Quarterly Report to Congress pursuant to section 104(g) of the Emergency Economic Stabilization Act of 2008

For the quarter ending
March 31, 2009

FINANCIAL STABILITY OVERSIGHT BOARD

Ben S. Bernanke, Chairperson
Chairman
Board of Governors of the Federal Reserve System

Timothy M. Geithner
Secretary
Department of the Treasury

Shaun Donovan
Secretary
Department of Housing and Urban Development

Mary L. Schapiro
Chairman
Securities and Exchange Commission

James B. Lockhart III
Director
Federal Housing Finance Agency
Table of Contents

I. Introduction .......................................................................................................................................................... 2

II. Oversight Activities of the Financial Stability Oversight Board ................................................................. 4

III. Evaluating the Effects of EESA Programs ........................................................................................................... 9

   a. Early assessment of the effect of the actions taken by Treasury in stabilizing the financial markets .................. 9
   b. Early assessment of the effects of the actions taken by Treasury on the housing markets ............................ 23

IV. Description of the Actions Taken by Treasury under the EESA during the Quarterly Period ....................... 26

   a. Term Asset-Backed Securities Loan Facility .................................................................................................... 26
   b. Unlocking Credit for Small Businesses ........................................................................................................ 29
   c. Home Affordable Modification Program ..................................................................................................... 31
   d. Capital Purchase Program ............................................................................................................................. 34
   e. Capital Assistance Program .......................................................................................................................... 39
   f. Public-Private Investment Program ............................................................................................................. 41
   g. Targeted Investment Program and Asset Guarantee Program .................................................................. 43
   h. American International Group, Inc. ............................................................................................................... 47
   i. Automotive Industry Financing Program ....................................................................................................... 50
   j. Auto Supplier Support Program .................................................................................................................. 52
   k. Warranty Commitment Program .................................................................................................................... 53
   l. Executive Compensation .................................................................................................................................. 53
   m. Administrative Activities of the Office of Financial Stability .................................................................... 56

Appendix A. Minutes of Financial Stability Oversight Board Meetings During the Quarterly Period .................. 61
I. INTRODUCTION

This report constitutes the second quarterly report of the Financial Stability Oversight Board (“Oversight Board”) pursuant to section 104(g) of the Emergency Economic Stabilization Act of 2008 (“EESA”). This report covers the period from January 1, 2009, through the quarter ending March 31, 2009 (the “quarterly period”).

In light of the extraordinary events occurring in the financial markets and the substantial risks such events posed to financial stability and the health of the U.S. economy, Congress passed the EESA and it was signed into law on October 3, 2008. The primary purpose of the EESA was “to immediately provide authority and facilities that the Secretary of the Treasury can use to restore liquidity and stability to the financial system of the United States.”¹ In particular, the EESA authorized the Secretary of the Treasury (“Secretary”) to establish the Troubled Assets Relief Program (“TARP”) and take a variety of actions under the TARP to achieve the purposes of the EESA. These authorities, combined with the commitment of up to $700 billion, provided the U.S. government with important new tools to help stabilize the financial system, maintain and restore the flow of credit to households and businesses, and mitigate the downward pressures caused by the financial crisis on jobs, the housing and housing finance markets, and economic conditions more broadly.

The Oversight Board was established by section 104 of the EESA to help oversee the TARP and other emergency authorities and facilities granted to the Secretary under the EESA. The Oversight Board is composed of the Secretary, the Chairman of the Board of Governors of the Federal Reserve System (“Federal Reserve Board”), the Director of the Federal Housing Finance Agency (“FHFA”), the Chairman of the Securities and Exchange Commission (“SEC”), and the Secretary of the Department of Housing and Urban Development (“HUD”). During the quarterly period, the membership of the Oversight Board was partially reconstituted due to the Presidential appointments and Senate confirmations of Mr. Timothy M. Geithner as Secretary of the Treasury, Mr. Shaun Donovan as Secretary of HUD, and Ms. Mary L. Schapiro as Chairman of the SEC. Chairman Bernanke was elected by the Members to serve as Chairperson of the Oversight Board.

During the quarterly period, Treasury announced several important initiatives under the EESA to help stabilize the financial markets and systemically important financial institutions, promote the availability of credit to consumers and small businesses, reduce preventable foreclosures, and promote the transparency of programs under the TARP. For example, in February 2009, Treasury announced the adoption of a comprehensive Financial Stability Plan to help address the financial crisis. This plan included: (1) a new capital program to provide banks with a safeguard against a deeper than expected downturn in economic conditions; (2) the expansion of the Term Asset-Backed Securities Loan Facility, a joint program with the Federal Reserve, to improve

the securitization markets that are a critical source of financing for consumer and small business lending, with the potential for additional expansions in the future; (3) a program to help stabilize the housing market by committing TARP resources to facilitate loan modifications for at-risk homeowners; (4) a new program to purchase legacy loans and securities that currently burden the financial system; and (5) steps to promote transparency in the operation of the TARP. The Oversight Board reviewed and monitored these new policies, as well as the ongoing implementation of existing policies and programs, developed by the Treasury to implement the TARP and promote financial stability in the United States.

The Oversight Board believes that the actions taken by Treasury under the EESA have provided critical support to the financial system during this period of market turbulence and weakening economic conditions and, together with other government actions, may have helped prevent the current financial crisis from triggering a 1930s-style global financial and economic meltdown. Through the TARP, Treasury has provided capital to financial institutions across the country to help support their lending and other intermediation functions and has helped stabilize financial institutions that are critical to the financial system as a whole. The effects of the financial crisis and a sharp decline in economic activity continue to place strains on the financial system, weighing significantly on both the demand for and supply of credit. The actions taken by Treasury under the EESA, however, have improved conditions in short-term funding markets and likely have had positive effects on bank and nonbank lending activity to households and businesses. In addition, the actions taken by the Treasury under the TARP, together with those taken by the Federal Reserve, have aided the housing market and mortgage borrowers by relieving strains in the functioning of credit markets and by contributing to lower interest rates on residential mortgages.

Going forward, the Oversight Board believes it will be important for the Treasury to continue to have the ability and flexibility to take effective actions under the TARP to stabilize financial markets, help strengthen financial institutions, improve the functioning of the credit markets, and address systemic risks given the disproportionate consequences that instability of the nation’s financial institutions and markets may have for the broader economy. Financial stability benefits all households and businesses and is a necessary precondition to the resumption of normal economic activity. Working with other agencies and parties, Treasury should continue its efforts to promote public understanding of the vitally important role that TARP, and participation in the TARP program has in maintaining and restoring the flow of credit to consumers and businesses of all sizes, stabilizing the housing markets, preserving homeownership, and the resumption of economic growth.

This report is divided into four parts. Following this Introduction (Part I), Part II (Oversight Activities of the Financial Stability Oversight Board) highlights the key oversight activities and administrative actions taken by the Oversight Board during the quarterly period. Part III (Evaluating the Effects of EESA Programs) presents the Oversight Board’s evaluation of the effects thus far of the policies and programs implemented by Treasury under the TARP. Finally, Part IV (Discussion of the Actions
Taken by Treasury under the EESA During the Quarterly Period) provides a more detailed description of the programs, policies and administrative actions taken, and financial commitments entered into, by the Treasury under the TARP during the quarterly period.

II. OVERSIGHT ACTIVITIES OF THE FINANCIAL STABILITY OVERSIGHT BOARD

The Oversight Board met five times during the quarterly period—on January 8, January 15, February 25, March 1, and March 19, 2009. To promote transparency, the Oversight Board makes minutes of its meetings publicly available, and the minutes of the meetings during the quarterly period are included in Appendix A of this report. The following highlights some of the key oversight activities conducted by the Oversight Board during the quarter ending March 31, 2009.

