TOO BIG TO MITIGATE? THE RISE OF ORGANIZATIONAL CONFLICTS OF INTEREST IN ASSET MANAGEMENT

Megan A. Bartley

I. INTRODUCTION

In March 2008, the equivalent of an economic fire alarm went off on Wall Street. Battered by a string of losses tied to mortgage securities, Bear Stearns, the

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Megan A. Bartley (mbartley@law.gwu.edu) is the student editor-in-chief of the Public Contract Law Journal *and expects to receive her J.D. from The George Washington University Law School in May 2011.* *She would like to thank Bill Speros and Diane Baldwin for their insight and valuable editing on this Note and her husband Matthew for his patience and support throughout law school. This Note was selected as the second-place winner of the 2010 Division I ABA Public Contract Law Writing Competition.*

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nation's fifth largest investment bank,[1] alerted the U.S. Government that it was facing immediate bankruptcy.[2] The Government faced a difficult decision: Let Bear Stearns fail and risk a ripple effect throughout the economy, or intervene and prevent further instability.[3] Fearing Bear Stearns was "too big to fail,"[4] the Federal Reserve Bank of New York ("FRBNY")[5] and the Treasury Department ("Treasury") facilitated a deal in which JPMorgan Chase ("JPMorgan") would buy Bear Stearns to avoid its collapse, and the Government would assume liability for $29 billion of Bear Stearns' "toxic" assets.[6]

1. *See* Gary Shorter, Cong. Research Serv., RL 34420, Bear Stearns: Crisis and "Rescue" for a Major Provider of Mortgage-Related Products 1 (2008) [hereinafter Bear Stearns: Crisis and "Rescue"].

2. On March 13, 2008, Bear Stearns informed the Federal Reserve that it "would have to file for Chapter 11 bankruptcy the next day unless alternative sources of funds became available." *The Economic Outlook*: *Hearing Before the J. Econ. Comm*., 110th Cong. 12 (2008) (statement of Benjamin Bernanke, Chairman, Federal Reserve). The "Federal Reserve" refers to the Federal Reserve System, which is composed of a central, governmental agency (the Board of Governors) and twelve regional Federal Reserve Banks. The Board and the Reserve Banks jointly supervise and regulate financial institutions and provide banking-related services to banks and the Federal Government. Bd. of Governors of the Fed. Reserve Sys., The Federal Reserve System: Purposes and Functions 3 (2005), *available at* http://www.federalreserve.gov/pf/pdf/pf_1.pdf.

3. The chairman of the Federal Reserve said, "the sudden failure of Bear Stearns likely would have led to a chaotic unwinding . . . [that] could have been severe and extremely difficult to contain." *The Economic Outlook*, *supra* note 2.

4. The "too-big-to-fail" doctrine reflects the fear that "if a large bank fail[s] . . . the entire banking system might be endangered." Daniel K. Tarullo, Governor of the Fed. Reserve, Speech at the Exchequer Club (Oct. 21, 2009), http://www.federalreserve.gov/newsevents/speech/tarullo20091021a.htm. Bear Stearns was the first investment bank, as opposed to commercial bank, that the Government decided was too big to fail. James Surowiecki, *Too Dumb to Fail*, New Yorker, Mar. 31, 2008, at 46, *available at* http://www.newyorker.com/talk/financial/2008/03/31/080331ta_talk_surowiecki. As some commentators noted, Bear Stearns might have been more accurately described as "too important to fail." *Id*.

5. The Federal Reserve Bank of New York ("FRBNY") is one of the twelve regional banks of the Federal Reserve. The regional banks carry out the day-to-day functions of the Federal Reserve. Pauline Smale, Cong. Research Serv., RS 20826, Structure and Functions of The Federal Reserve System 2, 4 (2005). This Note refers primarily to the FRBNY because it was responsible for contracting with asset management firms. *See Vendor Information*, Fed. Reserve Bank of N.Y., http://www.newyorkfed.org/aboutthefed/vendor_information.html (last visited Oct. 17, 2010) [hereinafter FRBNY Vendors] (listing the contracts for which the FRBNY is responsible). However, where appropriate, references to the Federal Reserve indicate that the described action or policy is attributable to the Federal Reserve as a whole.

6. The deal called for the FRBNY to loan JPMorgan Chase ("JPMorgan") $29 billion; in return, the FRBNY received $30 billion in assets as collateral. Bear Stearns: Crisis and "Rescue," *supra* note 1, at 7; *see also* Edmund L. Andrews, *In Sweeping Move*, *Fed Backs Buyout and Wall St. Loans*, N.Y. Times, Mar. 17, 2008, at A1, *available at* http://www.nytimes.com/2008/03/17/business/17fed.html (noting "[i]n a highly unusual maneuver," the Federal Reserve extended a $30 billion credit line to help JPMorgan acquire Bear Stearns). JPMorgan took the risk of the first $1 billion in losses, and the FRBNY assumed the rest. *See* Press Release, Fed. Reserve Bank of N.Y., Statement on Financing Arrangement of JPMorgan Chase's Acquisition of Bear Stearns (Mar. 24, 2008), http://www.newyorkfed.org/newsevents/news/markets/28/rp080324.html [hereinafter FRBNY Bear Stearns Statement]. The "toxic," or troubled, assets consisted of a "complex hodgepodge of souring commercial-property loans, securities backed by U.S. subprime loans, credit insurance written on troubled bond and mortgage insurers and loans tied to struggling hotels." Carrick Mollenkamp et al., *Mortgage Problems? Fed Can Relate*, Wall St. J., Apr. 2, 2010, at C1. An estimated $20 billion of the assets were mortgage-backed securities. *See* Bear Stearns: Crisis and "Rescue," *supra* note 1, at 7.

The Government's unprecedented action rocked Wall Street and signaled that a larger economic crisis might be at hand. Less attention was paid, however, to what the implications would be for the Government's increasingly complex relationship with private firms. At the time of the Bear Stearns deal, fundamental, yet elusive, questions remained about how the Government would manage billions in unstable assets: What were the assets worth? How "toxic" were they? Could the Government earn a return on its investment?[7] To answer these questions, the FRNBY turned to BlackRock, a well-known asset management firm.[8] BlackRock's expertise was crucial to the Bear Stearns deal. BlackRock initially provided valuations of the Bear Stearns assets before JPMorgan agreed to the deal, and then BlackRock agreed to manage the assets for the FRBNY.[9]

At the time of the Bear Stearns collapse, Blackrock's role in the sale and management of the assets may have seemed to be an anomaly—the rare consequence of a major investment bank failure. Throughout the ensuing economic crisis, however, the Government continued to engage private asset management firms to manage federally backed, troubled assets. Today, BlackRock's contract to manage the Bear Stearns assets is not an anomaly, but rather one of many instances in which the Government turned to asset management firms to value and manage the risky assets of financial institutions that the Government sought to rescue.

Despite the fact that the agreements between Blackrock and the FRBNY are essentially government contracts, these and similar agreements have largely eluded traditional procurement oversight. Given that the same firm may be in a position to set the value of an asset and subsequently manage that asset for the Government, agreements between asset management firms and government entities ("asset management contracts") create the potential for significant organizational conflicts of interest ("OCIs"). OCIs arise when an entity's ability to give impartial advice or objectively perform a contract is impaired, or when the entity otherwise gains an unfair competitive advantage regarding a contract.[10] In other words, an OCI arises when "an entity plays

7. *See, e.g.*, Vikas Bajaj, *Rescue Plan's Basic Mystery: What's All This Stuff Worth?*, N.Y. Times, Sept. 25, 2008, at A1, *available at* http://www.nytimes.com/2008/09/25/business/25value.html ("[T]he difficulty in valuing these assets could result in the government's buying them for more than they will ever be worth, a step that would benefit financial institutions at taxpayers' expense.").

8. BlackRock is the world's largest asset manager, and is now responsible for managing more than $3 trillion in assets. Sree Vidya Bhaktavatsalam, *BlackRock Completes $15.2 Billion Acquisition of BGI*, Bloomberg, Dec. 1, 2009, *available at* http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aCbcy4lbAAyk.

9. *See infra* Part II.A.

10. The FAR defines an OCI as a conflict that arises when "a person is unable or potentially unable to render impartial assistance or advice to the Government, or the person's objectivity in performing the contract work is or might be otherwise impaired, or a person has an unfair competitive advantage." FAR 2.101. The FAR's use of the term "person" is a misnomer, as OCIs arise at the organizational level. Keith R. Szeliga, *Conflict and Intrigue in Government Contracts: A Guide to Identifying and Mitigating Organizational Conflicts of Interest*, 35 Pub. Cont. L.J. 639, 640 n.1 (2006).

two or more roles that are, in some sense, at odds with one another."[11] In asset management contracts, these conflicting roles are often present: Asset management firms set the values for assets, manage the assets for a government entity, and often invest in the same assets for private clients. The task of identifying and mitigating OCIs in government procurement is not easy to begin with, as the Federal Acquisition Regulation (FAR) provides agencies with only minimal guidance on OCIs.[12] In the asset management context, it is even more daunting. A lack of a clear regulatory framework, the Government's need to provide economic stability, and a shortage of trusted firms make these contracts particularly susceptible to OCIs.

