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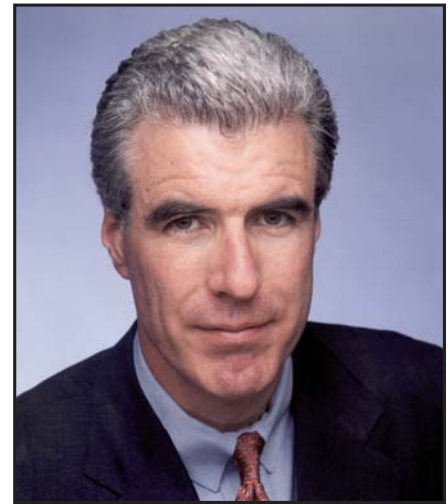
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Richard H. Girgenti



Michael R. Young

Neil Barofsky: Bringing Transparency To TARP

The Editor interviews Richard H. Girgenti, Principal and National Practice Leader for Forensic Services, KPMG LLP, and Michael R. Young, a litigation partner in the New York office of Willkie Farr & Gallagher LLP specializing in securities and financial reporting.

On July 28, Willkie and KPMG co-sponsored a special conference titled TARP Enforcement: The New Regulatory Regime, featuring a keynote address by Neil M. Barofsky, Special Inspector General for the Troubled Asset Relief Program ("SIGTARP"). TARP covers a multiplicity of programs, including the Capital Purchase Program ("CPP"), Term-Asset Backed Securities Loan Facility ("TALF"), Public-Private Investment Program ("PPIP"); Capital Assistance Program ("CAP"); Systemically Significant Failing Institutions Program ("SSFI"); Targeted Investment Program ("TIP"); Asset Guarantee Program ("AGP"); Automotive Industry Financing Program ("AIFP") and Making Home Affordable Program ("MHA"). It is overseen by

eight federal agencies. The conference program included two panel discussions: "Staying Out Of The Cross-Hairs: Using TARP And Its Related Programs," moderated by Mr. Young, and "Under Fire: Strategies For Navigating A TARP Investigation," moderated by Mr. Girgenti.

Editor: Please describe your respective roles in each of your organizations.

Girgenti: I am the National Head for the Forensic Practice of KPMG. My practice involves helping clients in a variety of ways, including assistance to the development of programs for prevention, detection and response in fraud and misconduct.

KPMG also plays a major role in serving the multifaceted needs of organizations involved with TARP and programs under its umbrella. These organizations' needs involve a variety of concerns, such as the adequacy of capital, mechanisms required to clean balance sheets of legacy assets, and

issues relating to public-private investments to help homeowners avoid foreclosure. With those multiple components there is considerable need for accounting and tax help because there are financial consequences depending upon each institution's circumstances.

In a closely related area, participants in TARP programs must conform to guidelines that require transparency, accountability and monitoring. They must have strong reporting processes, strong governance and strong compliance programs. Therefore, many of our clients need a wide range of assistance to help them with their governance, compliance and financial reporting requirements.

Young: I am a litigation partner at Willkie Farr & Gallagher and the Co-chair of the firm's Litigation Department and of its Securities Litigation and Enforcement practice group. My area of concentration deals

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For Your Company, For America**

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with financial reporting issues and regulatory enforcement. For example, I just completed service on the Principal Advisory Council to FASB where, among other things, we oversaw the development of the fair value accounting standards that are now being focused on by this new Inspector General of TARP. Along with KPMG, we see a number of issues coming down the pike in connection with TARP and TARP enforcement and thought it best to enable our clients and others to get ahead of the curve.

Editor: Would you also provide our readers with the reasons for the Willkie/KPMG Conference on TARP held on July 28? The new SIGTARP, Neil Barofsky, provided the keynote address. Why was he chosen?

Young: The new big thing seems to be TARP and TARP enforcement. TARP money is seemingly being “sprinkled,” although some might contend the better metaphor perhaps is “shoveled,” in all sorts of directions, and with the receipt of TARP money – whether an institution wants it or not – is the potential for examination by the new SIGTARP.

