

A Biweekly
Newsletter of
Federal Securities,
Corporate &
Banking Law
Developments

Freddie Mac Firings Highlight Corporate Governance Concerns

On June 10, 2003, Freddie Mac (the government-sponsored mortgage finance company) announced the involuntary departures of its top three officers: its Chairman and CEO, its President and COO, and its CFO. This sweeping management change suggests that boards of directors may be taking a more active role in identifying and quickly resolving corporate accountability problems in the post-Enron environment. These departures follow Freddie Mac's announcement last January of a potential accounting restatement of the past three years' worth of financial results, the effect of which would prevent the deferral of earnings into future quarters.

Freddie Mac stated that its board of directors initiated these departures, including the termination of the President because the board questioned his "cooperation and candor" in responding to the board's investigation of the accounting matters. The SEC is reportedly investigating whether these officers filed false Sarbanes-Oxley certifications with Freddie Mac's financial statements. Separate investigations are also reportedly being conducted by Freddie Mac's government regulator, the New York Stock Exchange and the local U.S. Attorney's office.

Boards of directors of public companies should actively manage corporate accountability problems to retain investor confidence. Directors should also expect that their actions might be scrutinized after the fact by regulators and by government investigators.

■ DIVIDEND AND CAPITAL GAINS TAX RATES REDUCED BY NEW TAX ACT

Under the Jobs and Growth Tax Relief Reconciliation Act of 2003 (the "Act") signed by President Bush on May 28, 2003, dividends and capital gains are subject to new lower tax rates. With respect to qualified dividends paid by domestic and certain foreign corporations to individual shareholders, a lower dividend tax rate of 15% is effective for dividends received in tax years beginning after 2002. On January 1, 2009, dividends will again be taxed as ordinary income. This differs from the President's proposal to eliminate the taxation of dividends.

With respect to the tax rate on capital gains, a lower capital gains tax rate of 15% is effective for transactions on or after March 6, 2003. The lower capital gains tax rate is applicable for both regular tax and AMT purposes. On January 1, 2009, the capital gains tax rate in place before the Act will return.

Corporations may face increased pressure to pay dividends to holders of common stock as a result of the lower tax rate on dividends. Also, debt securities may become less attractive to investors because the lower tax rate on dividends will increase the after-tax yield of equity securities.

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■ WHISTLEBLOWER PROTECTIONS EFFECTIVE SOON

The Sarbanes-Oxley Act of 2002 provides increased protection to employees of public companies who come forward with information about possible fraud involving their employer. Together with recent SEC regulations, the Sarbanes-Oxley Act provides that:

- Audit committees will be required to establish procedures for receiving and responding to whistleblower complaints involving audit or accounting matters.
- It will be unlawful for both officer and non-officer supervisory employees to retaliate against a whistleblower.
- A whistleblower will be protected even if the complaint turns out to be false, as long as the whistleblower reasonably believed that what was reported was a violation.
- In-house counsel will also be protected against retaliation for whistleblowing, but will have an additional affirmative obligation to report possible material violations of securities laws “up-the-ladder” in the company, to the board of directors if necessary, and to follow the standards of professional conduct established by the SEC.

(http://www.oalj.dol.gov/public/wblower/refrnc/107_204_806.htm)

These procedures will be effective the earlier of a company's first annual shareholder meeting after January 15, 2004, or October 31, 2004. **Companies should consider adopting a whistleblower policy or otherwise clarify standards of conduct in anticipation of the upcoming deadline. We also suggest this be accompanied by an education program for both employees and their supervisors to prevent inadvertent violations.**

■ NASD PROPOSES NEW OFFICER CERTIFICATIONS

On June 4, 2003, the NASD released proposed rules that would require both the CEO and the Chief Compliance Officer of each Nasdaq-listed company to certify annually that adequate compliance and supervisory policies and procedures are in place. The NASD intends the certification to focus senior management's attention on a company's compliance and supervisory systems, not to make the CEO and Chief Compliance Officer personally liable for every compliance failure. The SEC must approve this rule before the NASD can implement it. The NASD is accepting comments on this proposal until July 11, 2003. **Companies that are listed on Nasdaq should be aware of this possible addition to current compliance procedures.**

(<http://www.nasdr.com/pdf-text/0329ntm.pdf>)

Kutak Rock LLP is a national law firm with more than 325 attorneys located in 16 offices throughout the United States practicing in the areas of corporate, banking and securities law, public and corporate finance and complex commercial litigation matters.

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