As discussed in the minutes of the Oversight Board’s meetings, during the quarterly period the Oversight Board considered, reviewed and discussed the significant programs, policies and financial commitments established, maintained or entered into by Treasury under the TARP. In addition, the Oversight Board reviewed and discussed the ongoing operations of the Treasury’s Office of Financial Stability, which is the office at Treasury principally responsible for implementing programs under the TARP.

During the quarterly period, Treasury announced several important new or expanded initiatives under the TARP in order to address in a comprehensive manner the financial crisis and its impact on financial institutions, consumers, businesses and the economy. Many of these initiatives and actions were announced or implemented as part of the overall Financial Stability Plan announced by Treasury on February 10, 2009, with the support of the Federal Reserve and the other Federal banking agencies. The following highlights these key initiatives and actions, which were reviewed and discussed by the Oversight Board during the quarterly period.

Restoring the Flow of Credit to Consumers and Businesses

- The Consumer and Small Business Lending Initiative was established under the Financial Stability Plan. This initiative is designed to promote the resumption of normal credit flows to American consumers and businesses. In connection with this initiative--

- Treasury and the Federal Reserve announced the expansion of the Term Asset-Backed Securities Loan Facility (“TALF”) to include certain additional types of asset-backed securities, as well as the potential for the maximum size of the facility to be increased from

---

2 Approved minutes of the Oversight Board’s meetings are made available on the internet at [http://www.financialstability.gov/about/oversight.html](http://www.financialstability.gov/about/oversight.html).
$200 billion to $1 trillion and for additional asset classes to be made eligible for financing through the facility. The first tranche of subscriptions under this important facility closed on March 19, 2009, with additional subscription periods to follow on a monthly basis.

- Treasury established the Unlocking Credit for Small Businesses program. This program, which may be funded with up to $15 billion, is designed to help restore the flow of credit to small businesses through the purchase of securities backed by loans guaranteed or originated under certain Small Business Administration (“SBA”) programs.

**Preventing Avoidable Foreclosures**

- The Home Affordable Modification Program (“HAMP”) was established under the TARP to help at-risk homeowners avoid foreclosure and reduce the negative spillover effects of foreclosures on neighborhoods, communities and the broader economy. Treasury has committed up to $50 billion of TARP funds to support this important program. Treasury worked in conjunction with HUD, FHFA, the Federal Reserve and other agencies to develop this comprehensive loan modification program.

**Stabilizing Financial Markets and Financial Institutions and Maintaining Confidence in the U.S. Financial System**

- Treasury continued to provide capital to viable banking organizations of all sizes throughout the United States through the Capital Purchase Program (“CPP”) to support financial stability and promote the availability of credit during this crisis. During the quarterly period, more than $21 billion in capital was provided to 320 banking organizations under the CPP. As part of its commitment to create a program available to eligible U.S. banking organizations of all types and sizes, Treasury released the terms under which banking organizations organized under subchapter S of chapter 1 of the Internal Revenue Code (“S-Corporations”) may participate in the CPP on a comparable basis with other eligible banking organizations. This third term sheet under the CPP provides numerous smaller organizations with access to capital to remain strong and capable of meeting the credit needs of customers.

- Treasury announced a new Capital Assistance Program (“CAP”) to help ensure that U.S. financial institutions have sufficient high-quality capital to continue lending and absorb the potential losses
that could result from a severe decline in economic conditions. The CAP is a two-pronged program that includes a supervisory exercise by the Federal banking agencies to produce a more consistent and forward-looking assessment of the risks on banks’ balance sheets and their potential capital needs, and a new capital access program for qualifying financial institutions. Treasury worked extensively with the Federal banking agencies in developing the CAP.

- A new Public-Private Investment Program (“PPIP”) was announced to help promote liquidity in the market for legacy loans and securities, promote transparency in the pricing of such assets, and promote new lending by financial institutions by facilitating the cleansing of legacy assets from their balance sheets. The PPIP will be implemented by Treasury in conjunction with the Federal Reserve and the Federal Deposit Insurance Corporation (“FDIC”).

- In order to help maintain confidence in the financial system and the stability of systemically important financial institutions—
  
  - Treasury, in conjunction with the FDIC and the Federal Reserve, provided a package of capital, loss-sharing and liquidity supports to Bank of America Corporation (“Bank of America”), following its acquisition of Merrill Lynch & Company, Inc.;
  
  - Treasury announced that it would participate in a share exchange to be conducted by Citigroup Inc. (“Citigroup”) with its private preferred shareholders. These exchange transactions will improve the quality of the firm’s capital, better enable the company to weather the ongoing financial turmoil, and improve the structural seniority of certain of Treasury’s previously acquired interests in the company; and
  
  - Treasury, in conjunction with the Federal Reserve, restructured the supports provided by the U.S. government to American International Group, Inc. (“AIG”) in order to help stabilize the company and facilitate its ongoing global divestiture program. These actions included the commitment by Treasury of up to $30 billion in additional capital to AIG through a new 5-year capital facility and the modification of the terms of the existing non-convertible preferred stock of AIG held by Treasury.
Supporting the Orderly Restructuring of the Domestic Auto Companies

- In order to assist the domestic automotive industry in becoming financially viable, Treasury—
  - Provided $1.5 billion in senior financing to Chrysler Financial LLP (“Chrysler Financial”) to finance the extension of new consumer auto loans;
  - Established a new Auto Supplier Support Program, which includes a commitment of up to $5 billion under the TARP to help stabilize the automotive supply industry and support the orderly restructuring of the domestic automobile manufacturers by providing suppliers of such companies with access to government-backed protection and funding;
  - Agreed to provide up to 60 days of additional working capital to General Motors Corporation (“GM”) as it seeks to develop and implement a more aggressive and viable restructuring plan, and up to 30 days of additional working capital to Chrysler Holdings LLC (“Chrysler”) as it seeks to finalize its partnership with Fiat S.p.A. or another firm to remain viable; and
  - Announced a new Warranty Commitment Program to provide U.S. government guarantees for warranties issued by participating domestic auto manufacturers to help ensure that the automakers may remain competitive while they seek to develop acceptable restructuring plans.

Additional details concerning each of these programs and investments are included in Part IV below.

As part of its oversight activities, the Oversight Board during the quarterly period received presentations and briefings from Treasury officials and, where appropriate, officials from the Federal Reserve concerning the objectives, terms, and progress of TARP programs and initiatives. For example, as reflected in the minutes of its meetings, the Oversight Board reviewed, discussed and considered the assistance provided to GM, Chrysler, and GMAC LLC, as well as the package of capital, asset guarantees and liquidity support provided to Citigroup, at its meeting on January 8, 2009; the package of capital, asset guarantees and liquidity support provided to Bank of America at its meeting on January 25, 2009; the Capital Assistance Program, the Home Affordable Modification Program and recent changes to the TALF at its meeting on February 25, 2009; the Citigroup share exchange and the restructuring of the assistance provided to AIG at its meeting on March 1, 2009; and the PPIP program and the Auto Supplier Support Program at its meeting on March 19, 2009. In addition, the Oversight Board has received regular updates on developments in the Capital Purchase Program.
The Oversight Board also has monitored and discussed the aggregate level and distribution of commitments and disbursements under the TARP and the level of resources that remain available under the TARP. The following chart summarizes TARP commitments and disbursements as of March 31, 2009.

