is affiliated with a mutual fund from receiving 12b-1 fees in connection with plan investments in the fund.

Letter to Mr. F. Jefferson Bragdon re Company A 401(k) and Profit Sharing Plan (the Plan), ERISA Advisory Opinion 2006-06A (July 26, 2006), available at <http://www.dol.gov/ebsa/regs/aos/ao2006-06a.html>.

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President Bush signs the Pension Protection Act of 2006

August 18, 2006 9:14 AM

On August 17, 2006, President Bush signed the Pension Protection Act of 2006 (the "Act"). The Act, which the United States Senate passed on August 3, 2006, provides significant relief from certain of the plan asset and prohibited transaction rules under the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), and the corresponding rules under the Internal Revenue Code of 1986, as amended (the "Code").

Some provisions of the Act of particular interest to the investment management industry include:

- Liberalized Plan Asset Rule "25% Test" – The Act eliminates foreign benefit plans and United States governmental plans (and non-electing church plans) from having to be included in the so-called "25% test." Under the Act, only United States corporate or union pension plans, IRAs and other plans subject to ERISA or to Code Section 4975 need to be taken into account.
- *Pro Rata* Rule – The Act provides relief where a "plan assets" vehicle invests in another vehicle, such as a fund of funds. In determining whether a second-tier fund itself holds plan assets in cases where a plan asset first-tier fund invests in a second-tier fund, only the proportional interest of benefit plan investors in the first-tier fund—rather than 100% of the investment is counted.
- Statutory Prohibited Transaction Exemption for Certain Investment Advice - The Act provides a statutory exemption to permit advisers and other parties in interest to provide certain investment advice to 401(k) and other defined contribution plan participants, effective December 31, 2006. The investment advice provided by the fiduciary adviser must (i) be provided under an "eligible investment advice arrangement" which either (a) provides that fees do not vary depending on the basis of any investment option selection or (b) uses a computer model under an investment advice program," as defined in the Act, and (ii) satisfy other requirements including appropriate disclosure of the investment advice.
- Other Statutory Prohibited Transaction Exemptions – The Act provides statutory exemptions for the

following activities which were previously prohibited under ERISA, provided certain conditions are met:

(i) block trading, (ii) foreign exchange transactions and (iii) cross trading by large plans.

- Expansion of “Default” Funds for 401(k) Plans – The Act treats a 401(k) plan’s establishment and operation of a default investment fund as eligible for the fiduciary relief provisions of ERISA section 404(c), if certain notice requirements are satisfied. Regulations (to be issued within six months) will provide guidance on the appropriateness of designating default investments that include a mix of assets classes consistent with capital preservation and/or long-term capital appreciation – e.g., life-cycle funds.

Further information regarding this legislation is available in the WilmerHale Securities Email Alert, available at:

<http://www.wilmerhale.com/publications/whPubsDetail.aspx?publication=3309>. A copy of the Act is available at:

http://www.rules.house.gov/109_2nd/text/pensions_cr/HWC_373_xml.pdf

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Diego Tomás Ruiz to become SEC Executive Director

August 18, 2006 9:06 AM

On August 16, 2006, the SEC announced the appointment of Diego Tomás Ruiz as its next Executive Director. Mr. Ruiz, the current Deputy Chief of the Office of Strategic Planning and Policy Analysis of the Federal

Communications Commission, is a former long-time business executive of Univision, a large Spanish-language media company. Mr. Ruiz will begin his duties at the SEC on August 21, 2006. Mr. Ruiz succeeds Jim McConnell, who retired from the position in June 2006.

“Diego Tomás Ruiz Named Executive Director of the Securities and Exchange Commission” SEC Press Release No. 2006-141 (August 16, 2006), available at: <http://www.sec.gov/news/press/2006/2006-141.htm>.

