

# FINANCIAL SERVICES ALERT

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## DEVELOPMENTS OF NOTE

### Senate Banking Committee Passes Dodd Bill

The Senate Banking Committee approved Senator Christopher Dodd's financial regulatory reform bill (the "Dodd Bill") on a 13-10 party-line vote, with no Republicans voting in favor of the Dodd Bill. For more on the Dodd Bill, please see our discussion of the proposed legislation in the [March 16, 2010 Alert](#). Though over 400 amendments had been prepared for the Committee's mark-up session, the Dodd Bill was approved in substantially the form that it had been introduced. Only a manager's amendment, which did not address the most controversial issues, was approved before the vote was taken on the Dodd Bill itself. Further amendments to the Dodd Bill are expected to be introduced during the debate on the Senate floor. The *Alert* will continue to follow the developments surrounding financial regulatory reform and any modifications to the Dodd Bill.

### FINRA Rulemaking Addressing Placement Agent Pay-to-Play Activities May Forestall Proposed SEC Ban on Adviser Use of Placement Agents to Solicit Government Entity Clients

In a March 15, 2010 letter to the staff of the SEC (the "FINRA Letter"), the FINRA staff agreed to create rules that would, in broad terms, allow its broker-dealer members to act as placement agents in soliciting government entities on behalf of investment advisers provided the placement agents observe prohibitions on "pay-to-play" activities conducted on their own behalf or on behalf of investment advisers employing them ("FINRA Pay-to-Play Rule"). The FINRA Letter appears to be an indication that the SEC is

considering limiting its proposed pay-to-play rule under the Investment Advisers Act of 1940 (the “Advisers Act”) which would prohibit an investment adviser from paying any third parties (*e.g.*, solicitors, finders, placement agents or pension consultants) to solicit a state or local government entity as an advisory client (the “SEC Pay-to-Play Rule”).

The SEC Pay-to-Play Rule was part of proposed regulations published by the SEC during the summer of 2009, which are designed to address practices that may influence the selection of an investment adviser to manage money on behalf of state and local government entities (*e.g.*, for public pension plans, retirement plans and 529 plans) (as discussed in the [August 18, 2009 Alert](#).) The FINRA Letter appears to be a response to a December 18, 2009 letter from the SEC staff asking FINRA to consider promulgating the FINRA Pay-to-Play Rule, with the apparent understanding that the final SEC Pay-to-Play Rule would contain an exemption permitting an adviser to retain FINRA members to act as placement agents in soliciting state and local government entities as advisory clients so long as they comply with FINRA Pay-to-Play Rule.

The FINRA Letter anticipates that the FINRA Pay-to-Play Rule would impose pay-to-play regulatory requirements as rigorous and as expansive as would be imposed by the SEC on investment advisers. In drafting the FINRA Pay-to-Play Rule, FINRA expects to draw closely upon all the substantive and technical elements of the SEC’s pay-to-play proposal as well as FINRA’s regulatory expertise in examining and enforcing the MSRB rules upon which the SEC’s proposal is based.

### **Wachovia Agrees to Penalties for Anti-Money Laundering Violations**

Wachovia Bank, N.A. (the “Bank”) agreed to penalties totaling \$160 million to resolve charges that it willfully failed to meet various anti-money laundering (“AML”) obligations by entering into a deferred prosecution agreement with the U.S. Attorney’s Office in the Southern District of Florida and consenting to penalties from the U.S. Treasury Department’s Financial Crimes Enforcement Network (“FinCEN”) and the OCC. The charges stemmed from a joint investigation into transactions conducted by the Bank with Mexican currency exchange houses, commonly known as “casas de cambio” (“CDC”). As explained by Comptroller of the Currency John Dugan, these actions are designed to send “another strong message that [regulators and law enforcement] will not tolerate the use of the U.S. financial system to launder illegal monies.”

According to the [press release](#) from the U.S. Attorney’s Office, the [consent order](#) issued by FinCEN, and [consent orders](#) for civil money penalties and to cease and desist (the “C&D Order”) issued by the OCC, the Bank was penalized for failing to apply adequate AML procedures to correspondent accounts maintained for the CDCs. In particular, the Bank did not effectively monitor transactions by CDCs through its “bulk cash,” “pouch” deposit, and “remote deposit capture” (“RDC”) services, allowing narcotics traffickers to move millions of dollars in funds through the Bank to recipients throughout the world. By not applying an effective risk-based system of controls to CDCs using these services, the Bank failed to detect and report potential money laundering and other suspicious activities, such as deposits of large volumes of large denomination sequentially numbered travelers checks. FinCEN and the OCC also cited the Bank for not properly applying enhanced due diligence procedures for correspondent accounts of foreign financial institutions, as required by Section 312 of the USA Patriot Act; failing to adequately staff the compliance units responsible for monitoring the Bank’s correspondent relationships; insufficiently covering bulk cash, cash letter, RDC, and pouch activities, and enhanced due diligence processes in

the Bank's internal audit program; and failing to report large currency transactions to the U.S. Treasury Department.