![TARP/Financial Stability Plan Tracking Report](chart)

The Oversight Board also has reviewed and monitored the steps taken by Treasury to promote transparency in the operations of the TARP and improve communications with the public and Congress regarding the important actions being taken to help stabilize the financial and housing markets, restore the flow of credit to consumers and businesses, and protect the interests of taxpayers. These include the development and implementation of Monthly Intermediation Snapshots and Monthly Lending Reports to provide the public and Treasury with useful information concerning changes in the lending and intermediation activities of recipients of capital under TARP. Beginning in January 2009, Treasury also began to post on its website all contracts entered into with financial institutions receiving financial assistance under the TARP.

At its meetings, the Oversight Board also has reviewed and discussed ways to coordinate its activities with the other oversight bodies for the TARP, including the
Office of the Special Inspector General for the TARP (“SIGTARP”), the Government Accountability Office (“GAO”) and the Congressional Oversight Panel (“COP”). For example, at the Oversight Board’s invitation, Mr. Neil Barofsky, the Special Inspector General, met with the Oversight Board on January 8, 2009, to discuss ways of coordinating activities and how the SIGTARP could use its investigative and other powers most effectively to prevent fraud by persons that receive TARP funds. To help facilitate coordinated oversight and minimize the potential for duplication, staff of the Oversight Board and of the agencies represented by each Member of the Oversight Board also have regular discussions with representatives from the SIGTARP and GAO to discuss recent and upcoming activities of the oversight bodies.

III. EVALUATING THE EFFECTS OF EESA PROGRAMS

In light of severe stresses in the U.S. and global financial markets, Congress passed the EESA to “immediately provide authority and facilities that the Secretary of the Treasury can use to restore liquidity and stability to the financial system of the United States.” Utilizing this authority, Treasury has implemented or announced a range of programs to stabilize the financial markets and financial institutions, restore the flow of credit to consumers and businesses, and help at-risk homeowners remain in their homes and avoid foreclosure. These programs are described in more detail in Part IV of this Report. This section provides an early evaluation of the effects of Treasury’s efforts under EESA, building on the assessment made in the Oversight Board’s First Quarterly Report.

a. Early assessment of the effect of the actions taken by Treasury in stabilizing financial markets

Treasury’s actions under the EESA continued to provide meaningful support to core financial markets during the first quarter of 2009. The steps taken by the Treasury to bolster financial stability were reinforced by other actions taken by the United States and foreign governments to assist financial markets. Taken together, these actions improved conditions in short-term funding markets and likely had positive effects on bank and nonbank lending activity. Capital positions at larger bank holding companies rose significantly during the fourth quarter – despite large operating losses at some of the major banks – largely because the capital injections made under the CPP and TIP. However, the magnitude of the beneficial effects of Treasury’s actions is difficult to single out in light of the presence of other government programs, the broader weakness in U.S. and global economic activity, and the normal effects of this economic weakness on lending markets. Especially at this still-early stage, there remain significant conceptual and practical challenges to identifying the effect of Treasury’s actions in isolation on financial markets.

3 12 U.S.C. § 5201(1). For an overview of the conditions in the financial markets prior to passage of the EESA, see Part V.a of the Oversight Board’s First Quarterly Report to Congress for the quarter ending December 31, 2008 (“First Quarterly Report”).
The headwinds from the sharp decline in economic activity in recent quarters, in particular, have placed further strains on the financial system. Risk spreads in credit markets remained elevated in the first quarter of 2009, reflecting risk aversion on the part of investors and deterioration in the creditworthiness of some borrowers, including those most affected by weakened macroeconomic conditions. In addition, lending by banks and nonbanks has tapered off as both the financial crisis and the economic downturn have weighed on both the demand for and supply of credit.

Nevertheless, by providing capital assistance to numerous financial institutions and establishing programs to restore the flow of credit, the TARP has been a key stabilizing factor for the financial system and has likely prevented more serious weakness in the markets for credit to households, businesses, and communities. For example, TARP capital investments in banking organizations, in conjunction with other government programs, contributed to the easing of liquidity pressures at banking organizations in late 2008 and the first quarter of 2009.

As indicated in the Oversight Board’s First Quarterly Report, conditions in interbank markets have improved considerably since last fall. The spread of the LIBOR rate to the overnight index swap ("OIS") rate (figure 1), which is a useful measure of banks’ short-term borrowing costs, dropped sharply following the announcement of the CPP program in October of last year. After spiking to a record level of about 350 basis points in early October 2008, the spread of three-month LIBOR over OIS narrowed to about 100 basis points in January, and has remained at roughly that level through the first quarter of this year. The spread of one-month LIBOR to the OIS rate narrowed even more through the end of last year, but moved up a bit in the first quarter. While the LIBOR-OIS spreads indicate substantial improvement in the short-term interbank funding market since last fall, these spreads continue to be elevated relative to historical levels, suggesting that strains persist.
Conditions in other short-term funding markets also have improved due in part to government programs to stabilize financial markets. For example, conditions in commercial paper markets improved last fall after the Federal Reserve announced the Commercial Paper Funding Facility (“CPFF”) on October 7, 2008. Spreads on overnight commercial paper (figure 2) declined sharply last fall, and those on lower-rated (or A2/P2) commercial paper have moved down further on net through the first quarter of this year. With the benefit of CPFF, spreads among the three categories of A1 commercial paper (not shown)—financial, nonfinancial, and asset-backed—have largely reverted to pre-crisis levels.\(^4\) Outstanding balances of nonfinancial and asset-backed commercial paper changed little on net over the fourth quarter of last year, but have decreased in recent months likely reflecting lower demand for short-term funding, presumably attributable to slower economic activity. Meanwhile, outstanding financial commercial paper rose substantially over the fourth quarter of last year (figure 3), bolstered by support from the CPFF, and then fell sharply early this year as some issuers shifted to other funding instruments, including longer-term debt issued under the FDIC’s Temporary Liquidity Guarantee Program (“TLGP”).

---

\(^4\) Financial commercial paper is issued by depository and nondepository credit institutions, bank holding companies, insurers, and other financial institutions. Nonfinancial commercial paper is issued by nonfinancial corporations. Asset-backed commercial paper is issued by special-purpose vehicles to finance the purchase of receivables, term loans, and securities. For more information see \url{http://www.federalreserve.gov/releases/cp/about.htm}. 
Credit default swap ("CDS") spreads provide a useful barometer of the credit risk associated with being a creditor of the reference institution as judged by market participants. CDS spreads at several large banking organizations narrowed substantially after the CPP program was announced last October, suggesting that the announcement of the CPP helped reduce the perceived risk of these institutions (figures 4 and 5). These beneficial effects were overcome by subsequent adverse developments, at least for some firms, likely reflecting heightened concerns about write-downs and credit-related losses as discussed further below. By March 31, 2009, spreads ranged from 200 to more than
500 basis points. It is possible that these CDS spreads would have widened further had no policy actions been taken, although the likelihood is difficult to assess.

Figure 4

Identifying the effects of EESA programs on lending activity presents significant conceptual and practical challenges, especially at this early date. Foremost among these challenges are the inherent difficulties in disentangling the relative importance of reduced demand for credit due to weaker economic activity, reduced supply of credit because
borrowers appear less creditworthy, or reduced supply of credit because lenders face pressures that restrain them from extending credit, such as possible concerns about their capital.