There is a lot of uncertainty as to how Mr. Barofsky will be going about his work – what he will do, what his mandate is and how will he interpret that mandate. By coincidence, some of our partners worked with Neil Barofsky both when he was with the Department of Justice and in private practice, and we thought this would be a good opportunity to allow TARP fund recipients and others concerned about TARP (and it’s a very wide category) to meet Neil Barofsky personally, to hear him talk about his agenda and his approach, and basically to take their measure of the man.

Editor: Why would they be so interested in Neil Barofsky? What duties does he have that would draw people to the conference, which I understand was very well attended?

Young: That’s a great question and it gets to the core of the concern about the TARP program. And that is you’ve got a Special Inspector General who is vested with significant powers. Keep in mind that his office consists of people who can carry firearms and issue warrants, and that they are building up their capability very quickly. A lot of lawyers know how to work with the SEC, the DOJ, the PCAOB and so forth. But this Special Inspector General is a new kind of enforcement animal, and the parameters of his function are not clearly circumscribed. Add to that the billions and billions of dollars swishing about in the TARP program and you see a real need and desire to understand, as well as it can be understood, what the TARP enforcement agenda is going to be and how it’s going to work.

Editor: How would they find anyone with a background that would enable him to do a job like that effectively?

Girgenti: Neil Barofsky’s appointment brings a person to the Inspector General’s position that has a vast amount of prosecutorial experience in the financial ser-

vices and mortgage areas. With a very, very broad jurisdiction, a very, sophisticated staff, alliances with other law enforcement and investigative agencies, and a clear mandate, his focus has already produced results.

He plans to grow his office from its current capacity of around 35 to more than double that. He is bringing in people who have law enforcement experience as well as auditing backgrounds. His reach extends far beyond his own office. He has developed alliances with the Inspectors General who have responsibility for the various TARP components as well as those for the principal regulatory agencies in the financial services area, including the FDIC and the Board of Governors of the Federal Reserve System. He has also been involved with building a task force consisting of the FBI, FinCEN, the IRS’s Criminal Division, the SEC and the U.S. Postal Inspection Service.

Young: I would add to that that Neil Barofsky also brings to his position tremendous energy and enthusiasm for his responsibilities as well as an obvious passion for transparency in the use of TARP funds. So you put everything that Rich has described together with that kind of approach and you are talking about a formidable enforcement capability.

Girgenti: Let me add that you need only look at Mr. Barofsky’s words and actions to demonstrate that. At the conference he said, “You can’t push out \$3 trillion without someone taking advantage of it. We want to make sure that those considering crossing the line know someone’s watching.” The result of such focus and the energy behind it is that since January of this year, Mr. Barofsky’s office has already brought two prosecutions, one of which was a criminal prosecution and the other a cease and desist order. He has also opened 35 investigations, and these investigations, according to his comments at the conference and his own reports, cover everything from tax evasion to insider trading to possible securities fraud.

Editor: Do you get the impression that TARP funds were just thrown at the banks and the investment banks to do as they will?

Young: Pursuant to the TARP program there were some pretty strict rules put in place as to particular uses of TARP money. On the other hand, not all of the constraints were necessarily spelled out, which gives rise to a very practical problem, and that is, exactly what can you do and not do with TARP money? Mr. Barofsky says that he’s on the lookout for waste, fraud and abuse, but what exactly does that mean? Therein lies some of the danger of receiving TARP funds.

As to his authorizing mandate as a matter of law, it’s been widely reported in the press that ferreting out waste, fraud and abuse is exactly what the SIGTARP is legally authorized to do. However, his level of independence and to whom he is to be accountable have been the subject of some vigorous discussion even within the government itself. The SIGTARP and the Treasury Department have not always seen eye to eye on those issues.

