



## **CONFLICTS OF INTEREST GUIDANCE FOR TALF AGENTS PARTICIPATING IN THE TERM ASSET-BACKED SECURITIES LOAN FACILITY**

### **I. Introduction**

The purpose of this guidance pertaining to conflicts of interest for TALF Agents<sup>1</sup> participating in the Term Asset-backed Securities Loan Facility (“TALF program” or “Program”) is to highlight certain requirements and expectations of such TALF Agents in order to safeguard public confidence in the TALF program, the Federal Reserve and the participating TALF Agents.

Under the terms of the TALF program, a participating TALF Agent will perform a variety of critical roles. Because potential borrowers under the TALF program must interface with TALF Agents in order to obtain a TALF loan, the TALF Agents will act as agents on behalf of potential borrowers to submit loan requests to the Federal Reserve Bank of New York (“FRBNY”). In addition, a TALF Agent may be an underwriter of securities that may be pledged as collateral to the TALF program, a TALF borrower, or the sponsor of a TALF fund that borrows from the facility. TALF Agents are also expected to: (i) assess the eligibility of prospective borrowers and collateral, (ii) receive that portion of the interest and principal distributions on the collateral that is for the account of the borrowers, (iii) disburse such interest and principal to the borrowers, and (iv) perform certain due diligence and recordkeeping functions. In certain circumstances, a TALF Agent may also be affiliated to a sponsor or issuer of TALF eligible collateral. Finally, the TALF Agent may be a seller or broker of legacy CMBS to or for a TALF borrower.

This document is intended to ensure the integrity of the TALF program by (i) providing TALF Agents with guidance in navigating the multiple roles that they may perform and (ii) establishing a protocol for the TALF Agents to escalate, report and manage potential or actual conflicts of interest that may arise during the performance of their TALF duties.

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<sup>1</sup> A “TALF Agent” means each financial institution appearing from time to time on the list of Eligible TALF Agents available in the TALF Standing Loan Facility Procedures under the link “Eligible TALF Agents” that has become a party to the Master Loan and Security Agreement among the FRBNY and TALF Agents (the “MLSA”), individually and as agent for its Applicable Borrowers.

## II. Scope

Each participating TALF Agent is required to identify and remediate any potential conflicts of interest that arise or may arise in connection with activities undertaken under the TALF program and communicate a conflict of interest identification and remediation plan to the FRBNY no later than two business days prior to submitting an initial loan request. Pursuant to Section 11.3 of the MLSA, each participating TALF Agent has committed to abide by the following:

- 1) prior to submitting a TALF loan request on behalf of any person, a TALF Agent must establish, implement and maintain policies and procedures designed to identify the existence of any actual or potential conflict of interest that may exist or arise as a result of its intended activities under the TALF and take appropriate remedial action to address any conflict of interest identified; and
- 2) The conflict of interest identification and remediation plan (a “Remediation Plan”) should be designed to address actual or potential conflicts of interest that exist or may arise if (i) such TALF Agent or a Related Person<sup>2</sup> acted or intends to act as underwriter for the securities proposed or to be proposed as collateral for a TALF loan, (ii) such TALF Agent or a Related Person is a sponsor or issuer of the securities proposed or to be proposed as collateral for a TALF loan or (iii) such TALF Agents or a Related Person has submitted or intends to submit the TALF loan request to the FRBNY on behalf of itself or a Related Person.
- 3) with respect to a loan request supported by legacy CMBS, the Remediation Plan should be designed to address actual or potential conflicts of interest that may exist or may arise if (i) the TALF Agent acts as the seller of the legacy CMBS to the TALF borrower or (ii) CMBS having the same CUSIP number associated with the legacy CMBS proposed or to be proposed as collateral for a TALF loan are maintained by the TALF Agent either in a proprietary account or an account managed by the TALF Agent on behalf of a client. In addition, any fund managed by the TALF Agent that borrows under the TALF program to purchase legacy CMBS must either (a) be segregated from and managed independently from any other fund that holds legacy CMBS that are eligible to be financed under the TALF program or (b) the TALF Agent must provide a remediation plan detailing how it will ensure unbiased decision making on behalf of such funds and how potential or actual conflicts of interest will be mitigated.