Data from a recent Federal Reserve survey of senior loan officers at banks provide useful insight into the salience and direction of these various influences. The survey results appear to support the hypothesis that both supply and demand factors have contributed to a slower pace of loan growth. For example, domestic banks have been tightening standards since early 2008 for loans in both the commercial and industrial (“C&I”) loan category and the consumer loan category, although the net percentage that tightened has diminished a bit in recent months (figure 6). All of the banks that tightened indicated that concerns about a weaker or more uncertain economic outlook were important in their decision to do so. Most respondents also mentioned a worsening of problems in specific industries and their bank’s reduced tolerance for risk as important factors in their decision to tighten C&I lending policies. Fewer banks cited concerns about current or future deterioration in their own capital position as an important reason for raising loan standards – one-fourth of the banks in January 2009, compared with almost 40 percent in October 2008 – which suggests that perhaps TARP capital investments may have helped moderate tightening of lending standards. Also noteworthy is that a remarkably high net percentage of domestic banks reported weaker demand for C&I loans over the final months of 2008 (shown as negative net percent values in figure 7). Indicators of supply and demand for loans to small firms closely mirrored those for loans to larger firms.

Figure 6

Source: Federal Reserve Board, Senior Loan Officer Opinion Survey.
Parallel to the findings for C&I loans, a majority of domestic banks have reported tightening their standards for consumer and credit card loans (figure 8). Chief among these changes, the ability to grant exceptions to minimum credit-scoring thresholds was reduced at more than half of the survey respondents, and minimum required credit scores were raised and credit limits were lowered at almost half of the surveyed banks. Nearly half of the reporting banks on net reported a decline in demand for credit card and other consumer lending (figure 9).
Figure 8

Net Percentage of Domestic Respondents Tightening Standards for Consumer Loans

Source: Federal Reserve Board, Senior Loan Officer Opinion Survey.

Figure 9

Net Percentage of Domestic Respondents Reporting Stronger Demand for Consumer Loans

Source: Federal Reserve Board, Senior Loan Officer Opinion Survey.
Consistent with these trends in supply and demand for bank credit, data from the Flow of Funds Accounts published by the Federal Reserve Board show that growth in total loans at depository institutions slowed substantially in recent quarters (figure 10). On a year-over-year basis, loans on the books of depository institutions rose only 3.5 percent in the fourth quarter of 2008, the lowest rate since the emergence from the 2001 recession. From a historical perspective, sharp declines in loan growth at depository institutions are not unusual for recessions (shown as shaded areas).

Although Flow of Funds data for the first quarter will not be available for several weeks, the Oversight Board is interested in providing some assessment of lending activity for the most recent quarter. Data from a weekly survey of banks summarized in the Federal Reserve’s H.8 Statistical Release (Assets and Liabilities of Commercial Banks in the U.S.) provide some preliminary indications of the direction and magnitude of changes in loan balances during the first quarter of 2009. According to data from the H.8, domestic commercial bank credit contracted in the first three months of 2009 relative to year-end 2008. C&I loan outstandings declined as demand ebbed and banks reported widespread prepayments and other pay-downs of outstanding loans. A temporary build-up of residential real estate loans was unwound in March, as banks reportedly sold large amounts of such loans to the government-sponsored enterprises. Revolving home equity loans continued to grow, and consumer loan outstandings were mostly unchanged. Treasury’s Snapshot reports for October-December 2008 and for January 2009 also show that there continued to be a strong flow of new loan originations at the 20 banking organizations that had received the largest amounts of capital under the CPP, with particular strength in the residential mortgage category, although the stock of loans at these organizations had declined somewhat over this four-month period.
Providing further support to bank lending, increased deposit insurance coverage limits and introduction of the TLGP have aided banks’ ability to raise funds. Deposit growth has been robust, and some $269 billion of debt had been issued under the TLGP as of the end of February 2009. Capital at bank holding companies that file the quarterly Y-9C report (generally those with over $500 million in assets) rose significantly during the fourth quarter – despite large operating losses at some of the major banks – although by less than the full amount of the capital investments made in these institutions under CPP and TIP. It should be recognized, however, that rising levels of nonaccrual loans and other real estate owned (“OREO”) at commercial banks – which increased at an annualized 11 percent rate in the fourth quarter of 2008 – could put some pressure on these capital positions in future quarters.

Beyond credit provided on banks’ balance sheets, spreads on AAA-rated asset-backed securities (“ABS”) backed by consumer loans showed significant and sustained improvement in the period between the announcement of the TALF in late November 2008 and the first subscription for funding under this facility in late March (figure 11). As in most other asset categories, however, spreads on ABS remained elevated relative to historical norms. Spreads also remained elevated for corporate bonds, which in turn continue to reflect market concerns about potential defaults and a limited willingness to take on risk (figure 12).
Figure 12

Aggregating across banks and other lenders, growth in borrowing by nonfinancial businesses and households has tended to slow significantly in periods of economic weakness, and generally has not strengthened until after the trough in economic activity (figures 13 and 14, respectively). Viewed against that backdrop, available data through the fourth quarter of 2008 indicate that year-over-year growth in borrowing by households has decelerated more sharply than in other recessions while borrowing by nonfinancial businesses has, at least through March 31, decelerated in a manner that is not inconsistent with what occurred in earlier recessions.
Figure 13

Debt Growth for Nonfinancial Businesses

Four quarter percent change

Source: Federal Reserve Board, Flow of Funds Accounts.
Note: Shaded areas denote NBER recession periods. The solid line is the December 2007 business cycle peak identified by the NBER.

Figure 14

Debt Growth for Households

Four-quarter percent change

Source: Federal Reserve Board, Flow of Funds Accounts.
Note: Shaded areas denote NBER recession periods. The solid line is the December 2007 business cycle peak identified by the NBER.
CDS spread data suggest that market participants continued to have concerns regarding the financial health of some of the nation’s largest financial institutions, and these concerns may have risen during the first quarter of 2009. For example, the CDS spread for Bank of America rose sharply towards the end of 2008, as the bank neared completion of its acquisition of Merrill Lynch, which was consummated on January 1, 2009 (figure 4 above). On January 16, 2009, both Bank of America and Merrill Lynch reported losses for the fourth quarter of 2008, with the loss for Merrill Lynch being substantially greater than expected. On that same day, an additional package of capital, loss-protection and liquidity supports for Bank of America was announced by the Treasury, FDIC and Federal Reserve. Despite these actions, the CDS spread for Bank of America continued to rise during the remainder of the first quarter. Citigroup’s CDS spread also rose after year-end 2008, and generally continued on an upward trend for the balance of the quarter. Both institutions saw brief easing of their CDS spreads around the January 16 and February 25 announcements of major TARP programs and actions, especially the late February release of detailed terms and conditions for the CAP. Even with these negative overall trends during the first quarter, it is likely that both market assessments and the banks’ actual financial condition would have been materially worse without the supports provided by Treasury and other government programs.

The CDS spreads for AIG declined dramatically following the actions taken by the Treasury and the Federal Reserve in November 2008 to restructure the government’s supports for the company, indicating that market participants believed these actions would reduce the risk associated with being a creditor of AIG. However, reflecting heightened concerns about the credit risk associated with AIG, CDS spreads began to rise sharply in mid-February, moving from an already-high 5 percentage points to nearly 14 percentage points by February 27, 2009 (figure 15). A notable decline in the spread came with announcement on March 2 of a new package of measures to stabilize the company, facilitate its global divestiture program and prevent a disorderly failure of this systemically important firm. Within days, however, the CDS spread began to rise again, and reached its highest level at quarter-end since the early-November 2008 spike.

