



# ALERT:

## Treasury Issues Notice for Financial Agents to Manage Securities Acquired Under Capital Purchase Program

STEPTOE & JOHNSON <sup>LLP</sup>

On Friday, November 7, 2008, the Treasury issued a Notice to Financial Institutions seeking proposals for financial agents to provide asset management services for the portfolio of debt and equity securities that Treasury will acquire in financial institutions participating in the Capital Purchase Program (CPP) under the Emergency Economic Stabilization Act of 2008 (Act). (This is different from the Treasury's earlier Notice seeking financial agents to manage troubled mortgage-related securities or mortgage loans, which was issued in early October.) Proposals are due **no later than 5:00 p.m. on November 13, 2008**. Late proposals are at risk of not being considered.

Please click [here](#) for a copy of the November 7 Notice.

### **Background:**

Under the CPP, Treasury will purchase up to \$250 billion of equity securities or debt obligations, or may obtain warrants for common stock or other obligations in U.S. controlled banks, savings associations and certain other financial institutions. The Notice (at 2) also suggests that the Treasury may establish other (currently unspecified) programs in addition to the CPP under which it will obtain equity securities or debt obligations of financial institutions and that the asset managers selected pursuant to this Notice would manage those assets as well. The Notice is issued pursuant to authority granted to the Treasury under the Act, which specifically authorizes the Treasury to appoint "financial agents," and contemplates that the Secretary will retain asset managers. See Act at §§ 101(c)(3) & (d)(3); Notice at 15. The Notice distinguishes "financial agents" from "contractors" and states that neither the Notice nor the services being sought "is a procurement subject to the Federal Acquisition Regulation." Notice at 15.

The Notice contemplates selection of "multiple managers, large and small," *id.* at 6, and states that

these asset managers may be grouped into different tiers or segments, based on manager size, expertise, assignment to different parts of the capital structure, or other bases, or may be joined as co-managers or primary and sub-managers. Other asset managers may stand alone in handling their assigned portion of the portfolio. The Treasury will institute a framework of one or more manager models that will support an inclusive approach to involve both large and small asset managers. All asset managers selected will have a direct relationship with the Treasury as designated financial agents of the United States.

*Id.* In addition, the Notice contemplates that some managers may serve as a "Manager-of-Managers" and requests additional information from financial institutions interested in acting in that capacity. *Id.* at 7. As discussed further below, the Notice also expressly seeks responses from qualified minority- and women-owned or controlled Financial Institutions." *Id.*

## **Duties and Responsibilities**

The Notice (at 3) states that the services to be provided by the asset manager will include

valuing the assets issued by the public and private Financial Institutions, analyzing the on-going financial condition, capital structure, and risks of the public and private Financial Institutions, advising on the optimal disposition of the Treasury's assets, executing transactions in accordance with the Treasury's instructions and Investment Policy and Guidelines, and providing the Treasury with detailed analysis and recommendations on corporate actions, proxy voting, disclosures, consents, waivers, and other business events that could have an impact on Treasury's ownership stake and compliance responsibilities.

Part of the work to be performed will include advising Treasury on the "strategy and optimal timing to execute warrants or monetize preferred shares and other equity securities or debt obligations, consistent with both the duty to the taxpayer and the goal of market stability," *id.* at 4, and executing transfers, trades and other transactions in accordance with Treasury's Investment Policy and Guidelines. See *id.*

According to the Notice, the "size of the overall portfolio will reach hundreds of billions of dollars." *Id.* at 3. However, the asset managers will neither acquire nor have custody of the assets in the portfolio, and the portfolio is not expected to be actively traded.. *Id.* (Bank of New York, Mellon, which Treasury previously selected as custodian for TARP, will presumably act as custodian for these securities as well.) The arrangement is expected to "last at least several years." *Id.*

