

Financial Services Alert

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Developments of Note

➤ **FDIC Issues Final Rule Adopting and Modifying its Temporary Liquidity Guarantee Program**

The FDIC issued a final rule (the "Final Rule") adopting and modifying its Temporary Liquidity Guarantee Program (the "TLGP"). On October 13, 2008 (and as described in the October 14, 2008 *Alert*), the FDIC adopted and requested public comment on an Interim Rule establishing the TLGP. The FDIC said that it established the TLGP "to decrease the cost of bank funding so that bank lending to consumers and businesses will normalize." The TLGP has two components: (i) a guarantee of newly issued senior unsecured debt of any FDIC-insured depository institution and certain bank and savings and loan holding companies engaged only in financial activities (the "Debt Guarantee Program"); and (ii) full deposit insurance coverage of non-interest bearing deposit transaction accounts, regardless of dollar amount (the "Transaction Account Guarantee Program") The TLGP is funded through fees charged to participating financial institutions rather than through taxpayer funds or through the FDIC's Deposit Insurance Fund.

The key changes made in the Final Rule from the TLGP's Interim Rule are:

A. Debt Guarantee Program

- To add value to the guarantee and help banks obtain lower cost funding, the debt guarantee will be triggered by payment default rather than by bankruptcy or receivership.
- A banking organization's senior unsecured debt of less than 30 days' maturity will not be guaranteed under the TGLP.
- The FDIC confirmed that guarantees under the TLGP, just as FDIC coverage for deposits, will be backed by the full faith and credit of the U.S. Government.
- The 75 basis point flat fee for the debt guarantee is replaced with a sliding scale fee structure: 50 basis points for debt with maturities of 180 days or less; 75 basis points for debt with maturities of 181 days to 364 days; 100 basis points for debt with maturities of 365 days or longer. Also a 10 basis point surcharge for holding companies whose insured depository institutions represent less than 50% of their total assets.

- A bank that had no outstanding unsecured debt on September 30, 2008 may participate with new debt equal to up to 2% of its total liabilities.
- A banking institution can opt-out of the TLGP until December 5, 2008.

B. Transaction Account Guarantee Program

- NOW accounts with interest rates of 0.5% or less and IOLTAs (lawyers' trust accounts established for moneys of the lawyers' clients) whose interest does not accrue to the account owner have been added as types of account that will be covered by this program.
- Banking organizations will not have to aggregate accounts in determining coverage. Only balances over \$250,000 in transaction accounts will be covered and assessed, regardless of the account ownership.

For the Transaction Account Guarantee Program, the annual fee of 10 basis points and the expiration of coverage on December 31, 2009 were unchanged from the Interim Rule.

➤ **Further Update on U.S. Treasury's Temporary Guarantee Program for Money Market Funds**

As discussed in several recent editions of the *Alert*, the U.S. Treasury is providing a temporary guarantee program for certain money market funds (the "Treasury Program"), in which the Treasury will guarantee the value of the shares of participating funds that were owned by beneficial owners as of the close of business on September 19, 2008. Three recent developments for the Treasury Program are summarized below.

Extension of the Treasury Program. The Treasury announced that it is extending the Treasury Program until April 30, 2009. Only money market funds currently participating in the Treasury Program may participate in the extension, and the guarantee only will extend to those shares of participating funds that were owned by beneficial owners as of the close of business on September 19, 2008. To participate in the extension of the Treasury Program, a fund must meet the following conditions: (a) no Guarantee Event shall have occurred before December 19, 2008, the program extension date, (b) the fund's market-based net asset value per share must be at least \$0.9950 (or for a stable value fund, its Guaranteed Threshold Value), and (c) the fund's board of directors/trustees, including a majority of its disinterested directors/trustees, must have determined that participating in the Treasury Program extension is in the best interests of the fund and its shareholders.

Participating funds have **until 11:59 p.m. Washington, D.C. time, December 5, 2008** to submit a completed and executed Program Extension Notice and a Bring-Down Notice (Exhibits A and B, respectively, to the Treasury's extension notice), as well as the full program extension payment, to participate in the extension to April 30, 2008. All documents must be sent to the Treasury by e-mail. The amount of the payment for the extension period will be based on the participating fund's net asset value per share as of September 19, 2008, and is determined as follows:

- If the participating fund's market-based net asset value per share is at least 99.75% of its stable share price, the payment due is 0.015%, or 1.5 basis points, multiplied by the number of shares outstanding on September 19, 2008.
- If the participating fund's market-based net asset value per share is less than 99.75%, but at least 99.50%, of its stable share price, the payment due is 0.022%, or 2.2 basis points, multiplied by the number of shares outstanding on September 19, 2008.