This Note examines the potential for OCIs in asset management contracts ("asset management OCIs") and the obstacles to mitigating them. Part II describes how asset management OCIs arise, using BlackRock's asset management contracts with the Government as a case study. Part III then analyzes the existing, although inconsistent, approaches for mitigating OCIs and examines how asset management contracts after the economic crisis asset are especially susceptible to OCIs. Lastly, Part IV considers the challenges of mitigating asset management OCIs and examines whether OCIs in asset management can be effectively mitigated.

II. A CASE STUDY: BLACKROCK, THE "GO-TO" FIRM[13]

Throughout the economic crisis, the Government took drastic action to prevent major banks from collapse. While the primary step was extending loans to financial institutions, the Government also assumed liability for many firms' troubled assets.[14] To manage those assets, the Government relied on a small group of asset management firms,[15] but a favorite firm emerged: BlackRock. BlackRock "effectively bec[a]me the leading manager of Washington's bailout of Wall Street,"[16] securing more government contracts

11. Daniel I. Gordon, *Organizational Conflicts of Interest: A Growing Integrity Challenge*, 35 Pub. Cont. L.J. 25, 26 (2005). OCIs are a "subset" of conflicts of interest. *Id.* at 28.

12. *See generally* FAR 9.5; discussion *infra* Part III.

13. *See* Kambiz Foroohar & Sree Vidya Bhaktavatsalam, *BlackRock Is Go-To Firm to Divine Wall Street Assets*, Bloomberg, May 8, 2009, *available at* http://www.bloomberg.com/apps/news?pid=20601014&sid=a6TJmW9R44yc (quoting a managing director at UBS that "BlackRock has established itself as the go-to firm when you have problems").

14. The primary function of the Troubled Assets Relief Program ("TARP"), enacted as part of the Emergency Economic Stabilization Act ("EESA"), is to allow the Government to purchase up to $700 billion in troubled assets. *See* U.S. Gov't Accountability Office, GAO-10-16, Troubled Asset Relief Program: One Year Later, Actions Are Needed to Address Remaining Transparency and Accountability Challenges 1 (2009) [hereinafter One Year Later].

15. For instance, the FRBNY has also contracted with other well-known asset management firms, including Wellington Management Co.; Pacific Investment Management Co., LLC ("PIMCO"); and Goldman Sachs Asset Management. *See* FRBNY Vendors, *supra* note 5.

16. Suzanna Andrews, *Larry Fink's $12 Trillion Shadow*, Vanity Fair, Apr. 2010, *available at* http://www.vanityfair.com/business/features/2010/04/fink-201004.

than any other asset management firm.[17] BlackRock is now responsible for overseeing, evaluating, or advising on more than $6 trillion in assets owned or backed by the Government.[18]

BlackRock is not the only asset manager to contract with the Government in response to the economic crisis, but its contracts provide a striking example of the potential for asset management OCIs. The Government relies on asset management firms to determine what the toxic assets are worth and uses the same firm to buy, sell, or provide investment advice in a way that will provide the best return to the taxpayer.[19] While there is little doubt that BlackRock is a trusted asset management firm,[20] the potential for OCIs raises the question of whether BlackRock is the best contractor for the Government and the U.S. taxpayer.

A. *The Bear Stearns Assets*

When the FRBNY turned to BlackRock to manage the Bear Stearns assets, it was scrambling to finalize a deal over the weekend before the markets opened.[21] JPMorgan's purchase of Bear Stearns was contingent on the FRBNY taking on the risk of the troubled Bear Stearns assets.[22] Because valuing and managing such complex assets was beyond the FRBNY's expertise,[23] the chairman of the FRBNY contacted BlackRock.[24] BlackRock's valu-

17. Sree Vidya Bhaktavatsalam & Christopher Condon, *BlackRock to Earn $71 Million to Oversee Maiden Lane*, Bloomberg, July 14, 2009, *available at* http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aqOVY76FQxCk; *see also* Andrews, *supra* note 16 (noting "it is hard to argue that anyone, or any firm on Wall Street, gained as much stature from the economic crisis as did . . . BlackRock").

18. While there are different ways to measure the value of the assets, which vary depending on the market and other factors, some have tallied BlackRock's total management of the troubled assets held by Fannie Mae and Freddie Mac alone at $5 trillion. *See* Andrews, *supra* note 16. This figure does not include the more than $1 trillion in assets resulting from the Government's involvement in the Bear Stearns and AIG transactions, and the Government's attempts to revive the U.S. housing market. *Id*.

19. *See* Elana Schor, *Government Taps Bailout Contractors with Conflicts of Interest*, Wash. Indep. (May 29, 2009), http://washingtonindependent.com/44659/fed-taps-bailout-contractors-with-conflicts-of-interests ("Investment managers are setting values for securities that their companies may also hold privately.").

20. Andrews, *supra* note 16 (noting BlackRock is trusted on Wall Street because "BlackRock only trades money that belongs to its clients [and] unlike other Wall Street C.E.O.'s . . . [BlackRock's President] Fink is perceived as objective").

21. Kate Kelly, *Inside the Fall of Bear Stearns*, Wall St. J., May 9, 2009, at W3 (noting the Government "raced the clock through the weekend to sell Bear Stearns" and solidified a deal in 72 hours, announcing it at 7:05 p.m. on Sunday night).

22. *See* Bear Stearns: Crisis and "Rescue," *supra* note 1, at 6 (noting the FRBNY's role was "deemed necessary to overcome JP Morgan's reluctance to taking on much of Bear's risky portfolio of complex mortgages and other questionable investments"); Andrews, *supra* note 6, at A1 (noting that "the principal issue, according to officials, was how much insurance [the FRBNY] was willing to provide JPMorgan Chase in exchange for taking over Bear Stearns and its hard-to-quantify assets").

23. *See* Jo Becker & Gretchen Morgenson, *Member and Overseer of Finance Club*, N.Y. Times, Apr. 27, 2009, at A1 (noting the FRBNY "needed [BlackRock's] expertise").

24. *See* Foroohar & Bhaktavatsalam, *supra* note 13.

ation became the linchpin for the deal. There was no way to determine if BlackRock's valuation was reliable, nor was there time. The FRBNY relied on BlackRock's evaluation of the assets "even though those values were almost certain to decline as the economy deteriorated."[25] JPMorgan hired BlackRock to evaluate some of Bear Stearns's assets prior to agreeing to the sale, and the next day, the FRBNY hired BlackRock to analyze and manage the assets that the FRBNY would take on as part of the agreement.[26]

The details of the FRBNY's contract with BlackRock were not established until a later date,[27] but BlackRock's responsibility was to manage the assets in a way that would facilitate the return of the Government's $29 billion.[28] The FRBNY established a special lending vehicle, Maiden Lane LLC, that owns the assets, but which the FRBNY controls.[29]

B. *Additional BlackRock Contracts*

Six months after facilitating Bear Stearns' rescue, the FRBNY stepped in to save the insurance giant American International Group ("AIG") from collapse.[30] Once again, the Government turned to BlackRock, awarding BlackRock two contracts to manage more than $50 billion in troubled AIG assets.[31] BlackRock has also received a contract to manage troubled securities

25. Becker & Morgenson, *supra* note 23, at A1. Indeed, long after the sale of the Bear Stearns assets, questions lingered about the actual value of the assets. The FRBNY released detailed information for the first time on the specific holdings of the assets at the end of March 2010. *See* Press Release, Fed. Reserve Bank of N.Y., New York Fed Releases Additional Information on Maiden Lane Portfolios (Mar. 31, 2010), http://www.newyorkfed.org/newsevents/news/markets/2010/ma100331.html.

26. Eric Lipton & Michael J. de la Merced, *Wall St. Firm Draws Scrutiny as U.S. Adviser*, N.Y. Times, May 19, 2009, at A1, *available at* http://www.nytimes.com/2009/05/19/business/19blackrock.html.

27. *See* Becker & Morgenson, *supra* note 23, at A1 ("Indeed, the deal was cut so quickly that they worked out the fees only after the firm was hired."). The FRBNY at the time of the deal said only, "BlackRock Financial Management Inc. has been retained by the New York Fed to manage and liquidate the assets." Press Release, Fed. Reserve Bank of N.Y., Summary of Terms and Conditions Regarding the JPMorgan Chase Facility (Mar. 24, 2008), http://www.newyorkfed.org/newsevents/news/markets/2008/rp080324b.html [hereinafter FRBNY Bear Summary].

28. *See* Becker & Morgenson, *supra* note 23, at A1.