---

5 As is described later in this report, that announcement indicated that CAP was designed to ensure that the largest organizations have sufficient capital buffers to continue lending even through a severe economic downturn, and that the program would permit the conversion of CPP and TIP preferred stock into CAP mandatorily convertible preferred shares.
Treasury also has provided financial support under the TARP to GM and Chrysler to help prevent a significant disruption to the American automotive industry and to facilitate a restructuring of the companies to achieve long-term viability. To this end, Treasury required both companies to submit restructuring plans by February 17, 2009, that included specific actions aimed at assuring: (i) the repayment of the loans extended by TARP; (ii) the ability of the companies to comply with applicable federal fuel efficiency and emissions requirements and commence the domestic manufacturing of advanced technology vehicles in accordance with federal law; (iii) achievement of a positive net present value; (iv) rationalization of costs, capitalization, and capacity with respect to the manufacturing workforce, suppliers and dealerships of the companies; and (v) a product mix and cost structure that is competitive in the U.S. marketplace.

On February 17, 2009, GM and Chrysler submitted their restructuring plans to the Presidential Task Force on the Auto Industry (“Auto Task Force”) established by Treasury and the National Economic Council. On March 30, 2009, the Auto Task Force determined that the plans submitted by the companies would not result in long-term viability. In connection with this determination, the Auto Task Force provided GM until June 1, 2009, to develop a more aggressive restructuring plan and a credible strategy for implementing that plan. In addition, the Auto Task Force determined that Chrysler is not viable as a stand-alone company and provided the company until May 1, 2009, to conclude a definitive agreement with Fiat S.p.A., or another partner and secure the support of necessary stakeholders. The companies and Treasury continue to work towards the achievement of these goals and the Oversight Board will continue to monitor the progress of these efforts.
Early assessment of the effect of the actions taken by Treasury on the housing markets

The Oversight Board believes that actions taken by the Treasury under the TARP, together with those taken by the Federal Reserve, continued to aid the housing market and mortgage borrowers during the first quarter of 2009 by relieving strains in the functioning of credit markets and by contributing to lower interest rates. Purchases of mortgage-backed securities by the Federal Reserve and the Treasury, along with the Federal Reserve’s purchases of longer-term Treasury securities, helped bring the average interest rate on new conforming 30-year fixed-rate mortgages below 5 percent during the first quarter. In turn, according to data from the Mortgage Bankers Association, mortgage refinancing activity rose sharply in the first quarter of 2009 as homeowners took advantage of the opportunity to reduce their mortgage interest costs.

While interest rates declined generally, market participants continued to require wider spreads over reference rates than has been the historical norm for mortgage-backed securities, which is broadly consistent with the patterns evident in the markets for other financial instruments (described in Part III.a above). While the spread between mortgage-backed securities (“MBS”) yields and comparable Treasury yields has narrowed substantially from its early-2008 peak, it remained significantly above pre-crisis levels (figure 16).

Figure 16
The continuing decline in rates has not yet had an apparent impact on home values (figure 17). Both the FHFA and S&P/Case-Shiller indices of home prices showed further weakness through the early part of the first quarter.6

Reflecting both housing-specific and broader economic factors, the share of mortgage loans more than 90 days delinquent continued to rise significantly across a wide range of loan types through early 2009 (figure 18).

---

6 The FHFA index is constructed using homes with conforming, conventional mortgages that have been purchased or guaranteed by Fannie Mae or Freddie Mac (the “Enterprises”). The S&P/Case-Shiller index, by contrast, covers home sales with all types of financing - including cash sales, and transactions with jumbo and subprime mortgages - but has less complete geographic coverage than does the FHFA index.
Foreclosures, however, tapered off in late 2008 as many lenders, including Fannie Mae and Freddie Mac, placed a temporary moratorium on foreclosures and servicers and lenders – including those participating in the HOPE NOW Alliance – implemented additional measures to modify the loans of at-risk homeowners. Nonetheless, total foreclosures (per the Mortgage Bankers Association) reached more than 2.3 million properties in 2008, compared with 1.3 million in 2007. Demonstrating the significant potential negative effect on home prices – and the considerable potential value of foreclosure mitigation – the National Association of Realtors reported that foreclosures and other distressed sales accounted for a remarkable 40 to 45 percent of existing home sales nationwide in the month of February 2009.

Mortgage originations continued to be weighted toward loans with some form of government support, as the private label securities market remained weak. For example, FHA continued to provide strong support for mortgage credit flows in the first quarter of 2009, with single-family insurance volumes topping $70 billion for the third quarter in a row. By way of contrast, FHA insured less than $70 billion of new loans in all of 2007. The year-over-year growth in FHA activity this past quarter was 123 percent in dollar terms and 93 percent in numbers of households served. Over 400,000 households used FHA insurance to either purchase a home (46 percent) or refinance their home (54 percent) in the first quarter of 2009. This strong market presence is likely to continue throughout 2009, as private mortgage insurers restrict new insurance volumes to preserve capital for expected losses on outstanding business. Those restrictions at the private insurance companies have resulted in a significant improvement in the credit quality of borrowers coming to FHA, when compared with the year-earlier period. The weakness of the private mortgage insurers has affected Fannie Mae and Freddie Mac in the opposite way. Their first quarter securitization volume of more than $250 billion was larger than
recent quarters because of the decline in interest rates, but it was about 10 percent less than in last year's first quarter.

With the nation facing these conditions, Treasury in February 2009 unveiled the Making Home Affordable program to reduce the potential flow of future foreclosures and to address some of the frictions that have limited the pursuit by some lenders and servicers of alternatives to foreclosure that, in turn, can help to relieve downward pressure on home values. In addition, in March 2009, Treasury announced the Public-Private Investment Program—a program that could potentially ease high illiquidity premiums and discount rates associated with profound risk aversion and the widened spreads in MBS markets. PPIP is designed to provide a vehicle through which patient investors can combine their resources and expertise with government investment and funding to acquire legacy securities that trade at low prices now but could reasonably be expected to generate much higher than normal returns over time. Taken together, these programs represent a direct application of TARP resources by the Treasury as a potential counterweight to the concerns and uncertainties associated with mortgage assets that have played such an important role in this period of financial turmoil. The Oversight Board expects to evaluate the effects of these recently announced programs in its future quarterly reports.

IV. DESCRIPTION OF THE ACTIONS TAKEN BY TREASURY UNDER THE EESA DURING THE QUARTERLY PERIOD

This section of the report provides an overview of the various programs, policies, financial commitments and administrative actions taken by the Treasury under the EESA during the quarterly period, subject to the review and oversight of the Oversight Board.

a. Term Asset-Backed Securities Loan Facility

i. Program Details

The Term Asset-Backed Securities Loan Facility (“TALF”) is a joint program of the Federal Reserve and the Treasury that is aimed at supporting the securitization markets for key types of consumer and small business credit and, thereby, assist in making such credit more available and affordable. The securitization markets have served as an important source of funding for loans to consumers and small businesses. For example, issuances of consumer asset-backed securities (“ABS”) averaged $20 billion per month in 2007, and $18 billion per month during the first half of 2008. However, spreads on AAA-rated consumer ABS began to widen gradually in the summer of 2007, when dislocations in funding markets became apparent, and spiked to historically wide levels in the fourth quarter of 2008 as the severity of the economic downturn became increasingly apparent. New issuance of consumer ABS declined precipitously in the third quarter of 2008 before coming to a virtual halt in October 2008.
The TALF is designed to help market participants meet the credit needs of households and small businesses by supporting the issuance of eligible ABS. Under the TALF, the Federal Reserve extends three-year, non-recourse loans collateralized by certain types of ABS that are, in turn, backed by loans to consumers and small businesses. Treasury, through the TARP, provides credit protection to the Federal Reserve to support lending through the TALF. Development of the TALF initially was announced in November 2008, with a focus on newly or recently originated AAA-rated ABS backed by student loans, auto loans, credit card loans, and loans guaranteed by the SBA. When announced, the aggregate size of the TALF was expected to be up to $200 billion, supported by up to $20 billion of capital from TARP. The TALF is a key component of the Consumer and Business Lending Initiative under the Financial Stability Plan, announced on February 10, 2009.