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Erik R. Sirri to become SEC Director of the Division of Market Regulation

August 18, 2006 9:04 AM

On August 14, 2006, the Chairman Cox announced that Erik R. Sirri will become the next Securities and Exchange Commission Director of the Division of Market Regulation. Dr. Sirri, a Professor of Finance at Babson College, is currently a visiting scholar at Harvard Law School. Dr. Sirri previously served as Chief Economist for the SEC from 1996 to 1999. Dr. Sirri will begin his duties at the SEC on September 12, 2006.

“Chairman Cox Names Erik R. Sirri To Be the Commission’s Next Director of the Division of Market Regulation” SEC Press Release No. 2006-140 (August 14, 2006), available at: <http://www.sec.gov/news/press/2006/2006-140.htm>.

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SEC Prohibits Adviser Seeking No-Action Relief From Registering as an Investment Adviser

August 18, 2006 9:01 AM

On August 7, 2006, the SEC staff told an adviser that was requesting assurance that the staff would not recommend an enforcement action against the adviser if it did not register under the Advisers Act, that based on the facts and circumstances as described in the request letter, the adviser was prohibited from registering.

The staff's determination was based on the following facts:

- the adviser, which has its principal office and place of business in Illinois, provides nondiscretionary advice to three offshore advisers that manage offshore private funds of funds. The advice consists of (i) identifying and recommending investment funds, (ii) conducting due diligence on the managers of such funds, (iii) providing reports on these managers, and (iv) providing research on industry trends;
- the adviser does not have the authority to decide which securities to purchase or sell for the private funds, and it is not responsible for arranging the purchase or sale of interests in the underlying funds;
- the adviser does not serve as an investment adviser to any investment company registered under the Investment Company; and
- the adviser is regulated or required to be regulated as an investment adviser in Illinois.

Section 203A(a)(1) of the Advisers Act provides that: No investment adviser that is regulated or required to be regulated as an investment adviser in the State in which it maintains its principal office and place of business shall register under section 203, unless the investment adviser (A) has assets under management of not less than \$25,000,000, or such higher amount as the Commission may, by rule, deem appropriate in accordance with the purposes of this title . . . The SEC staff concluded that the adviser had no assets under management because it did not provide continuous and regular supervisory or management services. As a result, the adviser would be prohibited by section 203A(1) of the Advisers Act from registering with the SEC as an investment adviser. The adviser had sought the staff's guidance because prior no-action letters stated that even if a U.S. resident adviser had only foreign clients, it still was required to register.

Credit Agricole Asset Management Alternative Investments, Inc., SEC No-Action Letter (August 7, 2006),

available at: <http://sec.gov/divisions/investment/noaction/2006/creditagricole080706.pdf>.

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ALJ Dismisses Late Trading and Market Timing Charges Against Former Bank Executive

August 18, 2006 8:58 AM

On August 2, 2006, a SEC Administrative Law Judge dismissed all charges against a former managing director of a Canadian financial institution. The decision comes eight months after New York Attorney General Eliot Spitzer had dropped related criminal charges against the respondent. The charges stemmed from allegations that, while employed as a managing director at the financial institution, the respondent aided and abetted late trading and deceptive market timing of mutual fund shares by two hedge funds and a trust service provider. Although the two hedge funds and the trust service provider were found to have violated Section 17(a) of the Securities Act of 1933, Section 10(b) of the Securities Exchange Act of 1934, and Rule 10b-5 thereunder, as a result of their deceptive market-timing and late-trading practices, and the trust service provider was found to have violated Rule 22c-1 under the Investment Company Act of 1940 (the "Investment Company Act"), the ALJ was unable to conclude that the respondent willfully aided and abetted the primary violators, or caused their primary violations of the securities laws. Accordingly, all charges against the respondent were dismissed. The SEC was seeking civil penalties, disgorgement and other relief, which may have included permanently barring the respondent from the securities industry.