29. *See Maiden Lane Transactions*, Fed. Reserve Bank of N.Y., http://www.newyorkfed.org/markets/maidenlane.html (last visited Nov. 2, 2010) [hereinafter *Maiden Lane Transactions*]; Investment Manager Agreement by and among Fed. Reserve Bank of N.Y. and Maiden Lane LLC 15 (June 24, 2010) [hereinafter BlackRock Maiden Lane Agreements], *available at* http://www.ny.frb.org/aboutthefed/Blackrock_ML.pdf. Maiden Lane LLC is named after a street adjacent to the FRBNY's lower Manhattan headquarters. Serena Ng & Carrick Mollenkamp, *Fed Opens the Books on Bear, AIG Toxic Assets*, Wall St. J., Apr. 1, 2010, at C1.

30. The FRBNY extended an $85 billion loan to AIG. *See* Edmund L. Andrews et al., *Fed in an $85 Billion Rescue of an Insurer Near Failure*, N.Y. Times, Sept. 17, 2008, at A1, *available at* http://www.nytimes.com/2008/09/17/business/17insure.html; *see also* Gretchen Morgenson, *Your Money at Work: Fixing Others' Mistakes*, N.Y. Times, Sept. 21, 2008, at BU1, *available at* http://www.nytimes.com/2008/09/21/business/21gret.html (noting "if A.I.G. were to fail . . . the ripple effect could have turned into a tsunami").

31. BlackRock received two contracts from the FRBNY to manage the assets in two separate vehicles, Maiden Lane II and Maiden Lane III. *Maiden Lane Transactions*, *supra* note 29 (click on tabs for "Maiden Lane II" and "Maiden Lane III").

from Fannie Mae and Freddie Mac,[32] and a contract to value approximately $300 billion in Citibank assets.[33] In addition, Treasury selected BlackRock to serve as a co-manager of a $3 billion fund to purchase and manage additional toxic assets.[34]

Even though there were logical reasons for the Government to turn to BlackRock, the decision to rely on one firm for multiple asset management contracts raises questions. BlackRock emerged as a top adviser to the Government in responding to the economic crisis, even suggesting policy changes and making specific recommendations to Treasury and the Federal Reserve.[35] The FRBNY chairman and the Treasury secretary[36] often sought the advice of Blackrock's president during the economic crisis.[37] Notably, BlackRock's president was a key adviser in shaping portions of Treasury's recovery plan.[38]

While Blackrock's role as an adviser does not necessarily lead to the conclusion that BlackRock receives any undue preference in receiving contracts, it does mean that BlackRock already has the trust—and the ear—of the Government.[39] BlackRock has assured critics that it has internal controls to avoid conflicts.[40] Internal controls, however, do not adequately address OCIs

32. *See* Risk Reporting and Analytical Services Agreement between BlackRock Financial Management, Inc. and the Federal Reserve Bank of N.Y. (Aug. 14, 2009), *available at* http://www.newyorkfed.org/aboutthefed/Blackrock_Agreement_012810.pdf.

33. Special Inspector Gen. for the Troubled Asset Relief Program, Quarterly Report to Congress 72 (Apr. 2009) [hereinafter SIGTARP April 2009 Report].

34. The fund, part of the Public-Private Investment Program ("PPIP"), was a key piece of the Troubled Asset Relief Program ("TARP") for purchasing toxic assets from banks to help free up liquidity in the market. *See infra* Part III.C.

35. BlackRock "emerged as the top adviser on distressed securities to governments and financial institutions around the world since the credit crisis started unfolding last year." Erik Schatzker & Caroline Salas, *BlackRock's Fink Says Dollar Still Best for Long Term*, Bloomberg, Sept. 17, 2009, *available at* http://www.bloomberg.com/apps/news?pid=newsarchive&sid=alBhV.ZKrMnM; *see also* Sree Vidya Bhaktavatsalam, *BlackRock's Fink Proposes Mortgage Purchases to Obama*, Bloomberg, Dec. 11, 2008, *available at* http://www.bloomberg.com/apps/news?pid=20601087&sid=ayaBcI6VNilE&refer=home (noting that not long after receiving the AIG contract, BlackRock proposed policy ideas to then President-elect Obama).

36. The FRBNY chairman at the time was Timothy Geithner, who subsequently became the Treasury secretary in the Obama administration. Hank Paulson served as Treasury secretary until January 2009.

37. *See* Andrews, *supra* note 16 (noting top Treasury and FRBNY officials turned to BlackRock's president for advice on the financial markets at the peak of the crisis). BlackRock's president is known to communicate frequently with Treasury and Federal Reserve officials. Lipton & de la Merced, *supra* note 26, at A1 (noting Mr. Fink has been known to call Treasury officials in both the Bush and Obama administrations several times a day, in addition to occasional visits).

38. *See* Bhaktavatsalam, *supra* note 35. BlackRock's president "hasn't been bashful about using his BlackRock platform to offer advice on fixing the financial crisis." Foroohar & Bhaktavatsalam, *supra* note 13.

39. Thus, being the "go-to" firm for the Government provides more than purely financial benefits. As one banker noted, "[y]ou couldn't put a price on how valuable those contracts are." Andrews, *supra* note 16.

40. Lipton & de la Merced, *supra* note 26, at A1 (noting BlackRock has divided asset management employees and has them work in separate buildings).

because the conflict arises from the roles or responsibilities of the organization as a whole.[41] Thus, the question remains whether BlackRock as an organization is able to maintain objectivity in carrying out its responsibilities under multiple government contracts as well as for its private clients.

III. THE ECONOMIC CRISIS: A BREEDING GROUND FOR ORGANIZATIONAL CONFLICTS OF INTEREST

The economic crisis opened the door to a variety of government agreements with asset management firms. Because the Government was responding to an urgent crisis and, in some instances, taking on a new role as a contracting agency, agreements with these firms often were not formed pursuant to traditional government procurement principles. While the departure from adhering to such a framework may have been necessary, the result was few or no checks on whether these contracts present OCIs.

Even if asset management contracts complied with traditional procurement regimes such as the FAR, the FAR provides limited guidance on identifying and mitigating OCIs. As a result, the rules for identifying and mitigating OCIs have developed case by case, in bid protest forums such as the U.S. Government Accountability Office (GAO) and the U.S. Court of Federal Claims. Because asset management contracts are unlikely to be challenged in bid protest forums, however, mitigation of asset management OCIs depends on the individual contract terms or the efforts of the contracting agency.

A. *Identifying Organizational Conflicts of Interest*

Under the FAR, OCIs are to be assessed based on the individual circumstances of the contract.[42] Rather than defining OCIs, the FAR provides "underlying principles," directing agencies to use "common sense, good judgment, and sound discretion" in determining and mitigating conflicts.[43] The overarching principle is that OCIs should be mitigated where "conflicting roles . . . might bias a contractor's judgment" or where a contractor would benefit from an "unfair competitive advantage."[44]

Because of the FAR's limited guidance, GAO has developed three generally recognized categories of OCIs: "biased ground rules," "unequal access to information," and "impaired objectivity."[45] A biased ground rules OCI refers

41. *See infra* Part III.A.

42. FAR 9.505 provides that "each individual contracting situation should be examined on the basis of its particular facts and the nature of the proposed contract."

43. *Id.* As Professor Nash has pointed out, the FAR says to the agency, "you figure it out." Ralph C. Nash Jr., *Organizational Conflicts of Interest: An Increasing Problem*, 20 Nash & Cibinic Rep. ¶ 24, May 2006, at 1.

44. FAR 9.505(a)–(b).

45. *See* Aetna Gov't Health Plans, Inc., B-254397 et al., 95-2 CPD ¶ 129, at 12–13 (Comp. Gen. July 27, 1995) (categorizing the three types of OCIs). These terms do not appear explicitly in the FAR, but GAO drew on FAR principles to develop these distinct categories. *See* FAR 9.505-9, 9.505-4; Gordon, *supra* note 11, at 32.

to a situation where a contractor writes specifications for future contracts, and thus sets the rules.[46] An unequal access to information OCI arises where a contractor "has access to nonpublic information (typically through performance of a contract) that gives it an unfair advantage in the competition for a later contract."[47] Under an impaired objectivity OCI, a contractor's role outside the contract creates "doubt [about] the contractor's ability to be truly objective."[48] This often centers on whether the contractor is carrying out conflicting roles—for instance, evaluating work the contractor performed under a separate contract[49] or holding multiple contracts with an agency that require conflicting responsibilities.[50]

Of these three categories, impaired objectivity OCIs are the most difficult to identify because they are not limited to the contract itself; rather, they depend on whether the contractor's judgment could be affected by activities not related to the contract.[51] For example, a contractor's business relationships[52] or outside financial interests implicated in a contract can create an impaired objectivity OCI.[53] Indeed, a key question in GAO's analysis of impaired objectivity OCIs is whether economic interests could undermine the contractor's ability to provide impartial advice.[54]

B. *The Task of Mitigation: A Piecemeal Approach*

Even when OCIs are properly identified, there is still the challenge of how, and whether, they can be mitigated. As noted previously, the FAR does not

46. *See* Gordon, *supra* note 11, at 32. The concern is that the company might be able to "skew the competition" in favor of itself. *Aetna Gov't Health Plans*, 95-2 CPD ¶ 129, at 13.