ii. Program Updates

Several important developments with respect to the TALF occurred during the quarterly period, including the commencement of operations in March 2009. Specifically, on March 17, 2009, the Federal Reserve began to accept subscriptions under the TALF for funding from eligible owners of newly or recently originated AAA-rated ABS backed by student loans, auto loans, credit card loans and SBA-guaranteed loans. This initial subscription period closed on March 19, 2009, and the loans were settled on March 25, 2009. The loans supported the issuance of $8.3 billion of credit card and auto ABS. Additional subscriptions and fundings will continue, on a monthly basis, through December 2009, or longer if the Federal Reserve Board determines to extend the facility.

During the quarterly period, Treasury and the Federal Reserve also announced updates to the terms and conditions governing the current operations of the TALF. The updated terms and conditions contain several provisions that are designed to protect the interests of taxpayers, and are consistent with achieving the program’s focus of encouraging lending to consumers and small businesses.

- The TALF is a collateralized lending program that uses risk-based haircuts, ranging from 5 to 16 percent, to help protect the taxpayer against losses. Thus, for every $100 in pledged collateral, borrowers commit $5 to $16 of their own capital. These haircuts represent TALF borrowers’ equity interest in the arrangement, and serve as an additional buffer that is forfeited, along with the collateral, in the event the loan is not repaid. The haircuts vary across asset types depending on an assessment of the riskiness of the ABS and the average maturity of the underlying credits.

---

7 Updated terms and conditions for the TALF, as well as Frequently Asked Questions about the facility, are available on the internet at: http://www.newyorkfed.org/markets/talf.html.
• Further protection is provided by the risk premium included in the TALF loan rate. Generally, TALF loans will be extended at 100 basis points over one-month LIBOR for most floating rate ABS or 100 basis points above the three-year swap rate for most fixed-rate ABS. The Federal Reserve will claim a small portion of the income as its cost for providing liquidity, but the remainder, which represents a larger portion of the interest, will accumulate in the TALF facility in order to absorb any losses. This interest rate spread will provide a substantial buffer for taxpayers, paid for by the private sector, in the event that the ABS is surrendered in lieu of repayment of the TALF loan.

• The current economic situation is extraordinary and the outlook is therefore especially uncertain. Treasury and the Federal Reserve accounted for that uncertainty by making conservative assumptions when calibrating the haircuts. The haircuts are designed so that, even if the economy evolves in a manner significantly worse than currently expected, all credit costs will be more than covered by the haircuts and the excess interest rate spread paid by investors, resulting in no credit losses for the Treasury or Federal Reserve.

• The interest rates on TALF loans are set with a view to providing borrowers with an incentive to purchase eligible ABS at yield spreads higher than in more normal market conditions but lower than in the highly illiquid market conditions that have prevailed during the recent credit market turmoil. In doing so, TALF loan rates encourage the flow of credit, but provide the private sector with an incentive to borrow only selectively from taxpayer resources.

• Treasury and the Federal Reserve have indicated that they will periodically review and, if appropriate, adjust the TALF interest rate spread and haircuts for new loans, consistent with the policy objectives of the TALF. During the quarterly period, revisions were made to the terms and conditions that reduce the collateral haircuts, as well as the interest rates, for TALF loans secured by ABS guaranteed by the SBA or backed by U.S. government-guaranteed student loans. These modifications were made in light of the minimal credit risk on the assets owing to the existence of U.S. government guarantees. By making the terms of the TALF loans more attractive for investors in these ABS, it should encourage greater flows of credit to small businesses and students.

---

8 However, as described below, interest rate spreads for ABS guaranteed by the SBA or backed by government-guaranteed student loans were reduced during the quarterly period to reflect the reduced risk associated with these assets. The interest rate spread on TALF loans backed by collateral benefitting from a government guarantee will be 50 basis points, and different reference benchmarks may apply.
The TALF relies on specific collateral eligibility requirements in order to ensure that taxpayer funds are used to finance targeted asset classes whose probability of loss has been assessed by credit rating agencies. Given the important role that credit ratings play in the TALF’s eligibility criteria, Treasury and the Federal Reserve have conducted due diligence on rating agency methodologies for various ABS sectors. Moreover, each issuer is required to hire an external auditor that must provide an opinion, using examination standards, that management’s assertions concerning key collateral eligibility requirements are fairly stated in all material respects. The auditor’s attestation provides a high level of assurance concerning TALF collateral eligibility requirements.

In addition, following careful review and analysis, Treasury and the Federal Reserve on March 19, 2009, announced that the TALF would be expanded to include newly or recently issued AAA-rated ABS backed by four additional types of consumer and business loans – mortgage servicing advances, loans or leases relating to business equipment, leases of vehicle fleets, and floorplan loans. These new categories of collateral were eligible for inclusion in the April 2009, TALF subscription and funding process.

During the quarterly period, Treasury and the Federal Reserve also began to review, consider, and implement ways of further expanding the TALF. For example, on February 10, 2009, the Treasury and the Federal Reserve announced a potential expansion of the TALF, which could increase the maximum size of the facility from $200 billion to as much as $1 trillion and could broaden the eligible collateral to encompass additional types of ABS. Expansion of the TALF would be supported by an increase in the protection provided by Treasury from $20 billion to up to $80 billion.

The Federal Reserve and Treasury continue to carefully consider whether and under what conditions it would be appropriate to expand the TALF to include ABS backed by other asset classes, such as commercial mortgage-backed securities, private label residential mortgage-backed securities or structured financings backed by corporate debt. In addition, the agencies continue to carefully consider whether and under what conditions it would be appropriate to expand the TALF to include “legacy” ABS, that is, ABS that was not newly or recently issued.
b. **Unlocking Credit for Small Businesses**

Securitization of small business loans provides community banks and other lenders with an important source of capital from which to make additional loans. However, as a result of the severe dislocations in the credit markets that began in October 2008, both lenders that originate loans under SBA programs and the “pool assemblers” that package such loans for securitization have experienced significant difficulty in selling such loans or securities in the secondary market. This, in turn, has significantly reduced the ability of such lenders and pool assemblers to obtain funds to make or fund new small business loans. To help restore the confidence needed for financial institutions to increase lending to small businesses, Treasury announced the Unlocking Credit for Small Businesses program on March 16, 2009. The program is part of Treasury’s Consumer and Business Lending Initiative under the Financial Stability Plan.

Under the terms of the program as initially announced, Treasury will make up to $15 billion in TARP funds available to purchase securities backed by the SBA-guaranteed portions of loans made under the SBA’s 7(a) loan program, as well as first-lien mortgage securities made by private-sector lenders in connection with SBA’s 504 community development loan program. The SBA’s 7(a) program is the SBA’s most basic and widely used loan program. Under this program, lenders that structure their loans in accordance with SBA requirements are eligible to apply for and receive from the SBA a guarantee against payment default on a portion of a loan extended to a small business. To qualify for the program, a loan must not exceed $2 million, and the amount that may be guaranteed by the SBA is limited to no more than 90 percent of the loan.