Like prior TARP notices seeking financial agents, this Notice states that as financial agents, the Financial Institutions selected "will have a fiduciary responsibility to perform all services in the best interests of the United States." *Id.* at 6; see also *id.* at 13. The asset managers will also be required to establish and maintain "a compliance program designed to detect and prevent violations of Federal securities laws, and to identify, document, and enforce controls to mitigate conflicts of interest." *Id.* at 5. They will also have to agree to give Treasury and its auditors a broad right of access to books and records related to the services provided. *Id.*

## **Eligibility Requirements and Qualifications**

Like other Treasury solicitations for financial agents, this Notice includes a number of minimum qualifications and other eligibility requirements. Only "financial institutions," which are "any bank, savings association, credit union, security broker or dealer, or insurance company, established and regulated under the laws of the United States or any State, territory, or possession of the United States, [or] the District of Columbia . . . and having significant operations in the United States, but excluding any central bank of, or institution owned by, a foreign government;" *id.* at 7, are eligible. In addition, a financial institution (among other things):

- Must have been continuously engaged for the last three years as a "principal business in managing assets" and providing services comparable to the those described in the Notice;
- Must "have at least \$100 million in dollar-denominated assets under management;"
- Must propose a "primary manager assigned to the Treasury's account" who has "at least 10 years of experience in managing assets comparable to those described in this notice;"
- Must be able and willing to "partner" with other Financial Institutions selected to be managers, co-managers, Managers-of-Managers, etc., as directed by the Treasury;
- Must not be suspended, debarred or otherwise excluded from doing business with the Government;

- “Must not be delinquent on any debts owed to the Federal Government;” and,
- “Must not be subject to any pending or current enforcement actions that could impair its ability to provide any services under this notice.”

Id. at 7-8

### **Conflicts of Interest**

This Notice also places considerable emphasis on disclosure and avoidance and mitigation of actual and potential “conflicts of interest.” Id. at 8; see also id. at 15. The Notice focuses on conflicts that would impair an institution’s objectivity or ability to fulfill its fiduciary duties to the Treasury. Id. at 9. It states that conflicts of interest may exist if an institution, or its subsidiaries or affiliates “may be participating in the Troubled Asset Relief Program under the Act, or if you (1) have a personal, business, financial, or customer interest or relationship with a Financial Institution that may elect to participate in the Capital Purchase Program, or (2) manage proprietary or fiduciary accounts that hold securities issued by such Financial Institutions.” Id. The Notice specifically states that a “Financial Institution must be able and willing to enact and enforce information barriers sufficient to prevent the disclosure or misuse of material, non-public information received or obtained from, or derived on behalf of, the Treasury.” Id. at 8.

### **Proposal Requirements**

The Notice (at 8-9) details information required in initial proposals. This includes information on ownership and ownership structure; summary of capabilities and expertise; personnel; infrastructure capabilities; and information on assets under management and “annualized gross-of-fee returns for Government Investment Performance Standards (GIPS) compliant composites for 1-year, 3-years, and, if available, 5-years ending September 30, 2008, against a broad U.S. market benchmark(s).” Id. at 9. Respondents are also asked to provide two specific “ideas, recommendations, or insights on the strategy for managing the overall portfolio or the investment policy to govern the assets,” that the respondent would manage. Id. at 10.

In addition respondents are required to:

- Propose a plan to mitigate, neutralize or avoid any identified conflicts of interest;
- Describe their compliance and ethics programs, “including any policies, procedures, training requirements, and audit practices designed to detect and prevent violations of Federal securities laws and conflicts of interest.” Information regarding an organization’s compliance or risk officer, if any, is also requested.
- “Identify any Federal or State citations or enforcement actions your organization or any affiliate has received or been warned of, and any litigation or legal proceeding involving your asset management or investment consulting services involving fraud, negligence, criminal activity, or breach of fiduciary duty.”

Id. at 9-10. Finally, respondents are required to propose fees, explain the basis and rationale for those fees and “declare the all-in costs” for their services. Id. at 10.