47. Gordon, *supra* note 11, at 32. The difficult question in an unequal access case is whether the information is "the kind of specific, sensitive information that would create an OCI." Sys. Plus, Inc. v. United States, 69 Fed. Cl. 757, 772 (2006).

48. Gordon, *supra* note 11, at 32.

49. *See* Szeliga, *supra* note 10, at 661 (citing KPMG Peat Marwick, B-255224, 94-1 CPD ¶ 111 (Comp. Gen. Feb. 15, 1994)).

50. Ktech Corp., B-285330 et al., 2002 CPD ¶ 77, at 5 (Comp. Gen. Aug. 17, 2000) (acknowledging the "inherent conflict" in contractor's different responsibilities under two separate contracts).

51. Alion Sci. & Tech. Corp., B-297022.3, 2006 CPD ¶ 2, at 6 (Comp. Gen. Jan. 9, 2006) (stating that "potential impaired objectivity OCIs are created any time the performance of a contract requirement involves the contractor's exercise of judgment that could affect other contractor-related interests").

52. *See* Szeliga, *supra* note 10, at 662 (noting GAO is likely to find an OCI where "an outside business venture is related directly to the subject matter of the procurement").

53. *See, e.g.*, *Alion Sci. & Tech. Corp.*, 2006 CPD ¶ 2, at 6 (finding OCI existed where prime contractor had "multiple financial interests" in areas related to subject of subcontractor contract); Szeliga, *supra* note 10, at 661 (impaired objectivity can arise where a contractor "evaluate[s] the performance of a separate entity in which it possesses a financial interest").

54. *See* Daniel A. Cantu, *Organizational Conflicts of Interest/Edition IV*, Briefing Papers, Nov. 2006, at 1, 3 (describing a key prong of GAO's analysis for impaired objectivity OCIs: "Even if the firm is not evaluating itself, will providing impartial advice adversely impact any of the firm's economic interests?").

adequately address mitigation.[55] Thus, the task of developing mitigation rules has fallen to bid protest forums, notably GAO, where the rules emerge in a piecemeal fashion, case by case.[56]

1. Role of the Agency

Under the FAR, the agency bears the burden of identifying and approving a mitigation plan for an OCI.[57] Mitigation steps include meeting with the contractor to discuss and assess the potential OCI, developing a plan with the contractor to take action to mitigate the OCI, or denying the award altogether.[58] The FAR stresses that an agency should obtain information about a potential conflict from sources other than the contractor.[59] Above all, an agency should not rely on the contractor's self-assessment that it has properly mitigated an OCI.[60]

2. Mitigation Measures

There is no consensus on how to approach OCI mitigation. A successful mitigation measure depends on the type of OCI and the specific facts of the contract.[61] For instance, firewalls and restriction clauses are commonly used to mitigate unequal access OCIs but cannot properly mitigate biased ground rules or impaired objectivity OCIs. The agency, however, bears the burden of ensuring mitigation takes place.[62]

55. FAR 9.504(a)(2) directs agencies to "avoid, neutralize or mitigate significant potential conflicts" before awarding a contract, but FAR 9.5 does not detail how to mitigate OCIs. As Professor Nash notes, "[o]nly one of the nine examples in FAR 9.508 describes a mitigation situation." Ralph C. Nash Jr., *Postscript: Organizational Conflicts of Interest*, 22 Nash & Cibinic Rep. ¶ 1, Jan. 2008, at 2.

56. The lack of FAR guidance on mitigation has been subject to criticism, leading to calls for an updated approach that better addresses modern OCIs. *See, e.g.*, Acquisition Advisory Panel, Report of the Acquisition Advisory Panel to the Office of Federal Procurement Policy and the United States Congress 406 (2007) (noting the FAR does not "adequately [address] the range of possible conflicts that can arise in modern government contracting"); Nash, *supra* note 43, at 1 ("it is becoming increasingly clear that the [FAR] guidance is inadequate").

57. *See* Aetna Gov't Health Plans, Inc., B-254397 et al., 95-2 CPD ¶ 129, at 12 (Comp. Gen. July 27, 1995) ("The responsibility for determining whether an actual or apparent conflict of interest will arise, and to what extent the firm should be excluded from the competition, rests with the contracting agency.").

58. *See, e.g.*, Deutsche Bank, B-289111, 2001 CPD ¶ 210, at 4 (Comp. Gen. Dec. 12, 2001) (plan that included giving work to a subcontractor and erecting firewalls adequately mitigated impaired objectivity and unequal access to information OCIs); Szeliga, *supra* note 10, at 664–72 (discussing mitigation strategies specific to each variety of OCI). If the conflict is "significant," the agency is required to put a mitigation plan in writing. *See* FAR 9.506(b).

59. The FAR provides that agencies "first should seek the information from within the Government or from other readily available sources." FAR 9.506(a).

60. *See* L-3 Servs., Inc., B-400134.11 et al., 2009 CPD ¶ 171, at 12 (Comp. Gen. Sept. 3, 2009) (a mitigation plan cannot be "self-executing").

61. *See* FAR 9.505 ("each individual contracting situation should be examined on the basis of its particular facts and the nature of the proposed contract"); Szeliga, *supra* note 10, at 673.

62. *See* Johnson Controls World Servs., Inc., B-286714.2, 2001 CPD ¶ 20, at 8 (Comp. Gen. Feb. 13, 2001) (finding an agency cannot leave mitigation of "a potential conflict solely to the contractor" because the contractor is "not in a position to make an objective judgment").

To mitigate an unequal access to information OCI, a contractor can erect a firewall to preclude certain employees from receiving specific information or from communicating with other employees.[63] A firewall cannot adequately mitigate an impaired objectivity OCI, however,[64] because in an impaired objectivity OCI, the potential conflict arises by the nature of the organization's activities or relationships.[65] Thus, walling off individuals within the organization does not resolve the impairment.[66] Even where a contractor created "separate organizations" with "distinct business objectives" to carry out two different contracts with an agency, GAO rejected the walling effort as insufficient to mitigate an impaired objectivity OCI.[67] Another common mitigation method for unequal access OCIs is to include a clause in the contract that restricts the contractor from performing certain duties under the contract or from eligibility for future awards.[68]

As previously noted, impaired objectivity OCIs are the most difficult to mitigate, often requiring recusal, reassignment of the work, or outright denial of the contract.[69] Reassignment could involve giving the work to a subcontractor or other entity, or having the agency perform the work itself.[70] The other option is increased agency oversight; however, because oversight is a significant undertaking, it should be invoked only in exceptional circumstances.[71] Thus, an agency's generic claim that it will monitor a potential OCI is unlikely to be a sufficient mitigation effort.[72]

63. *See* Szeliga, *supra* note 10, at 665 (noting a firewall can consist of procedures or physical security that restrict "the flow of confidential information between certain contractor business units and personnel"). Firewalls can be used to mitigate unequal access to information OCIs as long as the information has not already been shared. *See* VRC, Inc., B-310100, 2007 CPD ¶ 202, at 4–5 (Comp. Gen. Nov. 2, 2007) (denying protest where the protestor disclosed its possession of source selection information obtained through a previous contract only after the submission of its proposal).

64. GAO has held that a firewall "is virtually irrelevant to an [OCI] involving potentially impaired objectivity." Aetna Gov't Health Plans, Inc., B-254397 et al., 95-2 CPD ¶ 129, at 16 (Comp. Gen. July 27, 1995); *see also* Alion Sci. & Tech. Corp., B-297022.3, 2006 CPD ¶ 2, at 11 (Comp. Gen. Jan. 9, 2006) (rejecting firewall where the activities of a contractor were so interrelated that they could not be adequately segregated).

65. Gordon, *supra* note 11, at 38–39 (noting a firewall cannot mitigate an impaired objectivity OCI because "all employees of the organization will work to further the organization's interest").

66. *See Aetna Gov't Health Plans, Inc.*, 95-2 CPD ¶ 129, at 16.

67. Nortel Gov't Solutions, Inc., B-299522.5 et al., 2009 CPD ¶ 10, at 7 (Comp. Gen. Dec. 30, 2008).

68. Such restrictions are one of a few mitigation techniques suggested by the FAR. *See* FAR 9.507-2. The FAR requires that restriction clauses specify the duration and type of restricted work. *Id.* However, the mere inclusion of a restriction clause is not sufficient to mitigate an OCI; the agency also must take affirmative steps to enforce its terms. *See* Johnson Controls World Servs., Inc., B-286714.2, 2001 CPD ¶ 20, at 8 (Comp. Gen. Feb. 13, 2001).