The SBA’s 504 loan program provides eligible small businesses with long-term, fixed-rate financing for major fixed assets, such as land and buildings. Typically, a 504 project includes (i) a loan secured with a senior lien from a private-sector lender covering up to 50 percent of the project cost, (ii) a loan secured with a junior lien from a community development corporation covering up to 40 percent of the cost, which is backed by a 100 percent SBA-guaranteed debenture, and (iii) a contribution of at least 10 percent equity from the small business receiving the financing. The maximum amount of financing a 504 project may receive from all sources is $10 million, and the maximum SBA debenture is $1.5 million to $4 million depending on the purpose of the project and the industry of the business receiving the loan.

Treasury is working with lenders, pool assemblers and others to finalize the terms and conditions under which purchases of SBA-related loans and securities will be made under the Unlocking Credit for Small Businesses program. Treasury also has hired Earnest Partners, an independent investment manager, to help implement the program. The Bank of New York Mellon will act as Treasury’s custodian for the securities.
c. **Home Affordable Modification Program**

Preserving homeownership and stabilizing communities are important objectives of the EESA and TARP. In light of these objectives, the Oversight Board in its First Quarterly Report noted that, as additional resources became available, it would be important for the TARP to continue to pursue effective strategies for providing resources in support of reducing preventable foreclosures due to the harm that such foreclosures may have on the affected borrowers, communities, the housing market, and the financial system and broader economy.

In February 2009, Treasury announced the Home Affordable Modification Program (“HAMP”), which is intended to bring relief to responsible homeowners struggling to make their mortgage payments, while mitigating the spillover effects of preventable foreclosures on neighborhoods, communities, the financial system and the economy. Updated and more detailed program guidelines for the HAMP were released on March 4, 2009. Treasury worked in conjunction with HUD, FHFA and the Federal banking agencies, among others, in developing the HAMP and the HAMP guidelines.

The HAMP is designed to promote loan modifications by establishing a standardized and streamlined process for servicers (including lenders or investors that service their own loans) to follow in evaluating and conducting modifications of existing mortgages, and by providing meaningful incentives to servicers, investors and borrowers to encourage loan modifications. Treasury has indicated that going forward all recipients of assistance under the Financial Stability Plan, including participants in the Capital Assistance Program, will be required to implement foreclosure mitigation plans that are consistent with the HAMP. In addition, the federal bank, thrift, and credit union regulatory agencies have encouraged all federally-regulated financial institutions that service or hold residential mortgage loans to participate in the HAMP. The following highlights some of the key terms and conditions of the HAMP.

**i. Eligible Homeowners**

The HAMP is available to homeowners with first-lien loans on owner-occupied properties that have an unpaid principal balance of up to $729,750, and that were originated on or before January 1, 2009. Higher limits are allowed for owner-occupied properties with two-to-four units.

**ii. Servicer obligations and reductions in monthly mortgage payments**

Servicers participating in the HAMP are required to apply a standardized net present value (“NPV”) test on each loan that is at least 60 days delinquent or at risk of

---

9 See sections 2(2)(B) and 103(3) of the EESA (12 U.S.C. §§ 5201(2)(B) and 5213(3)).

10 Additional details of the program can be located at: [http://www.financialstability.gov/roadtostability/homeowner.html](http://www.financialstability.gov/roadtostability/homeowner.html).
imminent default. Importantly, servicers participating in the HAMP must apply the NPV test to all eligible loans that they service, unless explicitly prohibited by contract, and are required to use reasonable efforts to obtain waivers or approvals from all necessary parties in order to carry out modifications under the HAMP. The NPV test compares the net present value of cash flows from the mortgage if modified under the HAMP and the net present value of the cash flows from the mortgage without modification. If the NPV test is positive – meaning that the net present value of expected cash flows is greater if modified under the HAMP than if the loan was not modified – the servicer must modify the loan in accordance with the HAMP guidelines, absent fraud or a contract prohibition. Servicers wishing to participate in the HAMP program must enter into the applicable program agreements with Fannie Mae, acting as Treasury’s financial agent, on or before December 31, 2009.

The HAMP includes a standardized set of procedures that services must follow in modifying eligible loans under the program and in estimating the expected cash flows of modified mortgages. Servicers participating in the HAMP must first reduce the borrower’s monthly payments on the first-lien mortgage so that the borrower’s monthly mortgage payment is no greater than 38 percent of his or her gross monthly income. Then, servicers must follow a specified sequence of steps in order to reduce the monthly payment on the first-lien mortgage to no more than 31 percent of the borrower’s gross monthly income (the “DTI ratio”). Under this modification sequence, the servicer must reduce the interest rate (subject to a rate floor of 2 percent), then extend the term or amortization period of the loan up to a maximum of 40 years (if necessary), and then forbear principal (if necessary).11 Importantly, the HAMP provides the servicer the option to reduce principal on a stand-alone basis or before any of the steps described above to help reduce the borrower’s monthly payment to no more than 31 percent of gross monthly income. The borrower must remain current on his or her modified mortgage payments for at least 90 days in order for the HAMP loan modification to become permanent.

iii. Servicer, Investor and Borrower Incentives

To increase participation in the HAMP and encourage borrowers to remain current on loan modifications under the program, Treasury will provide targeted incentives to borrowers, lenders and servicers that participate in the program. For example, Treasury will –

• Share with the investor on a dollar-for-dollar basis the cost of reducing the first-lien mortgage payment from a 38 percent DTI ratio to a 31 percent DTI ratio, for up to five years;

11 If the interest rate on the modified loan is reduced below the Freddie Mac Primary Mortgage Market Survey Rate for 30-year fixed-rate conforming mortgages at the time the modification document are prepared, the interest rate may be increased (or “step-up”) after the fifth year of the modified mortgage by up to 1 percent each year until it reaches such rate.
• Provide a $1,000 payment to the servicers for each eligible modification meeting the program’s guidelines;

• Provide a $1,000 “pay for success” payment to servicers for each year a borrower remains current on the modified loan, up to a maximum of 3 years;

• Pay up to $1,000 per year (up to a maximum of 5 years) on behalf of an eligible borrower to reduce the principal balance of the modified loans if the borrower remains current on the mortgage;

• Make a one-time bonus payment to participating servicers and investors for modifications that are performed for borrowers who are current on their existing mortgage, but facing imminent default; and

• Make payments to investors and lenders (up to a maximum amount of $10 billion) holding modified loans if the value of the home subsequently declines as determined by reference to an appropriate home price index for the area in which the home is located.

Certain of these payments would be made only if the loan modification reduced the borrower’s monthly payment on the first-lien mortgage by more than a de minimis amount. As part of the HAMP, servicers also must consider whether a borrower should be offered a HOPE for Homeowners refinancing whenever feasible, and Treasury will make similar servicer incentives available to servicers in connection with a HOPE for Homeowners refinancing.