In the Matter of Paul A. Flynn, Initial Decision No. 316, File No. 3-11390 (August 2, 2006), available at: <http://sec.gov/litigation/aljdec/2006/id316rgm.pdf>. A copy of the initial complaint is available at: <http://www.sec.gov/litigation/admin/33-8360.htm>. See also "SEC Charges Former CIBC Managing Director With Fraud for Role in Financing Unlawful Mutual Fund Trading" SEC Press Release No. 2004-12 (February 3, 2004).

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SEC Division of Investment Management Issues No-Action Letter in Response to ABA Letter Requesting Guidance in Light of Goldstein Decision

August 18, 2006 8:48 AM

In response to a July 31, 2006 request letter from the Subcommittee on Private Investment Entities of the ABA Section of Business Law (the “ABA Letter”), on August 10, 2006, the SEC Division of Investment Management issued a no-action letter providing relief from a number of potentially adverse consequences of the Goldstein Decision. The ABA Letter noted that the Goldstein Decision raised issues for hedge fund advisers that registered with the SEC as a result of the Hedge Fund Rule (“Covered Advisers”) whether the advisers decide to remain registered or to deregister as a result of the decision.

For Hedge Fund Advisers that Remain Registered

Offshore Advisers to Offshore Funds

After adoption of the Hedge Fund Rule, Rule 203(b)(3)-2(c) of the Advisers Act provided that advisers having a principal office and place of business outside of the United States would be exempt from the substantive provisions of the Advisers Act with respect to advising private funds organized outside the United States (“offshore funds”) and other non-U.S. clients. Although Rule 203(b)(3)-2(c) was vacated by the Goldstein Decision, the staff has confirmed that any such offshore adviser that remains registered will continue to be exempt from the substantive provisions of the Advisers Act with respect any offshore funds or other non-U.S. clients (to the extent it was exempt prior to adoption of the Hedge Fund Rule).

Records Supporting Performance Information

Rule 204-2(a)(16) requires any registered investment adviser that uses performance information to keep certain records that “form the basis for or demonstrate the calculation of the performance or rate of return.” The Hedge Fund Rule created a limited “transition” exception from this requirement for hedge fund advisers. See Rule 204-2(e)(3)(ii). Under the exception, those advisers were not required to maintain books and records meeting the requirements of Rule 204-2(a)(16) to support the performance of any private fund or other account for any period ended prior to February 10, 2005 (the “Effective Date”). Although the exception was vacated by the Goldstein Decision, the staff stated it would not recommend enforcement action if a Covered Adviser continues to rely on the relief that had been provided in the exception.

Prohibition on Performance Fees from Non-Qualified Clients

Registered investment advisers are generally prohibited from charging a performance fee to clients who are not “qualified clients,” *i.e.*, investors that invest at least \$750,000 with an investment adviser or have a net worth of \$1.5 million or more. The Hedge Fund Rule contained provisions which allowed hedge fund advisers that registered as a result of the Rule to continue receiving performance fees from private funds with non-qualified investors and from other clients who are not “qualified clients” if those persons became equity investors in the private fund or entered into investment advisory contracts with the adviser before the Effective Date. See Rules 205-3(c)(2) and (3). Although these Rules were vacated by the Goldstein Decision, the staff confirmed that it would not recommend enforcement action if a Covered Adviser receives a performance fee from a non-qualified investor if and to the extent that the adviser would have been exempt from the prohibition on receiving such compensation under these vacated Rules.

Custody Rule Relief for Funds of Funds

In order to be exempted from the certain aspects of the custody rules required by Rule 206(4)-2 of the Advisers Act, a fund must be subject to an annual audit of its financial statements prepared in accordance with generally accepted accounting principles and distribute the audited financial statements to all limited partners (or members or other beneficial owners) of the fund within 120 days of the end of the fund's fiscal year. This time frame was problematic for funds of funds, and, as part of the Hedge Fund Rule, the SEC amended Rule 206(4)-2 to extend the deadline from 120 to 180 days following a fiscal year end for delivery of audited financial statements of a fund of funds. Although the amended Rule 206(4)-2 was vacated by the Goldstein decision, the staff confirmed that it would not recommend enforcement action if a fund of funds delivers audited financial statements to its investors within 180 days after its fiscal year end.