Suffice it to say that Mr. Barofsky views the law as providing him with a very very broad mandate, and he intends

to interpret that broadly. As he said at our conference: “I view the scope of our office very broadly.” And he’s made it clear that he’s going to cast a very broad look at what institutions are doing with TARP funds and whether, in his judgment, the funds are being used appropriately.

Girgenti: The statutes give Mr. Barofsky authority to conduct, supervise and coordinate audits and investigations of the purchase, management and sale of assets by the Secretary of Treasury, meaning all of the programs under which TARP operates. His authority is to conduct, supervise and coordinate these audits or take any action that he deems appropriate. He describes his goal as being to advance economic stability through transparency, through coordinated oversight and through robust enforcement against those, whether inside or outside the government, who waste, steal or abuse TARP funds. As Michael pointed out, that’s obviously already very broad – and Mr. Barofsky interprets that mandate very broadly – and he’s got the mechanisms behind him to pursue it. His office does the investigations and the audits. He then hands the cases over to the prosecutorial authorities (particularly the Department of Justice) where evidence has been developed that warrants a criminal prosecution or in some instances civil litigation.

Young: Rich just made several very important points, and let me build on one of them. He mentioned that the SIGTARP is looking for waste, fraud and abuse. If you stop there, there’s nothing really new about that. Lots of other inspectors general created by the government do that. What makes the SIGTARP different is that he views his mission as not simply to seek waste, fraud and abuse within government but to seek waste, fraud and abuse within the private sector. What exactly does that mean? We have a sense of what waste, fraud and abuse means when we’re talking about it within the government. But what is waste, fraud and abuse within the private sector? Is it a golf outing? Is it a business conference at an expensive resort? Is it excessive executive compensation? When you consider the potential ambiguity of the parameters of this concept and couple it with the formidable powers of the SIGTARP, you see the reason for the large attendance at our conference.

Editor: Given this broad mandate and vigorous inspection capability, exactly to whom is the SIGTARP accountable?

Young: That’s actually an interesting feature of this whole area and an issue on which not everybody within the government agrees. Treasury seemed to be of the view that the Inspector General was, to a meaningful extent, accountable to Treasury. But the Inspector General did not appear to share that view and presented the view that he was really accountable to Congress. Ultimately, as a matter of law, he can only be removed by the President of the United States. One of the interesting features of this is that Congress, or at least important members of Congress, seem to share more the Inspector General’s view of his accountability than that of the leadership of Treasury, and certainly as a practical matter some members of Congress have been

suggesting areas of useful inquiry to the Inspector General. The Inspector General has responded by undertaking those inquiries. So the whole apparatus seems to be involving not strict oversight by the particular governmental department at issue, that is Treasury, but a direct relationship between the Inspector General and leaders in Congress.

Editor: Tell us about the jockeying between Treasury and the SIGTARP.

Young: I don’t know if I would characterize it as jockeying, but take a step back and consider the completely understandable perspectives of the leadership of Treasury on the one hand and the SIGTARP on the other. Treasury wants to save the financial world, and I think we pretty much all support that objective. That effort includes making it as painless as possible for financial institutions to receive TARP funds. If the receipt of TARP funds becomes too painful then financial institutions simply will not want them and they will want to return any money they have already received – and we can actually see that happening for understandable reasons. The SIGTARP, on the other hand, appears to be a little less concerned with the discomfort of the receipt of TARP funds and more concerned with accountability for how those funds are used. It’s probably for that reason that the word Neil Barofsky seemed to use most at our conference was “transparency.” The view he expressed is that if institutions are going to take taxpayer funds, they ought to be transparent with regard to how those funds are being used.

Another point he made is that he’s gotten terrific cooperation from the financial institutions that have received TARP funds, and he was manifestly pleased and gratified by their willingness to cooperate with his office and to make information available. But if you think about the different perspectives and objectives of Treasury, on the one hand, and the Inspector General, on the other, you can see how well-meaning leaders can find themselves in the position in which they don’t completely agree on what the SIGTARP should be doing.