The Treasury may make further extensions of the Treasury Program until September 18, 2009, but it has not announced any decision to extend the program past April 30, 2009. Any fund currently participating in the Treasury Program that elects not to participate in the extension to April 30, 2009 will not be permitted to participate in any further extension.

ICI Publishes Further Clarifications by the Treasury, SEC and FINRA Related to the Treasury Program. Since adoption of the Treasury Program, the Treasury, the SEC and FINRA have held periodic discussions with the Investment Company Institute (the “ICI”) to clarify, among other things, how certain laws and regulations are to apply to funds participating in the Treasury Program. A summary of some of those discussions was included in the October 14, 2008 *Alert*. Recently, the ICI held additional discussions with the Treasury, SEC and FINRA, in which it reported the following.

- A fund that is participating in the Treasury Program must continue to include the legend that states that an investment in the fund is not insured or guaranteed by the FDIC or any other agency, and that although the fund seeks to preserve the value of shareholder investments at \$1.00 per share, it is possible to lose money by investing in the fund (the “Required Money Market Fund Legend”). However, the fund also must disclose its participation in the Treasury Program by sticker or post-effective amendment information, and after the Required Money Market Fund Legend may provide a brief description of the guarantee provided to certain shareholders.
- Rule 482 advertisements and Rule 34b-1 supplemental sales materials, which also must incorporate the Required Money Market Fund Legend, may include immediately after the Required Money Market Fund Legend a brief description of the Treasury guarantee, provided that that description is followed by a statement that the guarantee does not apply to new investments made after September 19, 2008, the guarantee is scheduled to expire on December 18, 2008, and the reader should see the fund’s prospectus for more information about the Treasury Program.
- Sales materials that discuss the Treasury Program other than as described above should provide in substance the descriptive and cautionary information recently provided in FINRA Regulatory Notice 08-58 relating to NASD Rule 2210 (which was discussed in the October 28, 2008 *Alert*).
- Re-registrations and transfers of a shareholder account originally covered by the Treasury Program that occur after September 19, 2008 will be continue to be covered by the Treasury Program if the re-registration and transfer involve a shareholder’s estate or successor by will, intestacy, gift, court order or court approved settlement. Any other transfer of shares from one ownership structure to another will be deemed to be a new investment made after September 19, 2008, and ineligible for coverage under the Treasury Program.

SEC Publishes Interim Rule Providing Relief to Money Market Funds Participating in the Treasury Program Relating to Redemption Payments on Liquidation. The SEC has adopted temporary Rule 22e-3T to permit a money market fund that has commenced liquidation under the Treasury Program to suspend redemptions temporarily and postpone payment of redemption proceeds notwithstanding the limit on postponing redemption payments in Section 22(e) of the Investment Company Act of 1940, as amended (the “1940 Act”). Under the Treasury Program, a money market fund that experiences a “Guarantee Event” (e.g., “breaks a buck”) generally is required to initiate the actions necessary under applicable law to commence the liquidation of the fund within five business days following the Guarantee Event, and liquidate within thirty days. Section 22(e) of the 1940 Act prohibits a registered investment company, which would include a money market fund, from suspending the right of redemption, or postponing redemption payments for more than seven days, absent certain specified exemptions or an SEC order. Rule 22e-3T is intended to relieve funds from having to apply for an individual order or no-action relief under Section 22(e) if they experience a Guarantee Event. In general, the temporary rule will exempt a money market fund participating in the Treasury Program from the requirements of Section 22(e) provided that the fund (a) has delivered to the Treasury notice that it has experienced a Guarantee Event and will promptly commence liquidation under the terms of its agreement with the Treasury, and (b) has not cured the Guarantee Event, as provided under the terms of its agreement with the Treasury. Rule 22e-3T expires on October 18, 2009, that is, thirty days beyond the last date to which the Treasury may extend the Treasury Program.

➤ **OCC Grants Its First Conditional Preliminary Approval of a National Bank “Shelf-Charter”**

The OCC granted a conditional preliminary approval of a new type of national bank non-operating “shelf-charter,” thereby helping to expand the pool of potential equity and other investors in troubled banks and thrifts.

Currently, potential investors are required to control an operating bank or thrift in order to have access to the FDIC’s non-public list of failing or troubled banks and thrifts and to participate in the FDIC-run auctions for these troubled institutions. By granting preliminary approval for a national bank “shelf-charter”, the OCC effectively permits the participation of new investors and the infusion of new equity capital by allowing these new investors to participate in a process that, previously, only allowed access to investors already holding bank charters.