For Hedge Fund Advisers That Choose to Deregister

Availability of Section 203(b) after “Holding Out” as an Adviser and/or Having More Than 14 Clients While Registered

Prior to registering as an investment adviser with the SEC, many hedge fund advisers relied on

Section 203(b)(3) of the Advisers Act, which provides an exemption for any adviser that during the preceding twelve months had fewer than fifteen clients and does not hold itself out to the public as an investment adviser. Once registered, a hedge fund adviser need not abide by the Section 203(b)(3) constraints; so a hedge fund adviser that registered as a result of the Hedge Fund Rule may have held itself out generally to the public as an investment adviser, or taken on additional clients to exceed the 14 clients limit (counting each private fund as a client). The staff confirmed that it would not recommend enforcement action against a hedge fund adviser that registered as a result of the Hedge Fund Rule and that withdraws from registration in reliance on the Section 203(b)(3) exemption without regard to whether the adviser (i) held itself out generally to the public while it was registered, and/or (ii) had more than 14 clients while registered (counting each private fund as a single client). An adviser relying on this staff position must withdraw its registration with the SEC no later than February 1, 2007. For the first 12 months following withdrawal from SEC registration, the adviser, for purposes of assessing its eligibility for the Section 203(b)(3) exemption, may determine the number of clients it has had (and thus the availability of the exemption) by reference to a period of time beginning on the date of withdrawal, which may be a period of less than 12 months.

Form ADV-W Balance Sheet Requirement

Form ADV-W (the form filed by an adviser that is withdrawing its registration) requires certain balance sheet information for a withdrawing adviser that has custody of client assets. Although most registered hedge fund advisers are deemed to have custody of client assets under the Advisers Act's custody rule, the SEC does not require them to file a balance sheet with the annual update of their Form ADV registration form. As a result, the staff confirmed that it would not recommend enforcement action if a Covered Adviser that withdraws from registration with the SEC by February 1, 2007 does not provide any balance sheet information.

Additional Staff Guidance

Upon the adoption of the Hedge Fund Rule, certain questions were added to Form ADV requiring information on "private funds." These changes appear to have been vacated by the Goldstein Decision. The staff indicated that it will post on the SEC's website additional guidance on how SEC registered advisers may complete Form ADV pending implementation of changes to the Form.

The staff also noted that the Hedge Fund Rule included an amendment to Rule 204-2 providing that the records of a private fund are records of the adviser (and thus subject to examination by the staff) and affirmed that any registered adviser must make records available for examination by the in accordance with Section 204 of the Act. The adviser may not evade this requirement by holding records by or through any other person, including a related person or private fund.

ABA Subcommittee on Private Investment Entities, SEC No-Action Letter (August 10, 2006), available at <http://sec.gov/divisions/investment/noaction/aba081006.pdf>.

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SEC Decides Not to Appeal Goldstein Decision

August 18, 2006 8:33 AM

On August 7, 2006, the SEC announced that it would not appeal the U.S. Court of Appeals decision in *Phillip Goldstein, et al. v. Securities and Exchange Commission* (the “Goldstein Decision”), in which the U.S. Court of Appeals for the D.C. Circuit had unanimously held that the SEC’s rules requiring registration of hedge fund advisers (the “Hedge Fund Rule”) were arbitrary and had vacated and remanded the Rule to the SEC. In a statement announcing the decision not to appeal, SEC Chairman Cox stated that the SEC’s solicitor and general counsel concluded that appeal would be “futile” since the decision was based on multiple grounds and was unanimous. Chairman Cox noted that the SEC would instead focus on new rulemaking and staff guidance to address the legal consequences of the Rule’s invalidation. Chairman Cox indicated that initiatives under consideration include:

- proposing a new anti-fraud rule that would give hedge fund investors protection of the anti-fraud provisions of Sections 206(1) and 206(2) of the Investment Advisers Act of 1940, as amended (the “Advisers Act”); and
- increasing minimum asset and income requirements in the definition of “accredited investor.”