Editor: What kinds of things is the SIGTARP investigating? What are the challenges in compliance with TARP programs?

Young: The Inspector General is looking at the use of funds: he is inquiring into whether there were inappropriate external influences over the TARP application process; he’s looking at the process by which one major bank received TARP funds; he is looking at bonuses and whether in his judgment those raise issues; he’s looking at an insurance company’s payment to counterparties; he’s looking at the causes of the Chrysler bankruptcy — so he’s taken a very wide interpretation of the kinds of things he can look at.

Girgenti: In a recent SIGTARP report, Mr. Barofsky mentioned 35 criminal and civil investigations and also indicated that these investigations involved everything from suspected accounting fraud, securities fraud, insider trading, mortgage service or misconduct, mortgage fraud, public corruption, false statements and tax investigations.

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Young: He has an astonishing breadth of activity with what is really a pretty small crew compared to the work that it plans to do. Let me build on what Rich just said because these kinds of efforts take the SIGTARP in the direction of looking at such things as, for example, the fair valuation of financial instruments. Boy, there's a lot of opportunity for second-guessing judgments on something like that!

Editor: If you were a general counsel or financial vice president today of a company affected in some way by TARP, what steps would you be taking to avoid finding yourself in the Inspector General's cross-hairs?

Girgenti: If you're a general counsel or you're a board member or "C"-level officer, you're going to want to make sure that you meet the standards of the TARP program. They are pretty complex and broad in scope. We would advise our clients to ensure that they have proper controls and governance in place. They are going to be held accountable for explaining what they've done and how they've done it. This is all part of Mr. Barofsky's dedication to transparency and his desire to let people know that they have an Inspector General watchdog looking over their shoulder.

It's obvious to me that the folks in a corporation who are ultimately responsible for keeping it out of the SIGTARP's cross-hairs need to understand the restrictions on compensation. They are going to have to understand what their policies are relating to, and report effectively on, luxury expenses. They're going to have to ensure that they have an internal audit program around their TARP requirements. In some cases the banks' primary regulators are requiring them to implement an independent audit program – and some banks themselves are doing it in advance of any additional regulation and certainly are going to have to do it in anticipation of the audits that the SIGTARP is going to conduct.

The first thing that you generally do is try to understand what your organization's risks and challenges are as a result of participation in a particular TARP program. Each TARP program requires different approaches. Therefore, we help an organization with project management, we'll help them with the tools that they may need in addressing the accounting and tax considerations. We help them with risk frameworks, the compliance and control issues and developing mechanisms to avoid fraud, waste and abuse.

Let's take by way of example the Public-Private Investment Program, which was created to address the challenge of cleansing the balance sheets of financial institutions of legacy assets (often referred to as toxic assets). At the heart of the program is an asset evaluation designed to determine whether assets in the program are appropriately valued. There are issues around what the sellers will need and around whether there are proper operational controls prior to and through the transfer of any of these assets. Due diligence will be

required to avoid conflicts of interest. All of these tasks create trip wires in implementing the mandates of these programs for which they are getting funding, and all of these and many other things will be looked at very, very carefully by the regulators and certainly by the SIGTARP. Our clients have to make sure they can report that they are in compliance with the requirements of each of these specific programs. Remember there are 12 programs. They cover everything from funding for the automobile industry, funding for the Capital Assistance Program, funding for how we're going to handle the Loan Modification Programs. All these programs are very different, they are all very complex and they all need to be fully understood and complied with.

Editor: How does this interface with that certificate that the CEO and the CFO have to sign under Sarbanes-Oxley?

Girgenti: They are required under Section 404 of Sarbanes-Oxley to certify that they are familiar with the controls around their financial reporting and to their knowledge they have no issues with respect to deficiencies or any fraud with respect to that. To the extent that an investigation may reveal such deficiencies or fraud, it raises questions about the accuracy of their Section 404 certifications. This is something that corporate counsel has to be concerned about in connection with Section 404 certifications.

