Paul|Weiss

October 23, 2007

SEC Approves Fairness Opinion Rule

On October 11, 2007, the SEC approved the long outstanding rule proposed by the NASD (now known as FINRA) to require its members to include new disclosure in their fairness opinions, and establish procedures with respect to the approval of such opinions, to address conflicts of interest concerns. These rules were controversial when first introduced for public consideration in a Request for Comment in November 2004, and were criticized on many fronts from being confusingly vague to unfairly burdening NASD members without binding other fairness opinion providers. In the almost three years since the original Request, there have been several rounds of public comments and four amendments that have incorporated changes to address many of the commenters' concerns. We urge opinion providers to take this opportunity to review their procedures, including any fairness opinion forms, to ensure compliance with the new rules, which will take effect 30 days after FINRA's distribution of a Notice to Members announcing SEC approval of the rules.

We summarize the new requirements below. For a copy of the final rules, see http://www.finra.org/web/groups/rules_regs/documents/rule_filing/p019261.pdf.

Required Disclosure

New Rule 2290(a) prescribes new disclosure that must be included in fairness opinions issued to the board of directors (including to any committee or other subset of directors) if, at the time of issuance, the member knows or has reason to know that the fairness opinion will be provided or described to the company's public shareholders. FINRA clarifies that the member will be deemed to have such knowledge in situations where, for example, a shareholder vote is required.

In such cases, the member must disclose the following items in the fairness opinion:

(1) If the member has acted as a financial advisor to any party to the subject transaction, and, if applicable, that it will receive compensation that is contingent upon the successful completion of the transaction, for rendering the fairness opinion and/or serving as an advisor.

- FINRA clarifies that this and the other disclosure relating to contingent compensation and material relationships with the transaction parties described below need only be descriptive, rather than quantitative.

1285 Avenue of the Americas
New York, New York 10019-6064
(212) 373-3000

1615 L Street, NW
Washington, DC 20036-5694
(202) 223-7300

Alder Castle, 10 Noble Street
London EC2V 7JU England
(44-20) 7367 1600

Fukoku Seimei Building 2nd Floor
2-2, Uchisawaicho 2-chome
Chiyoda-ku, Tokyo 100-001, Japan
(81-3) 3597-8101

Unit 3601, Fortune Plaza Office Tower A
No. 7 Dong Sanhuan Zhonglu
Chao Yang District, Beijing 100020
People's Republic of China
(86-10) 5828-6300

12th Fl., Hong Kong Club Building
3A Chater Road, Central
Hong Kong
(852) 2536-9933

(2) If the member will receive any other significant payment or compensation contingent upon the successful completion of the transaction.

- FINRA clarifies that a "significant" payment is one that a "reasonable reader of the fairness opinion would have an interest in knowing about in order to assess whether the opinion provider has a potential conflict of interest".

(3) Each material relationship during the last two years or that is mutually understood to be contemplated in which any compensation was received or is intended to be received as a result of the relationship between the member and any party to the subject transaction.

(4) If any information that formed a substantial basis for the fairness opinion that was supplied by the company requesting the opinion concerning the companies that are parties to the transaction has been independently verified by the member, and if so, a description of the information or categories of information that were verified.

- FINRA clarifies that where no information has been verified, a blanket statement to that effect would be sufficient.

(5) Whether or not the fairness opinion was approved or issued by a fairness committee.

(6) Whether or not the fairness opinion expresses an opinion about the fairness of the amount or nature of the compensation to any of the company's officers, directors or employees, or any class of such persons, relative to the compensation to the public shareholders of the company.

- This provision was originally included as a fairness opinion procedure (discussed below). However, commenters thought that this could be interpreted to require members to evaluate compensation packages and undertake other analysis for which they are not qualified. As such, FINRA has converted the requirement to a disclosure item.

Required Fairness Opinion Procedures

New Rule 2290(b) requires the member to have written procedures for approval of a fairness opinion including the following:

(1) The types of transactions and the circumstances in which the member will use a fairness committee to approve or issue a fairness opinion.

(2) In those transactions in which the member uses a fairness committee:

- The process for selecting personnel to be on the fairness committee;

- The necessary qualifications of persons serving on the fairness committee; and

- The process to promote a balanced review by the fairness committee, which shall include the review and approval by persons who do not serve on the deal team to the transaction.

    - FINRA clarifies that the fairness committee does not need to be comprised entirely of persons not serving on or advising the deal team, only that there be enough such persons to provide a balanced review. Whether any person is considered part of the deal team is a facts and circumstances analysis and would not be determined by whether a person is included on all document distributions or participated in certain meetings.

(3) The process to determine whether the valuation analyses used in the fairness opinion are appropriate.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. If you have questions regarding the foregoing, please contact Jeffrey D. Marell (212-373-3105) or Frances F. Mi (212-373-3185).