69. *See* Szeliga, *supra* note 10, at 667–70.

70. *See id.* at 669–70.

71. *See id.* at 672 (noting that "strategies relying on agency oversight are unlikely to be effective unless they include specific procedures for identifying OCIs and mechanisms to resolve such OCIs as they arise").

72. *See, e.g.*, J&E Assocs., Inc., B-278771, 98-1 CPD ¶ 77, at 4 (Comp. Gen. Mar. 12, 1998) (rejecting agency's plan to mitigate OCI through general oversight because it would "only identify specific instances of apparent conflicts of interest as they arise" and "do nothing to avoid, mitigate, or neutralize such conflicts").

C. *Potential for OCIs in Asset Management Contracts*

The Government's contracts with asset management firms in response to the economic crisis are particularly susceptible to OCIs. First, because of economic urgency, certain contracts were either exempt from the FAR or awarded without full and open competition, which resulted in less scrutiny and oversight. Second, Treasury structured key programs under the Troubled Asset Relief Program ("TARP"),[73] the centerpiece of Treasury's recovery plan, in a way that made conflicts especially likely. While Treasury took steps to mitigate OCIs, key vulnerabilities remain. Third, even if asset management contracts were to follow a traditional procurement regime, there is no consistent approach for asset management OCIs. Instead, efforts to identify or mitigate OCIs vary depending on the individual contract, program, or agency.

1. A Regulatory No-Man's Land

The economic crisis set the stage for asset management contracts to be formed under an inconsistent and unclear procurement regime. With the enactment of TARP, Treasury was in charge of implementing a program of "unprecedented scope, scale, and complexity."[74] While agencies already can invoke "unusual and compelling urgency" exceptions to contract without satisfying full and open competition requirements,[75] Treasury received additional authority under TARP to waive FAR compliance.[76] Adding to the lack of clarity was the role of the Federal Reserve, which does not traditionally act as a contracting agency and is not required to comply with the FAR.[77]

In carrying out TARP, Treasury generally entered into two types of agreements: contracts and "financial agency agreements."[78] The financial agency

73. TARP, enacted as part of EESA, was signed into law on October 3, 2008. *See* Emergency Economic Stabilization Act ("EESA"), Pub. L. No. 110-343, § 101, 122 Stat. 3765, 3767 (2008) (codified at 12 U.S.C.A. § 5211 (West 2009)). TARP expired on October 3, 2010. *U.S. Dep't of Treasury—The Latest*, FinancialStability.gov, http://www.financialstability.gov/latest/index.html (last visited Nov. 29, 2010).

74. SIGTARP April 2009 Report, *supra* note 33, at 3. TARP gave Treasury authority for providing capital to banks, administering modifications for millions of home mortgages, and facilitating purchases of toxic assets, among other activities. *See id.*

75. *See* Competition in Contracting Act (CICA), 41 U.S.C. § 253(c)(2) (2006); *see also* FAR 6.302-2(b) (an agency can invoke the exception when "[a]n unusual and compelling urgency precludes full and open competition; and [d]elay in award of a contract would result in serious injury, financial or other, to the Government").

76. Under EESA, Treasury can find that "urgent and compelling circumstances make compliance with [the FAR] contrary to the public interest." EESA, § 107, 122 Stat. at 3773. As Treasury can invoke an unusual and compelling exception under CICA and the FAR, it is questionable whether this additional exemption is necessary or provided Treasury with more authority.

77. The Federal Reserve Act does not require the Federal Reserve to follow the FAR. *See* U.S. Gov't Accountability Office, GAO-02-774, Federal Reserve System: Update on GAO's 1996 Recommendations 11 (2002) (the Federal Reserve was not specifically directed to follow the FAR, but tends to follow "the spirit of the federal government contracting rules").

78. *See* Cong. Oversight Panel, October Oversight Report: Examining Treasury's Use of Financial Crisis Contracting Authority 7–8 (2010), *available at* http://cop.senate.gov/reports/library/report-101410-cop.cfm; One Year Later, *supra* note 14, at 28.

agreements, enacted pursuant to Treasury's existing statutory authority, are not subject to the FAR.[79] Thus, Treasury had three options at its disposal for retaining firms under TARP: (1) Treasury could enter into contracts pursuant to the FAR; (2) it could contract without adhering to the FAR; or (3) it could enter into financial agency agreements. In hiring asset management firms, Treasury chose the latter two options.[80] Nearly all of the asset management firms providing services under TARP hold financial agency agreements, and thus are not subject to the FAR.[81]

In addition, the FRBNY took the unusual step of assuming the role of a contracting agency.[82] As the Federal Reserve is not subject to FAR procurement requirements, it is unclear what, if any, regulations governed the FRBNY's contracts with BlackRock.[83] Months after awarding BlackRock the Bear Stearns contract, the FRBNY said BlackRock would manage the assets "under guidelines established by [the FRBNY]."[84] Even if the FRBNY was acting under its own internal acquisition guidelines, however, those guidelines were circumvented in selecting BlackRock. As the Federal Reserve chairman stated, due to the "unique pressures associated with the unexpected and rapid collapse of Bear Stearns and [AIG]," the "time frames [were] too short" to allow competitive bidding.[85] Further, although the FRBNY lists BlackRock's

79. *See* One Year Later, *supra* note 14, at 28 n.32.

80. *See* Special Inspector Gen. for the Troubled Asset Relief Program, Quarterly Report to Congress 130–32 (Jan. 2010) [hereinafter SIGTARP January 2010 Report] (indicating that ten out of eleven asset management firms were hired according to financial agency agreements); *see also* Cong. Oversight Panel, *supra* note 78, at 7–8.

81. *See* SIGTARP January 2010 Report, *supra* note 80, at 130–32. Although Treasury used a solicitation process to choose certain asset management firms, Treasury has not specified whether they are contractors or financial agents; Treasury simply refers to the firms as "fund managers." U.S. Dep't of Treasury, *Legacy Securities Public-Private Investment Program*, Fin. Stability.gov, http://www.financialstability.gov/roadtostability/legacysecurities.html (last visited Oct. 17, 2010) [hereinafter PPIP Information]. Under the TARP Public-Private Investment Program ("PPIP"), Treasury selected managers from a pool of more than 100 managers, based on their capacity to raise capital, experience investing in certain assets, and ability to manage funds. *See* Press Release, U.S. Dep't of the Treasury, Joint Statement by Secretary of the Treasury Timothy F. Geithner, Chairman of the Board of Governors of the Federal Reserve System Ben S. Bernanke, and Chairman of the Federal Deposit Insurance Corporation Sheila Bair on the Legacy Asset Program (July 8, 2009), http://www.treas.gov/press/releases/tg200.htm [hereinafter PPIP Joint Statement].

82. *See* Richard W. Painter, *Bailouts: An Essay on Conflicts of Interest and Ethics When Government Pays the Tab*, 41 McGeorge L. Rev. 131, 154 (2009) (noting "[c]omplex financial transactions and asset management are relatively new areas for government outsourcing to private firms").

83. The Federal Reserve is not subject to CICA and is not required to follow the FAR. *See* discussion *supra* note 77. Federal Reserve Chairman Bernanke said that BlackRock was "selected under the FRBNY's Acquisition Guidelines." Letter from Ben S. Bernanke, Chairman, Fed. Reserve, to Rep. Alan Grayson 2 (Apr. 23, 2009) [hereinafter Bernanke Letter] (on file with author).

84. Press Release, Fed. Reserve Bank of N.Y., New York Fed Completes Financing Arrangement Related to JPMorgan Chase's Acquisition of Bear Stearns (June 26, 2008), http://www.newyorkfed.org/newsevents/news/markets/2008/ma080626.html.

85. *See* Bernanke Letter, *supra* note 83, at 2. Chairman Bernanke has said that "generally speaking [we use] an RFP-type process." *An Examination of the Extraordinary Efforts by the Federal Reserve to Provide Liquidity in the Current Financial Crisis: Hearing Before the H. Fin. Servs. Comm.*, 111th Cong. 13 (2009) (statement of Ben Bernanke, Chairman, Federal Reserve) [hereinafter Bernanke statement].

agreements as "contracts," the FRBNY has suggested that these agreements are less formal than contracts.[86]

2. Inherent Structural Conflicts

TARP itself created a new potential for OCIs. Because TARP programs rely heavily on asset management firms and other private sector financial institutions[87] to increase capital and liquidity for banks, the potential for OCIs in these programs is inherent in the program's structure.[88] In particular, the role of asset management firms under one of TARP's main programs, the Public-Private Investment Program ("PPIP"), creates multiple opportunities for conflicts.[89]

An asset management firm hired under PPIP ("PPIP asset manager") could be in the position of managing the assets of existing clients as well as PPIP assets or managing PPIP assets for an institution in which it has an ownership or investment interest.[90] Either situation presents the appearance of a conflict.[91] In addition, while a PPIP asset manager risks some of its own funds in the investment, half of the investment money comes from public funds, lessening the risk and increasing the reward for the firm.[92] This gives PPIP asset managers a "powerful incentive to make investment decisions that benefit themselves at the expense of the taxpayer."[93] The structure of PPIP has led some to comment that the arrangement is indicative of the "increasingly symbiotic relationship between Washington and Wall Street."[94] Moreover, BlackRock is one of the nine PPIP asset managers Treasury selected to manage the PPIP funds—each of which can hold up to $3 billion in assets.[95]

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86. The FRBNY said it "retained" BlackRock and lists the contracts as "investment management agreements." *See Maiden Lane Transactions*, *supra* note 29; FRBNY Vendors, *supra* note 5. For clarity, this Note refers to these agreements as contracts.

