

May 2009

Public-Private Investment Program Oversight Legislation Passed by Senate

On May 6, 2009, the Senate approved S. 896, the “Helping Families Save Their Homes Act of 2009” by a margin of 95–1. The legislation includes amendments by Senators Barbara Boxer (D-CA) and John Ensign (R-NV) (collectively, the “Amendments”) to provide additional oversight over the Public-Private Investment Program (“PPIP”) announced by the U.S. Department of the Treasury (“Treasury”). The Amendments impose significant duties on PPIP fund managers, including an obligation to acknowledge fiduciary duties to investors, which may limit managers’ interest in participating in the PPIP. A copy of S.896 is available [here](#).

Overview

The Amendments, collectively titled the “Public Private Investment Program Improvement and Oversight Act of 2009,” follow the release of the Special Inspector General of the Troubled Asset Relief Program’s (“SIGTARP”) April 21, 2009 Quarterly Report to Congress, in which SIGTARP highlighted several vulnerabilities in the PPIP, including risks of conflicts of interest, collusion and money laundering, and provided several recommendations for improvements in PPIP and its relationship with the Term Asset-Backed Securities Loan Facility (“TALF”).

The Amendments provide that any program established by the Federal government to create a public-private investment fund (“PPIF”) shall:

- in consultation with SIGTARP, impose strict conflict of interest rules on managers of PPIFs to ensure that securities bought by the PPIFs are purchased in arm’s-length transactions, that fiduciary duties to public and private investors in the fund are not violated, and that there is full disclosure of relevant facts and financial interests (which conflict of interest rules shall be implemented by the manager of a PPIF prior to the PPIF receiving any Federal government financing);
- require each manager of a PPIF to acknowledge, in writing, a fiduciary duty to both the public and private investors in such PPIF;
- require each manager of a PPIF to develop a robust ethics policy that includes methods to ensure compliance with such policy;
- require strict investor screening procedures for PPIFs;
- require each manager of a PPIF to identify for Treasury each investor

that, individually or together with its affiliates, directly or indirectly holds equity interests in the PPIF acquired as a result of:

- any investment by such investor or any of its affiliates in a vehicle formed for the purpose of directly or indirectly investing in the PPIF (such as feeder funds); or
- any other investment decision by such investor or any of its affiliates to directly or indirectly invest in the PPIF an amount that, in the aggregate, equals at least 10 percent of the equity interests in such PPIF;
- require each PPIF to make a quarterly report to Treasury that discloses the 10 largest positions of the PPIF (which reports shall be publicly disclosed at such time as Treasury determines that such disclosure will not harm the ongoing business operations of the PPIF);
- allow SIGTARP access to all books and records of a PPIF, including all records of financial transactions in machine readable form, while requiring SIGTARP to protect the confidentiality of all such information; and

→ require each manager of a PPIF to retain all books, documents and records relating to such PPIF, including electronic messages.

Acknowledging a fiduciary duty to both public and private investors is contrary to the partnership agreements for many private investment funds, which expressly state that no fiduciary duty is owed by the manager to investors. Imposing such a duty on managers of PPIFs to investors, coupled with the additional information and disclosure requirements and the access to information by SIGTARP, may serve as a disincentive for private investment fund managers to participate in PPIF. In addition, it is not clear why the investor identification requirements apply to all investors in feeder funds, but only to 10 percent investors if they invest directly in the PPIF.

The Amendments require Treasury to consult with SIGTARP and issue regulations governing the interaction

of PPIF, TALF and other similar public-private investment programs. These regulations will be designed to address concerns regarding excessive leverage that could result from interactions between such programs.

The Amendments also require SIGTARP to submit a report to Congress not later than 60 days after the date of the establishment of the oversight program and appropriate an additional \$15 million to SIGTARP to prioritize the performance of audits or investigations of recipients of non-recourse Federal loans made under PPIF or TALF to determine the existence of any collusion between the loan recipient and the seller or originator of the asset used as loan collateral, or any other conflict of interest that may have led the loan recipient deliberately to overstate the value of the asset used as loan collateral.

Conclusion

Although S.896 passed the Senate on May 6, 2009, the prospect of the PPIF provisions becoming law remains unclear. The House of Representatives approved mortgage legislation (H.R. 1106 and H.R. 1728) on March 5 and May 7, 2009, respectively, but neither House bill included provisions relating to additional oversight of PPIFs. If similar legislation ultimately is passed by the House of Representatives or included in a compromise bill, and the legislation is enacted, private sector participants in both the Legacy Securities Program and the Legacy Loan Program of PPIF will be subject to significant additional oversight and duties. This additional oversight, including the express obligation to acknowledge fiduciary duties to both public and private investors in a PPIF and the additional information and disclosure requirements, may limit interest in participating in these programs.



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