Under this new charter mechanism, the OCC initially evaluates the qualification of the proposed management team, the sources and amount of capital that would be available to the troubled institution and a “streamlined” business plan that discusses the operation of the acquired institution. The OCC may then grant conditional preliminary approval of a national bank charter, thereby, permitting the investor to participate in the FDIC’s process. The OCC is likely to subject the final approval of the preliminary charter to various conditions and requirements, including submission of a more detailed operating plan satisfactory to the OCC. A preliminary charter remains “on the shelf” for up to 18 months and can be used for multiple bids during that period.

If the holder of a “shelf-charter” is selected by the FDIC to acquire a failing or troubled bank, and the OCC accepts the detailed operating proposal, the OCC may then remove the preliminary charter from “the shelf” and grant final approval of the national bank charter subject to final approval of deposit insurance by the FDIC.

While certainly showing some progress with the OCC, an investor who participates in a “shelf-charter” process must also carefully consider whether it may be required to register as a bank holding company, particularly given the FRB’s views of “whole bank” acquisitions, as well as whether it will remain subject to other regulatory requirements.

➤ **SEC Staff Provides No-Action Relief from Prohibition on Past Specific Recommendations to Permit Adviser Advertising with Best and Worst Performers Information**

The staff of the SEC’s Division of Investment Management (the “Staff”) provided no-action relief to a registered adviser seeking to include information in advertising materials on how its best performing and worst performing security selections affected the performance of an investment strategy the adviser provides to its clients. Rule 206(4)-1(a)(2) under the Investment Advisers Act of 1940, as amended (the “Advisers Act”), prohibits a registered adviser from using any advertisement that refers to past specific recommendations that were or would have been profitable unless the advertisement includes or offers to furnish a list of all the adviser’s recommendations with specified information for each recommendation. The Staff has previously provided no-action relief from the prohibition in Rule 206(4)-1(a)(2) to allow an adviser to use an advertisement that contained information regarding the performance of selected securities recommendations provided they were chosen based on “objective, non-performance based criteria consistently applied.”

The current no-action relief broadens the scope of permitted securities recommendations presentations by allowing an ad to show securities recommendations selected based on their performance, albeit subject to a number of conditions. For an identified investment strategy, an adviser must select no fewer than ten individual holdings from a representative account, consisting of an equal number of (a) holdings that most positively contributed to the account’s return for the period and (b) holdings that most negatively contributed to the account’s return for the period. Holdings must be selected solely on the basis of a calculation that multiplies a holding’s weight in the portfolio for the period by its rate of return for that period. The presentation must provide both the average weight of the holdings during the

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Mark S. Raffman
Derek N. Steingarten
William E. Stern
Michael P. Whalen

To e-mail any of the above attorneys, use first initial of first name followed by last name followed by @goodwinprocter.com. For example, the e-mail address for Gregory J. Lyons would be glyons@goodwinprocter.com

period and the contribution of the holdings to the representative account's return. The presentation of that information and number of holdings shown must be consistent from period to period. The advertisement must disclose how to obtain (a) the methodology for selecting the securities shown and (b) a list showing the contribution of each holding in the representative account to that account's performance during the period. The best and worst performing holdings must be shown on the same page with equal prominence, with legends disclosing that the holdings identified do not represent all of the securities purchased, sold or recommended for advisory clients, and past performance does not guarantee future results. An adviser that uses advertising containing past specific securities recommendations in reliance on the no-action relief must maintain specified supporting documentation for each ad and make it available for inspection by SEC personnel. The no-action relief cautions that an advertisement complying with its terms must, nevertheless, also comply with the general anti-fraud provisions of the Advisers Act and its rules.

Other Item of Note

➤ **SEC Votes to Adopt Mutual Fund Summary Prospectus Proposal**

At its open meeting on Wednesday, November 19, 2008, the SEC voted to adopt its "Summary Prospectus" proposal, which (i) revises the disclosure requirements for the statutory prospectus currently used by registered open-end management investment companies ("mutual funds") and (ii) creates the new Summary Prospectus for use in mutual fund sales. The revisions to mutual fund disclosure requirements create a brief, self-contained presentation of key fund characteristics that will appear in both the current statutory prospectus and the new Summary Prospectus. Funds will be able to use the Summary Prospectus to satisfy certain prospectus use and delivery requirements under the Securities Act of 1933, as amended, subject to several conditions that include providing investors access to the statutory prospectus and other fund documents via the Internet. (For a detailed discussion of the SEC's original proposal, see the December 5, 2007 *Alert*.) As stated in the press release announcing this SEC action, the rule changes are effective on February 28, 2009, and funds must begin complying with the form changes on January 1, 2010. The *Alert* will provide a more detailed description once an adopting release with full details of the proposal becomes publicly available.