87. *See* One Year Later, *supra* note 14, at 29.

88. A few months after Treasury began implementing TARP, GAO cautioned that "Treasury's reliance on private sector resources to assist with implementing TARP has underscored the importance of addressing conflicts of interest issues." U.S. Gov't Accountability Office, GAO-09-161, Troubled Asset Relief Program: Additional Actions Needed to Better Ensure Integrity, Accountability, and Transparency 40 (2008).

89. Under PPIP, public Treasury investments and private firm investments are combined into a single fund managed by a private asset manager. The fund manager purchases troubled assets from banks and other funds to take the assets off their balance sheets. The manager then monitors the assets and makes investment decisions. *See* PPIP Information, *supra* note 81.

90. *See* Special Inspector Gen. for the Troubled Asset Relief Program, Quarterly Report to Congress 166 (July 2009) [hereinafter SIGTARP July 2009 Report]. These are not the only examples of potential conflicts. For instance, if a manager does not own the asset but is "managing other funds that hold the [same asset] . . . the manager earns fees based on the value of that fund." SIGTARP April 2009 Report, *supra* note 33, at 148.

91. *See* SIGTARP July 2009 Report, *supra* note 90, at 166.

92. *See* PPIP Information, *supra* note 81.

93. SIGTARP April 2009 Report, *supra* note 33, at 147. This is because the fund's "transactions . . . will have a significant impact on how any particular asset is priced . . . [therefore,] an asset will greatly benefit anyone who owns or manages the same asset, including the PPIF manager who is making the investment decisions." *Id.*

94. Lipton & de la Merced, *supra* note 26, at A1.

95. SIGTARP July 2009 Report, *supra* note 90, at 87. Three of the nine, including BlackRock, also hold contracts with the FRBNY to manage assets. *See* FRBNY Vendors, *supra* note 5.

This has led the Office of the Special Inspector General for TARP ("SIGTARP")[96] to warn that PPIP is "inherently vulnerable to fraud, waste, and abuse."[97] For instance, PPIP asset managers have the power to set prices for the assets they purchase, giving them significant market power.[98] SIGTARP noted conflicts can arise in PPIP when firms "perform similar work for Treasury and other clients" or when firms "find that their duty to certain clients may impair their objectivity when advising Treasury or may affect their judgment about the proper use of non-public information."[99] Thus, the potential for impaired objectivity OCIs is inherent in the PPIP asset manager structure.

D. *Efforts to Mitigate Asset Management OCIs*

Both Treasury and the FRBNY have taken steps to address asset management OCIs; however, neither agency has adopted a proactive approach to ensure OCIs will be mitigated. Under current asset management contracts with the Government, the contractor, not the agency, bears the responsibility of identifying and mitigating any OCIs. Under this existing framework, asset management OCIs may fail to be adequately mitigated.

1. Treasury OCI Rule

Treasury has issued a rule ("Treasury OCI rule") aimed at preventing a range of conflicts, including OCIs, that could arise under TARP programs.[100] The Treasury OCI rule includes these examples of potential asset management OCIs: having an unfair advantage based on prior agreements with Treasury; providing the same services to Treasury and private clients; using information from Treasury agreements to benefit other clients; or holding a financial interest that could affect the agreement with Treasury.[101] The rule applies to both contracts and financial agency agreements, and thus appears to provide a strong standard that would apply to all TARP agreements.[102]

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96. SIGTARP, created as part of EESA, received additional investigatory powers by Congress in March 2009 under the SIGTARP Act. *See* SIGTARP April 2009 Report, *supra* note 33, at 11.

97. *Id.* at 147.

98. SIGTARP July 2009 Report, *supra* note 90, at 175, 178.

99. Special Inspector Gen. for the Troubled Asset Relief Program, Quarterly Report to Congress 152 (Oct. 2009).

100. EESA required Treasury to "issue regulations or guidelines necessary to address and manage or to prohibit conflicts of interest that may arise in connection with the administration and execution of [TARP]." Pub. L. No. 110-343, § 108(a), 122 Stat. 3765, 3774 (codified at 12 U.S.C.A. § 5218 (West 2009)). The statute listed "conflicts arising in the selection or hiring of contractors or advisors, including asset managers; the purchase of troubled assets; the management of the troubled assets held; post-employment restrictions on employees; and any other potential conflict of interest, as the Secretary deems necessary or appropriate in the public interest." *Id.*

101. *See* TARP Conflicts of Interest, 74 Fed. Reg. 3431, 3433 (Jan. 21, 2009) (interim rule) (to be codified at 31 C.F.R. pt. 31).

102. *See id.* Treasury strengthened the initial rule based on GAO recommendations and, after revising the rule, sought to renegotiate some of its contracts under TARP. *See* One Year Later, *supra* note 14, at 29 n.34, 30.

Despite the rule, SIGTARP has continued to identify potential OCIs that are not adequately mitigated.[103] For instance, SIGTARP has repeatedly called on Treasury to require strict firewalls in the PPIP program and to separate PPIP asset managers making decisions about TARP investments from others within the asset management firm making investment decisions for private investments.[104] It is questionable, however, whether firewalls would solve the OCIs presented by PPIP asset managers. By calling for firewalls, SIGTARP has equated the PPIP conflicts with unequal access to information OCIs.[105] Yet, the conflicting roles of PPIP asset managers also raise the possibility of impaired objectivity OCIs. While firewalls could potentially resolve unequal access OCIs, they are not appropriate for mitigating impaired objectivity OCIs.[106]

2. Duty to Mitigate

The FRBNY's contracts with BlackRock also contain provisions aimed at minimizing OCIs. However, like Treasury's OCI rule, they place the responsibility on BlackRock to identify and mitigate any OCIs.[107] BlackRock must inform the FRBNY that it has policies in place to address OCIs.[108] The contracts also suggest that BlackRock should implement firewalls.[109] While the FRBNY contracts with BlackRock take an approach similar to Treasury's OCI rule, there are two key differences. First, there is no clear regulation governing the contracts or setting a standard for mitigating OCIs. Second, unlike TARP, there is no independent monitor to review the contracts.[110] Thus, these contracts remain especially vulnerable to asset management OCIs.

103. *See* SIGTARP April 2009 Report, *supra* note 33, at 147 (describing circumstances that could lead to an impaired objectivity OCI); Special Inspector Gen. for the Troubled Asset Relief Program, Quarterly Report to Congress 27 (July 2010).

104. *See* SIGTARP January 2010 Report, *supra* note 80, at 140 (calling strict information barriers "one of SIGTARP'S most important recommendations"). Treasury has refused to implement such a measure, arguing that strict firewalls "would be detrimental to the program." Daniel Wagner & Alan Zibel, *Watchdog: Bailouts Created More Risk in System*, Associated Press, Jan. 31, 2010, *available at* http://abcnews.go.com/Business/wireStory?id=9709670.

105. *See* SIGTARP July 2009 Report, *supra* note 90, at 166 (noting fund managers could gain access to "material non-public information" by working on Treasury portfolios).

106. *See supra* Part III.B.

107. BlackRock "shall provide the [FRBNY] with the internal ethics policies and procedures put in place to govern the conduct of its employees." BlackRock Maiden Lane Agreements, *supra* note 29, at 18.

108. *See id.*

109. The contract notes that BlackRock's policies must "at a minimum ensure that personnel assigned to the management of the [assets] are adequately segregated from personnel involved with [BlackRock's] general trading, brokerage, sales, or other activities that might be in conflict with [BlackRock's] duty." *Id.* Chairman Bernanke has said that "we [generally] . . . try to make sure that the usual firewalls are in place." Bernanke statement, *supra* note 85, at 13.