Moreover, the FRBNY has determined that additional safeguards are required under certain circumstances. These additional safeguards are outlined in Section V.

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<sup>2</sup> Related Person” means any affiliate (as defined in the MLSA) of a TALF Agent, or any other person that has been formed or sponsored by, or is controlled or managed by or otherwise affiliated with, such TALF Agent or any of its affiliates.

### **III. Conflict of Interest Identification and Remediation**

#### **A. General Requirement**

Participating TALF Agents are required to establish conflict of interest policies and procedures associated with their TALF activities. Such policies and procedures must include conflict of interest identification and remediation measures designed to address actual and potential conflicts that may arise out of the TALF Agent's multiple roles in any TALF transaction, including the risk that the TALF Agent or a Related Person may gain, or stand to gain, an unfair competitive advantage in arranging a loan under the TALF. Moreover, measures taken must ensure that all eligible borrowers who seek a loan from the TALF through a TALF Agent are treated fairly and that the integrity of the TALF Agent's participation in the TALF is not undermined. Each TALF Agent must designate a person or committee with a reporting line independent of the sales and trading business of the TALF Agent which shall be responsible for oversight and mitigation of any conflicts of interest arising from the administration of the TALF program.

#### **B. Specified Remediation Plan for Submission to FRBNY**

As noted, prior to submitting a loan request a TALF Agent must submit a Remediation Plan to the FRBNY under the conditions set forth in Section II above. In such circumstances, the Remediation Plan developed by the TALF Agent should at a minimum meet the requirements of this Subsection.

##### **i. Identification**

A Remediation Plan must identify any actual or potential conflicts of interest that may arise pursuant to the TALF Agent's duties under the TALF program and must include all information necessary for FRBNY to assess such actual or potential conflict. If a TALF Agent identifies a conflict, its Remediation Plan must include, at a minimum, the following identification information:

- 1) the TALF Agent's relationship to the TALF borrower;
- 2) a description of the activities that give rise to the conflict;
- 3) any actual or potential Personal<sup>3</sup> or Organizational<sup>4</sup> Conflicts of Interest;
- 4) a description of the conflicts remediation process established by the TALF Agent; and

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<sup>3</sup> "Personal Conflict of Interest" means a personal, business, or financial interest of an individual, his or her spouse, minor child, or other family member with whom the individual has a close personal relationship that could adversely affect (i) the individual's ability to perform his or her duties, or (ii) his or her objectivity or judgment in performance of such duties.

<sup>4</sup> "Organizational Conflict of Interest" means a situation in which the TALF Agent has an interest or relationship that could cause a reasonable person with knowledge of the relevant facts to question the TALF Agent's objectivity or judgment to perform TALF activities or its ability to adequately represent parties with adverse interests.

- 5) clearly identify any material Personal or Organizational Conflicts of Interest that have not been fully mitigated by the firm's Remediation Plan.

## **ii. Remediation**

Mitigation measures may depend on a variety of factors, including the type of conflict, the structure of the offering, and the organizational structure of the TALF Agent and the Related Person. Measures designed to address the conflict may include:

- 1) adoption, implementation, and enforcement of a code of conduct or other ethics policy that may address conflicts of interest;
- 2) adoption, implementation, and enforcement of appropriate information barriers to prevent unauthorized individuals from obtaining nonpublic information relating to the loan or offering;
- 3) protocols that separate the conflicting activities of a TALF Agent or a Related Person;
- 4) execution of processes or procedures to ensure that the sale or placement of the TALF eligible securities would be conducted fairly; and
- 5) any other steps appropriate under the circumstances.

## **iii. Monitoring**

Each TALF Agent shall maintain a log of any actual conflicts that arise under the TALF program. This log shall clearly identify the conflict, the parties involved and the steps taken by the TALF Agent to remediate the conflict. Any conflict that cannot be remediated internally must be either escalated to the Chief Compliance Officer of the FRBNY pursuant to Subsection B (iv) below or the relationship or transaction which gave rise to the conflict must be terminated.

## **iv. Waivers**

The Chief Compliance Officer of the FRBNY may grant requests for waivers submitted under a Remediation Plan when it is clear, from the totality of the circumstances, that a waiver is appropriate and consistent with the just administration of the TALF program.