Editor: Does the False Claims Act, as amended by the Fraud Enforcement and Recovery Act of 2009 ("FERA"), provide a basis for bringing claims, in particular against recipients of TARP funds?

Girgenti: The big thing here is that the False Claims Act has been expanded and amended recently. It prohibits any individual from knowingly submitting any false claims for payment to the U.S. government. FERA extended liability to claims of indirect recipients of federal funds. Now, indirect recipients who defraud recipients of federal funds under TARP will come under the purview of the False Claims Act.

Editor: What are the standards for proving fraud under the False Claims Act?

Young: When you are talking, for example, about cases involving the valuation of financial instruments, that kind of issue can involve such extraordinary and fundamental levels of judgment that proving fraud can be very difficult – and it should be, because fraudulent conduct may not in fact have been involved. So is some fraud easy to prove? Sometimes, but a lot of times it can be more difficult.

Girgenti: Criminal liability might not even involve the necessity to prove a fraud. It's sufficient, and very often easier, for the government to prove that there was a falsification of a material fact simply by pointing to a false statement on an application for federal moneys or maybe on a survey that SIGTARP sends out to all financial institutions. The government does not have to prove a fraud. It has to

prove that there was a knowing false statement – and in some instances that can be a much easier path to criminal liability. Many states have also passed false claims acts. False claims acts – both state and federal – have become a powerful weapon for enforcing the integrity of claims for government funds.

Editor: What is the SIGTARP's role with respect to executive compensation?

Girgenti: Kenneth Feinberg, the new executive pay czar, is actually running that piece by presidential appointment. The SIGTARP will have to wait until the guidelines for executive compensation are available. Then the SIGTARP might get involved to the extent that there is noncompliance with their requirements.

Editor: Should institutions beyond those receiving TARP funds be interested in TARP and TARP enforcement?

Young: Absolutely. The more you think about the TARP program and the implications of TARP enforcement, the more you realize the proliferating number of categories of institutions and organizations that have reason to pay attention, beyond the TARP fund recipients themselves. Those that are contemplating the receipt of TARP funds or who might end up with TARP funds whether they are enthusiastic about receiving them or not is one such category. Those thinking about investing in institutions that have received TARP funds have reason to understand how the TARP program works and the risks posed by TARP

enforcement. You can expand beyond that to include insurers of those receiving TARP funds. You can think about auditors of the financial statements of those receiving TARP funds. You can even think about counterparties and those doing business with TARP fund recipients. Summing up, the range of those directly and indirectly affected by TARP is circumscribed only by your imagination.

Girgenti: In a recent KPMG fraud survey, a key finding was that a third of executives across all industries believe that fraud will rise in their organizations this year. I believe that there is a combination of factors that has resulted in the perception that fraud will increase.

One factor of course, is the times we're in, and the incredible economic pressures and individual pressures that companies and individual employees and officers are under.

Another factor conducive to fraud is that TARP involves an enormous infusion of money. Whenever you have trillions of dollars being infused into the economy you certainly have the opportunity for fraud.

The third piece, which goes right to the heart of the TARP program and the SIGTARP, is that you have an increased focus in this administration generally, and particularly with respect to TARP funding, on the creation of transparency wherever possible and enforcing accountability for how funds are going to be used.

Put the three together and you really have a toxic brew, if you will, that has gotten the attention of corporate America.

wilson international Law LLC
is pleased to announce

ERIC S. GALLER

formerly senior vice president
and general counsel of global secure corp.,
has joined the firm as a partner

and

ELENA RYZHKOVA

has joined the firm as an associate.

Mr. Galler is admitted to practice in Maryland, Washington, DC and before the United States Supreme Court.

Ms. Ryzhkova is admitted to practice in Virginia, and is awaiting admission in New York and Washington, DC.

William A. Wilson III, founder of the firm, is admitted to practice in Hong Kong, New York, Connecticut and Washington, DC.

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