In addition, Chairman Cox said the SEC staff plans to issue other guidance that will help eliminate disincentives for voluntary SEC registration and enable hedge fund advisers who are already registered with the SEC to stay registered. (See the following News Summary item).

Statement of Chairman Cox Concerning the Decision of the U.S. Court of Appeals In Phillip Goldstein, Et Al. v. SEC, SEC Press Release No. 2006-135 (August 7, 2006), available at: <http://www.sec.gov/news/press/2006/2006-135.htm>. See also Goldstein v. SEC, 2006 WL 1715766 (D.C. Cir.

June 23, 2006) (No. 04-1434). Information regarding Chairman Cox's Senate testimony addressing SEC hedge fund actions after the Goldstein Decision is available in the WilmerHale Securities Email Alert, available at: <http://www.wilmerhale.com/publications/whPubsDetail.aspx?publication=3292> .

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IAA/NRS Report Finds Dramatic Growth in Number of SEC-Registered Hedge Fund Advisers

August 7, 2006 9:42 AM

On July 31, 2006, the Investment Adviser Association (IAA) and National Regulatory Services issued their annual report that profiles the investment adviser profession. Among their key findings, the report notes:

- A dramatic increase in the number of SEC-registered advisers to 10,290 from 8,614 in 2005 – representing a 19.5% increase.
- A dramatic increase in the number of SEC-registered hedge fund advisers. 2,423 registered hedge fund advisers (a registered adviser that reports advising at least one hedge fund client), representing 23.6% of all SEC-registered investment advisers, manage hedge funds with a reported aggregate value of \$2.4 trillion. 1,336 can be characterized as firms that primarily advise hedge funds (more than 75% of clients are hedge funds) and 1,092 are firms that have registered during the past year.
- Total assets under management (AUM) reported by SEC-registered investment advisers reached \$31.4 trillion, increasing 17.2% over the \$26.8 trillion reported in 2005.

The report is based on data obtained from electronic filings by registered investment advisers with the Securities and Exchange Commission (SEC) as of April 7, 2006.

The Investment Adviser Association and National Regulatory Services Report, "Evolution Revolution 2006. A

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FSA Fines a Hedge Fund Manager and its Former Managing Director £750,000 each for Market Abuse

August 7, 2006 9:39 AM

On August 1, 2006, the Financial Services Authority (FSA) announced that it had fined one of Europe's largest hedge fund managers and a former managing director of the manager 750,000 pounds each for market abuse and breaching FSA principles. The FSA noted that the fine on the former managing director is the largest ever imposed on an individual.

The FSA found that the former managing director had used confidential information about a convertible bond sale in February 2003 for a Japanese financial company. The hedge fund manager was also found responsible for its former managing director's market abuse, as the FSA Director of Enforcement noted that firms are accountable for the behavior of their employees, particularly if they are at a senior level.

FSA fines GLG Partners and Philippe Jabre £750,000 each for market abuse. FSA Press Release FSA/PN/077/2006 (1 August 2006). The Final Notice is available at <http://www.fsa.gov.uk/pubs/final/jabre.pdf>.

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Mary L. Schapiro to become NASD Chairman and CEO

August 7, 2006 9:35 AM

On July 20, 2006, Robert Glauber, Chairman and CEO of the NASD, announced his intention to advance his retirement date to August 31. Mr. Glauber, who was expected to retire at the end of the year, served as the NASD's Chairman and CEO for nearly six years. Mr. Glauber, who had been a professor at the Harvard Business School and a lecturer at Harvard's Kennedy School of Government, plans to return to Harvard as a visiting professor in its law school. Mr. Glauber will be succeeded by Mary L. Schapiro, NASD's Vice Chairman and President of its Regulatory Policy and Oversight Division.