Additional information is required for financial institutions interested in acting as a manager-of-managers, and for minority or women-owned or controlled businesses. With respect to the latter, the Notice does not establish a specific ownership percentage or certification requirement for qualification or disqualification of such businesses. Rather, such organizations are asked to provide information regarding extent of minority or women ownership and executive management. Information on existing certification as minority or women-owned business can also be provided. Id. at 10-11.

## **Selection Process**

Treasury again has proposed a multi-step selection process. See *id.* at 11. The first phase is evaluation of initial proposals. This is followed by exchanges with selected respondents, at which point the institution may be required to provide additional information on a number of the topics discussed above. The third phase may include face-to-face discussions and will involve further exchanges with the respondent on matters relevant to its capabilities and qualifications, after which final selections will be made. (Selection may be on a phased basis.) The Notice repeatedly emphasizes the Treasury’s discretion in the evaluation and selection of financial agents. See *id.* at 1, 11-13, 16. In addition, financial institutions selected must sign a Financial Agency Agreement. For an example of the Financial Agency Agreement previously entered into with The Bank of New York Mellon, please click [here](#); for a summary of the Financial Agency Agreement with The Bank of New York Mellon, please click [here](#).

Format requirements, page limits for proposals and a requirement for a certification relating to eligibility and certain other matters are set out at page 13 of the Notice. The Notice also includes a list of “non-exclusive” evaluation factors which includes:

- “[V]alue and rigor of the [respondent’s] ideas, recommendations, and insights;”
- Qualifications of proposed staff;
- Prior “experience in managing and analyzing the types of assets and performing the types of services identified in this notice;”
- Existing infrastructure and capability to implement any necessary additional infrastructure;
- Conflicts of interest and ability to neutralize or mitigate such conflicts.
- Overall financial and management stability.
- Proposed fee schedule and all-in costs.

*Id.* at 14.

## **Other Provisions to Note**

Financial Institutions interested in responding to the Notice should also note the following provisions relating to obtaining, submitting and receiving information relating to the Notice:

- The Notice (at 12) states that respondents should not to contact Treasury (or its employees or agents) for additional information about the Notice and cautions them that “[n]o information gained from any such communication may be considered in any way binding or limiting on the Treasury;”
- Imposes confidentiality requirements, including limitations on further disclosure, on information which a respondent receives from Treasury relating to the evaluation of its proposal or received in connection with the Notice; and
- Also states that “Treasury shall have the unlimited right to use, for any governmental purpose, any information submitted in connection with this notice.” *Id.* at 15 (emphasis supplied).

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Stephoe's new Troubled Asset Task Force is ready to advise financial institutions, sellers and purchasers of assets, asset managers, and program managers on the economic stabilization legislation passed this week by the U.S. Congress. Focused on helping businesses at every scale nationwide navigate wisely in the wake of the current tumult in capital markets, the Task Force is structured to advise clients in the post bailout economy and the new regulatory landscape. This multi-disciplinary group will provide coordinated representation in matters involving Congressional oversight investigations; white collar criminal defense; federal contracting opportunities; tax law, ERISA and executive compensation; and, mortgage and asset securitization and structured financing. Steptoe's restructuring and distressed asset attorneys are also aboard to formulate complex and innovative approaches to workouts and troubled real estate transactions, and counsel clients on the judicious sale and acquisition strategies and liquidation of distressed assets. The Troubled Asset Task Force is well aligned with and supports the firm's national Subprime & Credit Crisis Team, organized last year in response to early concerns within the residential lending market.

Leadership of the Task Force is provided by Washington, D.C.-based partners Scott A. Sinder, chair of Steptoe's Government Affairs & Public Policy practice and General Counsel to the Commercial Mortgage Securities Association; John T. Collins, a member of the firm's Corporate, Securities and Finance practice and its Regulatory & Industry Affairs Department, who was formerly General Counsel to the US Senate Banking Committee, a Senior Attorney at the Washington D.C. Federal Reserve Board and a Staff Attorney with the SEC; and Scott H. Katzman, head of Steptoe's Corporate, Securities and Finance practice.

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