Under the deferred prosecution agreement, the Bank agreed to forfeit \$110 million to the United States government, which represents the proceeds of illegal narcotics sales that were allegedly laundered through the Bank. The Bank also agreed to the assessment of a \$110 million fine by FinCEN, which is deemed satisfied by the Bank's forfeiture to the U.S. government, and an additional \$50 million civil money penalty by the OCC. In addition, the Bank agreed in the C&D Order to take a range of steps to improve its AML compliance program. The C&D Order and the Bank's deferred prosecution agreement with the U.S. Attorney's Office bind Wells Fargo, as the Bank's successor, to implement these remedial measures following the Bank's merger into Wells Fargo.

### **Banking Agencies Issue a Final Policy Statement on Funding and Liquidity Risk Management**

The FRB, FDIC, OCC, OTS and NCUA, in cooperation with the Conference of State Bank Supervisors, (the "Agencies") jointly issued a final policy statement on the Agencies' expectations for financial institutions' ("FIs", and each an "FI") funding and liquidity risk management practices (the "Policy Statement"). The Agencies stated that the recent turmoil in the financial markets demonstrated the importance of good liquidity risk management in maintaining the safety and soundness of FIs. A proposed version of the Policy Statement was issued in July 2009 and discussed in the [July 7, 2009 Alert](#). The final Policy Statement summarizes and updates prior guidance issued by the Agencies concerning liquidity risk management and largely adopts the guidance included in the proposed version of the Policy Statement. The Policy Statement also, said the Agencies, "supplements [that prior guidance] with [applicable provisions in] the *Principles for Sound Liquidity Risk Management and Supervision* issued in September 2008 by the Basel Committee on Banking Supervision," which contains 17 principles concerning international supervisory guidance for sound liquidity risk management.

The Policy Statement stresses the importance of cash flow projections, diversified funding sources, stress testing, maintaining a cushion of liquid assets, intraday liquidity management and operating with a written, well-thought-through contingency funding plan as key elements of sound liquidity risk management.

The Policy Statement does not mandate specific liquidity levels, but states that an FI's liquidity management process should be tailored and sufficient to address the FI's funding and liquidity risk "using processes and systems that are commensurate with the [FI's] complexity, risk profile and scope of operations."

The Policy Statement deletes a prior requirement in the Agencies' guidance that separately regulated entities maintain liquidity on a stand-alone basis. The Agencies also provide in the Policy Statement a discussion of their expectations as to the manner in which the Board of Directors of an FI will meet its corporate governance responsibilities with respect to funding and liquidity risk management. Specifically, the Policy Statement states that an FI's Board of Directors should ensure that it:

- Understands the nature of the liquidity risks of its FI and periodically reviews information necessary to maintain this understanding.

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- Establishes executive-level lines of authority and responsibility for managing the FI's liquidity risk.
- Enforces management's duties to identify, measure, monitor, and control liquidity risk.
- Understands and periodically reviews the FI's [contingency funding plans] for handling potential adverse liquidity events.
- Understands the liquidity risk profiles of important subsidiaries and affiliates as appropriate.

The Policy Statement will become effective on May 21, 2010.

**Second Circuit Holds that FRB Must Release Information Relating to Loans to Financial Institutions**

The U.S. Court of Appeals for the Second Circuit (the "Second Circuit") held that the FRB must disclose the identity of borrowers, amount borrowed, loan origination and maturity dates and collateral given for loans made at the discount window or other financial assistance to financial institutions. The decision affirmed a district court ruling that had ordered the FRB to grant Bloomberg News' Freedom of Information Act ("FOIA") request seeking the release of documents disclosing such information. The FRB had denied the FOIA requests, asserting that the information was privileged and confidential and therefore exempt from disclosure. The Second Circuit held that the FOIA "sets forth no basis for the exemption the [FRB] asks us to read into it." The Second Circuit further stated that "[i]f the [FRB] believes such an exemption would better serve the national interest, it should ask Congress to amend the statute." Notably, the financial reform legislation that has passed the House and the financial reform bill pending in the Senate both would require the FRB to disclose such information. In a related decision, the Second Circuit held that the FRB must search the records of its Reserve Bank to comply with a separate FOIA request by Fox News LLC seeking information on loans to financial institutions. The FRB has indicated that it is considering its options for reconsideration or appeal of these decisions.

**OTHER ITEM OF NOTE**

**New ERISA Litigation Update Available**

Goodwin Procter's ERISA Litigation Practice published a new [ERISA Litigation Update](#), which discusses recent settlements and decisions and analyzes important trends affecting ERISA litigation.