NASD News "Robert R. Glauber, NASD Chairman And CEO, Will Retire From NASD On August 31. Will Return To Harvard To Teach At Its Law School" (July 26, 2006).

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Conrad Hewitt to become SEC Chief Accountant

August 7, 2006 9:31 AM

On July 24, 2006, the SEC announced that Conrad Hewitt will become the next Securities and Exchange Commission Chief Accountant. Mr. Hewitt is currently the chair of the audit committee of a California high technology company. Mr. Hewitt will begin his duties at the SEC on Aug. 18, 2006. Deputy Chief Accountant Scott Taub has been acting chief accountant since former chief accountant, Donald Nicolaisen, departed the SEC on Nov. 4, 2005 to return to the private sector.

“Chairman Christopher Cox Names Conrad Hewitt to Be the Commission's Next Chief Accountant” SEC Press Release No. 2006-122 (July 24, 2006), available at: <http://www.sec.gov/news/press/2006/2006-122.htm>.

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SEC to Conduct Study to Compare Roles of Investment Advisers and Broker-Dealers

August 7, 2006 9:26 AM

On August 1, 2006, the SEC issued a request for contract proposals to conduct the first stage of a major study that compares how the different regulatory systems that apply to broker-dealers and investment advisers affect investors. Broker-dealers are regulated under the Securities Exchange Act of 1934, while investment advisers are regulated under the Investment Advisers Act of 1940.

The SEC explained that the study first was suggested in connection with a rule adopted in April 2005 that allows broker-dealers to offer fee-based brokerage accounts without being required to comply with the Advisers Act. The study will help the SEC determine whether concerns raised by commenters in the public comment period merit further action in furtherance of investor protection.

SEC Moves Forward on Study to Compare Roles of Investment Advisers, Broker-Dealers. SEC Press Release No. 2006-129 (August 1, 2006), available at: <http://www.sec.gov/news/press/2006-129.htm>.

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SEC Adopts Updates to Executive Compensation Disclosure

August 7, 2006 9:18 AM

On July 26, 2006, the Securities and Exchange Commission adopted certain changes to the executive and director compensation disclosure rules, related person transactions, director independence and other corporate governance matters, and security ownership of officers and directors. These changes would affect disclosure in proxy statements, annual reports and registration statements. The changes also require most of the disclosure to be in plain English.

The new rules will elicit clearer and more complete disclosure of the compensation of the principal executive officer, the principal financial officer, the three other highest paid executive officers, and the directors by requiring additional narrative to accompany traditional tabular disclosure. The disclosure shall be presented under a standardized heading, "Compensation Discussion and Analysis." The Compensation Discussion and Analysis will be required to be filed with the SEC and certified by the principal executive officer and principal financial officer.

Registered Investment Companies

Certain elements of the adopted changes relate specifically to registered investment companies, including the following:

- Applying operating company executive compensation disclosure requirements in their entirety to business development companies;
- Increasing to \$120,000 the current \$60,000 threshold for disclosure of certain interests, transactions, and relationships of independent directors of registered investment companies, similar to the increase proposed for operating companies with respect to related party disclosure; and
- Reorganizing the proxy rules applicable to investment companies to reflect organizational changes proposed for operating companies.

Compliance

The changes apply to all initial registration statements and post-effective amendments that are annual updates to effective registration statements that are filed on Forms N-1A, N-2 and N-3 (except those filed by business development companies) and all proxy and information statements covering registered investment companies, that are filed on or after Dec. 15, 2006.

SEC Votes to Adopt Changes to Disclosure Requirements Concerning Executive Compensation and Related Matters, SEC Press Release No. 2006-123 (July 26, 2006), available at <http://www.sec.gov/news/press/2006/2006-123.htm>. A copy of the proposed rule is available at <http://sec.gov/rules/proposed/33-8655.pdf>. Additional details will be available in a future news summary once the final rule is released.

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