

SEC TAKES FIRST-EVER ACTION AGAINST 529 SAVINGS PLAN

On August 4, the Securities and Exchange Commission announced the settlement of its first case against a Section 529 educational savings plan. 529 plans are popular investment vehicles that allow people to save for educational expenses without paying certain taxes. The SEC also issued an investor guide that explains the basic information that investors should know before they start saving for college.



529 Savings Plans are a popular way to save for future college costs because they offer certain tax advantages

The SEC action involved the Utah Educational Savings Plan Trust (UESP) and stemmed from untrue statements and omissions by the UESP relating to errors in its operating systems and accounting methods. For instance, UESP publicly and falsely characterized misappropriated funds as "administrative" and incorrectly claimed that investors had not been harmed by their misappropriation.

The SEC also filed a civil complaint against the a former UESP director. In this complaint, the SEC alleged that by at least 2002, as a result of his position as UESP director, the individual became aware of errors in the UESP database system and manipulated them to his benefit.

The complaint specifically alleges that the director misappropriated over \$500,000 from UESP accounts and transferred the funds into UESP accounts secretly controlled by him. Furthermore, the SEC alleges that in 2004, the director withdrew approximately \$85,000 from those accounts for personal use, and then attempted to withdraw an additional

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\$200,000 from those accounts but was prevented from doing so by UESP staff.

UESP subsequently discovered the flaws in its system of operation and cooperated fully with the SEC's inquiry. Due to UESP's extensive cooperation with the SEC inquiry and the fact that UESP has already repaid its investors in full, the SEC did not impose a fine against UESP.

This case again highlights the importance of maintaining good internal controls to prevent and detect fraud at all levels and the value of full cooperation with regulators.■

CORPORATE MINUTES AVAILABLE TO SHAREHOLDERS

The Delaware Court of Chancery recently ruled that shareholders have a right to "broad access" to a company's minutes to evaluate whether the company's directors have met their fiduciary duties under Delaware law.

In this case, a shareholder, Amalgamated Bank, brought an action to inspect the books and records of a corporation, UICI, under Delaware law. According to the court, Amalgamated's purpose was, among other things, to investigate whether UICI's directors breached their fiduciary duty in connection with certain related-party transactions. Amalgamated noted that they were specifically interested in certain related-party transactions between UICI and its affiliates.

In order to access board minutes, the court stated that the shareholder

must demonstrate a proper purpose (or, a purpose "reasonably related to such person's interest as a stockholder") and the scope be limited to books and records "reasonably required to satisfy the purpose of the demand." The court held that

DELAWARE LAW PROVIDES THAT ANY SHAREHOLDER SHALL, UPON WRITTEN DEMAND, HAVE THE RIGHT TO INSPECT FOR ANY PROPER PURPOSE THE CORPORATION'S BOOKS AND RECORDS .

Amalgamated should get "broad access" to UICI's full minutes to assess the independence and disinterestedness of the directors.

The court next addressed the

need for a confidentiality agreement. According to the court, a standard that all nonpublic information is confidential is too broad, but requiring a company to show harm is too narrow. While the court agreed that a confidentiality agreement may be required, it stated that determining whether a document is entitled to confidential treatment requires a balancing of various considerations. The court stated that information that UICI believes, in good faith, constitutes confidential, proprietary, or commercially or personally sensitive information should be treated as confidential.

Upon receipt of a request, companies should consult with counsel to determine whether the purpose is proper and regarding the confidentiality of the books and records at issue.■

FORMER CEO SENTENCED TO TEN YEARS AND \$256.6 MILLION IN RESTITUTION

The Securities and Exchange Commission recently announced that the United States District Court for the Eastern District of Michigan sentenced the former CEO of MCA Financial Corporation (MCA), to ten years in prison and \$256.6 million in restitution for his actions relating to a fraudulent scheme perpetrated by MCA. The former CEO pled guilty in February 2004.

The former CEO was one of seven defendants whom the SEC complaint alleges violated, or aided and abetted violations of, the antifraud provisions of federal securities laws as a result of their involvement in a securities offering and accounting fraud scheme by MCA.

It is alleged that MCA sold securitized interests in pools of

mortgage loans while misrepresenting the risk, rate of return, and historical performance. As a result, the complaint alleges that investors lost at least \$49 million. It is also alleged that MCA sold debentures by including materially misleading financial



Four of the defendants in this securities fraud case have been sentenced to jail time

statements, and, as a result, the complaint alleges that investors lost all of the \$19 million that was invested in the debentures.

All seven defendants have pled guilty to federal criminal charges relating to MCA's fraudulent scheme. Including the former CEO, three of the defendants have been ordered to pay \$256.6 million each in restitution, and one has been ordered to pay \$128 million. Four of the defendants have been ordered to serve jail time; however, the former CEO's prison sentence was much longer than the others due to his integral role in the fraud. Three of the defendants have not been sentenced yet.

This case is a reminder of the high costs associated with conduct violating federal securities laws.■

NEW POST-EMPLOYMENT REGULATIONS FOR BANK EXAMINERS?

On August 4, 2005, the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation and the Office of Thrift Supervision (together, the "federal banking agencies") issued proposed rules to implement post-employment restrictions on certain senior examiners. The proposed rules were issued in response to the Intelligence Reform and Terrorism Prevention Act of 2004.

Pursuant to the proposed rules, under certain circumstances an examiner of a bank or its holding company may not accept compensation from that bank or

holding company for a period of one year following the end of their employment with a federal banking agency. This prohibition applies to examiners that act as senior examiner of the bank for two or more months during the twelve months prior to the end of their employment.

Examiners that violate the restriction could be subject to a five year industry-wide employment prohibition and a civil money penalty of \$250,000.

CERTAIN SENIOR EXAMINERS ARE NOT ALLOWED TO ACCEPT COMPENSATION AS AN EMPLOYEE, OFFICER, DIRECTOR, OR CONSULTANT FROM THE BANK, ITS HOLDING COMPANY, OR FROM CERTAIN RELATED ENTITIES.

Although the penalties only affect potential employees, banks should clarify their human resources policies to account for these proposed changes.■

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