110. SIGTARP's authority is limited to TARP programs, and the FRBNY's contracts with BlackRock exist outside of TARP. *See* SIGTARP April 2009 Report, *supra* note 33, at 11. Further, GAO has limited statutory authority to review Federal Reserve actions. *See* U.S. Gov't Accountability Office, GAO-10-25, Treasury Needs to Strengthen Its Decision-Making Process on the Term Asset-Backed Securities Loan Facility 2–3 n.7, 89 (2010). As part of the recent financial reform bill, Congress directed GAO to conduct a one-time audit of the Federal Reserve's actions during the economic crisis, including the Maiden Lane vehicles. *See* Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 1109, 124 Stat.

E. *Vulnerabilities Remain*

Asset management contracts remain vulnerable to OCIs. The efforts by Treasury and the FRBNY to mitigate asset management OCIs are at odds with core FAR principles and likely would not survive a GAO protest. For instance, GAO has upheld the FAR principle that the agency bears a significant responsibility to identify and mitigate OCIs, and should not rely on the contractor.[111] In addition, GAO has scrutinized the potential for biased advice and impaired objectivity, supported agency action excluding a contractor for having outside business relationships that could lead to biased advice,[112] and sustained protests where the awardee had financial interests related to the subject of a contract.[113] GAO also has adhered strictly to the argument that firewalls cannot adequately mitigate impaired objectivity OCIs.[114]

These are not the standards that have been applied to current asset management contracts. Neither Treasury nor the FRBNY has carried the burden of identifying potential OCIs. Nor has either agency relied on independent information in identifying potential OCIs. Rather, Treasury and the FRBNY have relied on information provided by the asset management firm.[115] Treasury's OCI rule also places the responsibility to identify and mitigate conflicts on the contractor, as opposed to the agency.[116] In addition, the sole proposal to mitigate asset management OCIs has been to erect firewalls.[117] Yet, this approach may be wholly inadequate to mitigate impaired objectivity OCIs in asset management contracts.[118]

1376, 2127 (2010). The GAO is to assess whether any credit facility inappropriately favored any institution and if there were any conflicts in how facilities were established or operated. *Id.* at § 1109(a)(2). The bill also expands the GAO's ability to review certain Federal Reserve actions. *See*, e.g., *id.* at § 1102.

111. *See* Aetna Gov't Health Plans, Inc., B-254397 et al., 95-2 CPD ¶ 129, at 12 (Comp. Gen. July 27, 1995).

112. *See* Wash. Util. Grp., B-266333, 96-1 CPD ¶ 27, at 2 (Comp. Gen. Jan. 29, 1996) (denying protest where a key employee of the disappointed offeror had relationships with other organizations that were directly involved in work similar to the contract).

113. *See, e.g.*, Alion Sci. & Tech. Corp., B-297022.3, 2006 CPD ¶ 2, at 6 (Comp. Gen. Jan. 9, 2006).

114. *See* Nortel Gov't Solutions, Inc., B-299522.5 et al., 2009 CPD ¶ 10, at 7 (Comp. Gen. Dec. 30, 2008) (rejecting firewall even where organization was separated into different groups with distinct business objectives); *Alion Sci. & Tech. Corp.*, 2006 CPD ¶ 2, at 11 (finding firewall could not mitigate OCI because contractor's activities were too interrelated).

115. *See* BlackRock Maiden Lane Agreements, *supra* note 29, at 18.

116. The Treasury OCI rule makes it the contractor's responsibility to "not permit an [OCI, and to] . . . maintain a compliance program designed to detect and prevent violations" of OCIs. TARP Conflicts of Interest, 74 Fed. Reg. 3431, 3434 (Jan. 21, 2009) (interim rule) (to be codified at 31 C.F.R. pt. 31). While FAR 9.504(a) requires the agency to identify potential OCIs as early as possible, the Treasury OCI rule requires the *contractor* to identify potential OCIs as soon as possible. *Id*.

117. The FRBNY, the Federal Reserve, BlackRock, and even SIGTARP have suggested that a firewall would be sufficient to mitigate asset management OCIs. *See* BlackRock Maiden Lane Agreements, *supra* note 29, at 18 (proposing firewalls); SIGTARP July 2009 Report, *supra* note 90, at 9, 175–76 (calling on Treasury to enact firewalls in PPIP); Lipton & de la Merced, *supra* note 26, at A1 (noting BlackRock has defended its contracts based on the fact that it has firewalls in place).

118. *See supra* note 64.

Further, while Treasury's OCI rule is the only clear rule to address asset management OCIs, it may not actually mitigate conflicts because asset management contracts can still fall outside the scope of the rule. For instance, because Treasury identifies PPIP asset managers as "fund managers," and not as contractors or financial agents,[119] it is not clear if they are subject to the OCI rule. In addition, the FRBNY's asset management contracts—arguably the most critical asset management contracts related to the economic crisis—are not subject to the Treasury OCI rule because they fall outside the scope of TARP.[120] If the FRBNY's contracts with BlackRock were subject to the Treasury OCI rule, however, they could not be upheld.

Treasury's OCI rule provides four examples of OCIs that could be relevant to BlackRock's contracts:

> (1) A prior or current arrangement between the Treasury and the retained entity that may give the retained entity an unfair competitive advantage in obtaining a new arrangement with Treasury.
>
> . . . .
>
> (3) The retained entity provides services for Treasury relating to the acquisition, valuation, disposition, or management of troubled assets at the same time it provides those services for itself or others.
>
> (4) The retained entity gains, or stands to gain, an unfair competitive advantage in private business arrangements or investments by using information provided under an arrangement or obtained or developed pursuant to an arrangement with Treasury.
>
> (5) The retained entity . . . has a financial interest that could be affected by its performance of the arrangement.[121]

The rule's first example of a possible OCI could be directly applied to BlackRock's Bear Stearns contract with the FRBNY to manage the Bear Stearns assets. While holding the Bear Stearns contract, BlackRock received two identical contracts to manage AIG assets.[122] The rule's second OCI example applies to BlackRock in nearly all of its asset management contracts with the Government because BlackRock provides asset valuation and management to multiple private clients while providing those services to the Government on multiple fronts. BlackRock's contracts also present the possibility for an unfair advantage under the third example, as BlackRock could use information from its government contracts to the benefit of its private clients. The fourth example is also problematic for BlackRock, as the crux of its interest in these contracts is financial. Thus, the FRBNY's contracts with BlackRock demonstrate that even where agencies have attempted to address OCI mitigation, those efforts may not reach the full spectrum of asset management OCIs.

119. *See* PPIP Information, *supra* note 81.

120. These contracts were formed before TARP was passed. Even if TARP had been in place, however, these contracts would likely fall outside the scope, since the contracts do not fall within specific TARP programs. *See* SIGTARP April 2009 Report, *supra* note 33, at 147.

121. TARP Conflicts of Interest, 74 Fed. Reg. at 3433.

122. *See Maiden Lane Transactions*, *supra* note 29; discussion *supra* Part II.B.

IV. THE ASSET MANAGEMENT OCI LANDSCAPE

The economic crisis provided the perfect storm for asset management firms to hold multiple, overlapping contracts that create fertile ground for OCIs. Given the unique circumstances that led to these asset management contracts, such OCIs may be unavoidable. Nonetheless, the potential for OCIs present serious obstacles to the effective management of toxic assets and investments that have implications for taxpayer funds. Further, asset management OCIs present an example of a type of OCI that procurement law has yet to consider.

Even if asset management OCIs are an unavoidable occurrence of the economic crisis, the Government should make a good faith effort to remain vigilant about identifying and mitigating OCIs in all contexts. At a minimum, this should include upholding FAR principles that require agencies, not contractors, to assess whether OCIs exist and take proactive steps to mitigate them. Beyond that, however, the FAR should be modernized to respond to the types of OCIs that are emerging in modern government procurement.

A. *Is Mitigation Possible?*

There is a distinct possibility that asset management OCIs cannot be mitigated. Even if asset management OCIs were subject to the identification and mitigation requirements in the FAR and set forth in GAO case law, three distinct obstacles remain.

First, conflicts are "inherent" in the field of asset management.[123] A report by the asset management industry identified a range of potential OCIs, including conflicts within the valuation process, business arrangements with affiliates, relationships with third-party service providers, and different funds managed by the same manager.[124] In asset management contacts, trust and reputation often may be given priority over the appearance of a conflict.[125]

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123. Asset Managers' Comm., Best Practices for the Hedge Fund Industry: Report of the Asset Managers' Committee to the President's Working Group on Financial Markets 47 (2009) [hereinafter Asset Managers' Report].

124. *Id.* at 47–49. The Report recognizes that conflicts may include

(a) Conflicts between the Manager and its fund(s), such as:
   - (i) Conflicts arising from proprietary trading or proprietary holdings in specified investments;
   - (ii) Conflicts arising from the valuation process;
   - (iii) Conflicts relating to the allocation of costs and expenses between the Manager and the fund;
   - (iv) Conflicts relating to transactions or business arrangements with affiliates . . . and
   - (v) Conflicts relating to relationships with third-party service providers.