## **v. Submission**

Each TALF Agent must submit its Remediation Plan to the TALF Compliance Director no later than two business days prior to submitting a loan request under the conditions set forth in Section II above. Additionally, TALF Agents must immediately communicate to the TALF Compliance Director any material changes or updates to their Remediation Plans, and must submit a subsequent Remediation Plan upon request. TALF Agents must also provide FRBNY with a copy of the conflicts log maintained in accordance with Subsection B (iii) above upon request of the TALF Compliance Director. Remediation Plans and conflicts logs should be transmitted via email to [talf.compliance@ny.frb.org](mailto:talf.compliance@ny.frb.org).

### **C. Transaction Based Escalation Requirement**

Certain transactions present potential conflicts of interest which warrant a high level of scrutiny and, as a result, should be escalated both to the TALF Agent's designated person or committee described in Subsection B (iii) above and to the TALF Compliance Director via email to [talf.compliance@ny.frb.org](mailto:talf.compliance@ny.frb.org) immediately upon determination that a conflict exists. These include, but are not limited to, the following:

- Where a potential borrower is the TALF Agent or an affiliate of the TALF Agent;
- When proceeds of newly issued securities pledged to TALF will be used to repay any financing from the TALF Agent or its affiliates; or
- Where a TALF Agent or its affiliate is the sponsor of the newly issued asset-backed securities or is the originator of the collateral supporting the asset-backed securities.

### **IV. Exemptions**

Under Section 36 of the Securities Exchange Act of 1934 ("Exchange Act"), the United States Securities and Exchange Commission issued an exemption granting limited relief from the prohibition on arranging certain credit contained in Section 11(d)(1) of the Exchange Act. Specifically, such relief was requested to permit SEC-registered brokers-dealers that act as TALF Agents to participate in the TALF by facilitating extensions of nonrecourse credit on behalf of the FRBNY to purchasers of certain new issues of asset-backed securities in the distribution of which they may have participated as member of a selling syndicate or group within the meaning of Section 11(d)(1). For more information, please refer to the letters containing the SEC exemptive relief at the following addresses:

<http://www.sec.gov/divisions/marketreg/mr-noaction/2009/frbny021709.pdf> and  
<http://www.sec.gov/divisions/marketreg/mr-noaction/2009/frbny082109.pdf>.

### **V. Additional Safeguards for the TALF program**

A basic tenet that underlies the TALF program is that eligible collateral will be most prudently selected if an independent investor's economic capital is put to risk. Accordingly, the Federal Reserve has imposed the following requirements to limit possible conflicts between the TALF's goals and the interest of other participants.

#### **A. Restriction on Moral Recourse and Related Certification**

On December 31<sup>st</sup> of each year of the TALF program, each TALF Agent is required to submit a certification to the FRBNY stating that neither the TALF Agent nor any affiliate will enter into any agreement pursuant to which the TALF Agent or its affiliates will, directly or indirectly, acquire from any borrower any collateral the issuance of which was underwritten or

sold by such TALF Agent (“Subject Collateral”) at a price designed to reduce or eliminate any loss that such borrower would realize on the sale of such Subject Collateral in a fair market value transaction, or enter into any other agreement or consummate any other transaction intended to have the same effect. For additional information see Appendix 1 of the MLSA.

**B. Limitation on Hedging Transactions**

With respect to Subject Collateral, the limitation described in Subsection A. of this Section also prohibits a TALF Agent or an affiliate from entering into any transaction that is designed to hedge against losses specific to securities purchased with TALF financing. This prohibition extends to both direct hedges, such as credit default swaps, and correlative hedges, such as short-selling the ABX index. However, the prohibition does not extend to hedges on a borrower’s broader portfolio, which may include Subject Collateral.

**C. Restriction on Purchasing Self-Originations**

TALF Agents and their affiliates are prohibited from purchasing with the proceeds of a TALF loan TALF collateral that was securitized by the TALF Agent or an affiliate or securities that contain underlying credit exposures that were originated by such TALF Agent or any Related Person.

**VI. Questions and Comments**

Questions and comments made with respect to this guidance are encouraged by the FRBNY and may be submitted to the TALF Compliance Director via telephone at 1-212-720-2363 or via email at [talf.compliance@ny.frb.org](mailto:talf.compliance@ny.frb.org). This guidance is subject to change at any time.