(b) Conflicts between funds managed by the same Manager or between funds and separate accounts managed by the same Manager (e.g., conflicts in the allocation of investment opportunities).

Id. at 48.

125. *See* Andrews, *supra* note 16 (noting that industry insiders have begun to question how BlackRock handles conflicts of interest and the way in which BlackRock's connections seem to have resulted in contract awards).

Second, there is the unavoidable backdrop of economic necessity that led to asset management contracts. These contracts were formed under urgent circumstances in which time was short and economic stability hung in the balance.[126] Thus, even if stronger OCI rules were put in place to govern these contracts in the future, there is a significant likelihood that the need to respond quickly would once again override OCI concerns. If the Government steps in to save firms that are indeed "too big to fail," the appearance of a conflict is unlikely to be a deterring factor.[127]

Finally, the Government arguably faces a shortage of alternatives to asset management firms. While there are a number of firms that can provide asset management,[128] there are very few firms with the capability to manage complex assets.[129] Thus, the sequence of events that led to BlackRock's asset management contracts is likely to repeat itself. Just as the FRBNY turned to BlackRock because it already knew and trusted the firm, when the Government is compelled to respond to a future crisis, it will likely turn to a firm that it knows and trusts.

B. *Accounting for Modern OCIs*

It has long been recognized that the FAR does not adequately deal with the types of OCIs arising in today's procurement world.[130] The emergence of asset management contracts and the potential they pose for OCIs underscore the need for the FAR's OCI provisions to take a more modern approach. The FAR Council has undertaken this task and is in the process of updating FAR OCI rules.[131] A modernized approach for dealing with OCIs across the procurement spectrum could provide useful guidance for better identifying and mitigating asset management OCIs as well.

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126. *See generally* Kelly, *supra* note 21.

127. Even if future government action to rescue financial firms is less likely after the unpopularity of TARP, *see* Cong. Oversight Panel, Assessing TARP on the Eve of Its Expiration 96 (2010), *available at* http://cop.senate.gov/documents/cop-091610-report.pdf, that does not mean the potential for OCIs in asset management disappears. The Government may be more likely in the future to utilize private firms to avoid the perception that the Government is "bailing out" Wall Street. Further, even though TARP has ended does not mean the Government may never contemplate similar action in the future. *See, e.g.*, Gretchen Morgenson, *Count on Sequels to TARP*, N.Y. Times, Oct. 2, 2010, at BU1, *available at* http://www.nytimes.com/2010/10/03/business/economy/03gret.html?=dbk (noting the ballooning of the derivatives market, for one, has the potential to require a government backstop in the future). Indeed, because the Government is most likely to look to precedent if faced with a future crisis, the Government may use its approach to the 2008–2009 crisis as a model.

128. For instance, more than 100 asset management firms applied to be PPIP asset managers. *See* PPIP Joint Statement, *supra* note 81.

129. *See* Foroohar & Bhaktavatsalam, *supra* note 13 (noting that BlackRock has competition "[i]n theory," citing Goldman Sachs, PIMCO, and Legg Mason as possible competitors); Andrews, *supra* note 16 (discussing how BlackRock's president has emerged as the "Wall Street Wise Man," and is more trusted than any other asset manager).

130. *See, e.g.*, Nash, *supra* note 43, at 1.

131. *See* FAR Case 2007-018, Organizational Conflicts of Interest, 73 Fed. Reg. 15,962, 15,962 (proposed Mar. 26, 2008) (to be codified at FAR pts. 9, 52). These revisions will likely result in a restructuring of the FAR OCI rules and could include a more expansive list of what constitutes an OCI. For instance, some have suggested creating a "global term [that would] capture . . . services

An updated FAR could provide a clearer answer to the important question, namely, what constitutes an impaired objectivity OCI? The difficult task of identifying impaired objectivity OCIs will only become murkier as government contractors carry out more conflicting roles, and as the Government increases its reliance on large contractors.[132] As demonstrated by asset management OCIs, traditional OCI concerns may be present in nontraditional contexts. Further, an OCI-type conflict may arise without being termed an OCI. A FAR rule that provides additional examples of how impaired objectivity can arise in modern contracting will provide a broader understanding of what can constitute an OCI.

The FAR could also realize its limits by relying on other agencies and industries to help develop the definition of what constitutes an impaired objectivity OCI. In an area like asset management, for instance, the agencies that make up the FAR Council[133] cannot be expected to develop detailed examples of when conflicts might arise among asset management firms. Instead, the best examples will likely come from the agencies that oversee the industry or from members of the industry. The asset management industry, for example, identified eleven distinct potential conflicts in asset management that the FAR Council is unlikely to identify.[134] As OCIs continue to evolve and emerge, turning to the agencies and members of the industry who best understand the specific OCIs that can arise could provide useful guidance.

C. *The Risk of the "One Firm" Approach*

Underlying OCIs in asset management contracts is the unavoidable fact that the potential for conflict increases when the Government must select its contractors from a few large conglomerates. This is not unique to the financial world. Indeed, defense procurement frequently grapples with the same issue.[135] In the asset management context, however, when one firm values, monitors, and advises on billions of dollars in assets, it wields significant power over financial decisions that can impact the entire financial system and the economy.[136]

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that create 'potential' OCIs." Letter from David A. Churchill, Jenner & Block LLP, to Reg'l Secretariat, U.S. Gen. Servs. Admin. 1 (May 27, 2008), http://www.regulations.gov/search/Regs/home.html#documentDetail?R=0900006480610b7f (follow PDF hyperlink).

132. *See* Gordon, *supra* note 11, at 41 ("The factors leading to OCIs are unlikely to disappear: the consolidation within the industrial sectors selling to the Government, mergers and acquisitions leading to the presence of multifaceted corporations selling a wide range of goods and services to the Government, the reliance on umbrella contracts, and public/private competitions.").

133. These agencies include the Department of Defense, NASA, and the General Services Administration.

134. *See* Asset Managers' Report, *supra* note 123, at 47–49.

135. *See, e.g.*, Def. Sci. Bd. Task Force on Def. Indus. Structure for Transformation, U.S. Dep't of Def., Creating an Effective National Security Industrial Base for the 21st Century: An Action Plan to Address the Coming Crisis 24 (2008) (noting the "significant risk of emerging [OCIs] with consolidation of systems and/or product firms").

136. As Columbia University law professor John Coffee noted, if someone is "giving common advice to $3 trillion worth of funds, [it is] going to [have] an impact that could increase systemic risk. There can be systemic risk if one person or entity is able to make a bet-the-

This prospect is particularly startling given the assets that are at issue in these asset management contracts: These are the same overvalued securities and unstable mortgages that were the source of the nation's economic unraveling.[137] The single, most significant lesson from the economic crisis is that a system that is too intertwined and interdependent is also too vulnerable. The irony, then, is that the Government's asset management contracts are relying on the same futile principle.

The Government has entrusted BlackRock to manage some of the nation's most economically sensitive assets. If private banks cannot afford to retain these assets, and the Government does not have the expertise to manage them, then the natural question arises: Are we certain that one firm can? There are, of course, good reasons to trust BlackRock: BlackRock has been successful in the past, it is trusted across the globe, and, arguably, it possesses unmatched expertise.[138] Regardless, we should still question the soundness of relying on one firm to provide economic stability in a highly unstable area. The Government has put these troubled assets largely in the hands of one trusted source: BlackRock. But BlackRock itself is not the problem. Rather, the problem is the Government's willingness to rely on the same firm to manage sensitive assets, again and again. If BlackRock is successful in managing these assets, the Government and the taxpayers will benefit. But if BlackRock is not, there could be a steep economic price to pay.

V. CONCLUSION

The Government's reliance on large firms for asset management may be the result of necessity, but it also creates fertile ground for OCIs. BlackRock's multiple contracts that span across federal agencies—and are subject to inconsistent, or little, regulation—demonstrate how easily asset management OCIs can emerge. It remains to be seen if mitigating asset management OCIs is even possible. In responding to the economic crisis, government agencies often chose urgency and trust over identifying and mitigating potential conflicts. This is a policy choice and, perhaps in the long run, a correct one. But to uphold the integrity of government procurement—in all its forms—agencies should apply procurement principles wherever possible. If agencies cannot fully mitigate asset management OCIs, they should at least identify and address OCIs in a consistent manner. Anything less weakens the body of law that governs OCIs and, especially in the growing area of complex financial transactions, leaves the door open for future OCIs to remain unmitigated.

farm-investment decision based on poor investment analysis for an extraordinary large amount of capital." Tomoeh Murakami Tse, *With BlackRock's Reach Set to Expand, CEO Defends Money Manager's Stability*, Wash. Post, June 17, 2009, at A12, *available at* http://www.washingtonpost.com/wp-dyn/content/article/2009/06/16/AR2009061603343.html?sid=ST2009061700164.

137. *See* Mollenkamp et al., *supra* note 6.

138. *See* Andrews, *supra* note 16.