In addition, the HAMP will provide incentives for extinguishing second-liens on loans modified under the program and for short sales or deeds-in-lieu in cases where borrowers are not eligible for, or default on, a HAMP-modified loan. Borrowers whose total monthly debt payments (including housing and non-housing related debts) exceed 55 percent of their total monthly income must agree to obtain counseling from a HUD-approved counselor in order to reduce their total debt service payment, and thus improve their ability to remain current on their HAMP-modified loan.

iv. Taxpayer Protections

The terms of the program contain various provisions to protect the interests of taxpayers and reduce the potential for fraud. For example, borrowers will be required to provide declarations under penalty of perjury attesting to the truthfulness of the information that they have provided to the servicer to determine the borrower’s eligibility for entry into the HAMP. Borrowers also must provide evidence supporting their income
and a signed affidavit of financial hardship. Property owner occupancy status will be verified through the borrower’s credit report and other documentation to help ensure that investor-owned, vacant, or condemned properties do not enter the program. Servicers also will be required to collect, maintain and transmit records for verification and compliance review, including documentation and data relating to borrower eligibility, underwriting, incentive payments, property verification, and other matters. Treasury also has hired Freddie Mac to serve as its compliance agent in connection with the HAMP.

The HAMP, which will be funded under the TARP, is one component of the Administration’s Making Home Affordable plan. The broader Making Home Affordable plan also includes a separate refinancing program that will be offered through Fannie Mae and Freddie Mac and is designed to provide a low-cost refinancing option to eligible homeowners whose mortgages are owned or guaranteed by Fannie Mae or Freddie Mac. This separate refinancing program will be operated and funded outside of TARP.\(^\text{12}\)

d. Capital Purchase Program

Treasury created the Capital Purchase Program (“CPP”) in October 2008 to address the severe stresses facing financial institutions and markets, maintain confidence in U.S. financial institutions, and provide financial institutions with the capital needed to support the flow of credit to businesses and consumers during the financial turmoil and economic downturn. The CPP is Treasury’s largest and most significant financial stability program under the EESA.

To achieve Treasury’s goals of maintaining stability and confidence in the financial system, the CPP was purposefully designed to encourage the broad participation of institutions of all sizes and types across the country. The CPP is open to qualifying banks, savings associations, bank holding companies and savings and loan holding companies (Qualifying Financial Institutions or “QFIs”) of all sizes that are viable and Treasury has worked to establish common, standardized terms under which different types of eligible institutions (e.g., publicly held organizations, privately-held organizations and S-Corporations) may participate.

The application deadline for eligible publicly-held financial institutions to apply for capital under the CPP was November 14, 2008, and the application deadline for eligible privately-held financial institutions (other than S-Corporations) was December 8, 2008. As discussed below, Treasury during the quarterly period also established standardized terms under which eligible S-Corporations may participate in the CPP. The application deadline for Subchapter S-Corporations was February 13, 2009.

Pursuant to the EESA, Treasury built into the terms of the CPP agreements provisions to protect the interests of taxpayers and generate a return on the capital

\(^{12}\) Additional information concerning the separate refinancing program offered through Fannie Mae and Freddie Mac is available at: [http://www.treas.gov/press/releases/reports/housing_fact_sheet.pdf](http://www.treas.gov/press/releases/reports/housing_fact_sheet.pdf).
provided. For example, institutions that participate in the CPP are subject to executive compensation, dividend and stock repurchase restrictions and must provide the Treasury warrants in accordance with the EESA, Treasury’s regulations and guidance, and the terms of the purchase agreements entered into between Treasury and the institution.13

i. Update on Transactions under the CPP

As of March 31, 2009, Treasury had invested approximately $198.8 billion under the CPP in senior preferred shares or other senior securities of 532 financial institutions located in 48 states, the District of Columbia, and Puerto Rico.14 Treasury designed the CPP to provide capital to a broad range of institutions in communities across the country, and the institutions that Treasury has funded under the CPP include small, community, regional and large banking organizations, as well as community development financial institutions, with investment amounts ranging from as large as $25 billion to as small as $301,000.

As part of Treasury efforts to ensure greater transparency of its programs under the EESA and the Financial Stability Plan, Treasury announced on January 28, 2009, that it will begin posting all of its investment contracts on Treasury’s website in five to ten business days of each transaction’s closing. Treasury has posted many CPP contracts and is currently in the process of posting all CPP contracts signed prior to January 28 to the website.15

ii. Establishment of terms relating to Subchapter S-Corporations

During the quarterly period, Treasury released standardized terms for CPP investments in QFIs that have elected to be taxed as S-Corporations. Under the Internal Revenue Code, S-Corporations may not have more than one class of stock and, thus, may not issue preferred stock to Treasury like other QFIs under the CPP. Additionally, S-Corporations may not have more than 100 shareholders, subject to limited exceptions, and the institution’s shareholders must all be natural persons. In light of these restrictions, Treasury, in consultation with the Federal banking agencies, worked to structure a security that S-Corporation QFIs could issue to Treasury that was economically comparable to the senior preferred stock and warrants issued by other QFIs under the CPP and would be considered regulatory capital of the issuing organization.

13 Additional background information concerning the CPP is included in the Board’s First Quarterly Report and is available at: http://www.financialstability.gov/docs/FSOB/FINSOB-Qrtly-Rpt-123108.pdf.


The CPP terms for S-Corporations, which were released on January 14, 2009, and reviewed and considered by the Oversight Board, provide for such organizations to issue senior subordinated debentures instead of equity to the Treasury. The subordinated debentures will have a maturity of 30 years and will pay an annual interest rate of 7.7 percent for five years, and thereafter pay an annual interest rate of 13.8 percent. The subordinated debentures are senior to the QFI’s common stock (and any other class of equity if the QFI converts to a C Corporation), but must be expressly subordinated to claims of depositors and other debt obligations to the organization’s general and secured creditors, unless those debt obligations are subordinate to the senior securities. Other terms of the senior subordinated debentures are similar to those applicable to the perpetual preferred stock issued under the CPP. For example, the maximum subscription amount for an S-Corporation under the CPP is equal to the lesser of 3 percent of its risk-weighted assets or $25 billion.

The CPP terms developed for S-Corporations also include several provisions designed to protect the interests of taxpayers. For example, in connection with each investment, as required by the EESA, Treasury will receive warrants to purchase additional subordinated debentures in an amount equal to 5 percent of Treasury’s investment. These warrants are immediately exercisable, in whole or in part, at a price of $0.01, and have a term of 10 years. Treasury has regularly exercised these warrants immediately following closing. In addition, S-Corporations that receive CPP capital must abide by restrictions on dividends and share buybacks that are designed to be equivalent to the restrictions imposed on other types of institutions participating in the CPP. S-Corporation participants, like all CPP participants, also must abide by all executive compensation restrictions applicable under EESA and Treasury regulations and guidelines.

iii. Implementation of and Results of Monthly Intermediation Snapshots and Lending Reports

In January 2009, Treasury initiated a monthly intermediation survey or “Snapshot” of the 20 QFIs receiving the largest amount of capital under the CPP. These institutions are Bank of America, BB&T, Bank of New York Mellon, Capital One, CIT, Citigroup, Comerica, Fifth Third, Goldman Sachs, JPMorgan Chase, KeyCorp, Marshall & Ilsley, Morgan Stanley, Northern Trust, PNC, Regions, State Street, SunTrust, U.S. Bancorp and Wells Fargo. In March 2009, American Express was included in this group following approval of its application under the CPP. The survey obtains data from the institutions on their lending and intermediation activities during the relevant monthly period. The monthly intermediation surveys of the largest CPP

---

16 On an after-tax basis, and assuming a 35 percent tax rate, these are the same rates applicable to other classes of institutions participating in the CPP (i.e., interest rates of 5 percent and 9 percent, respectively).

17 Lending data is requested for first mortgage loans, home equity loans, managed credit
recipients are designed to provide Treasury and the public regular and frequent insights into the lending and other intermediation activities of these institutions, and how such activities may change over time.

The first intermediation snapshots were requested in January 2009, and covered the period during October, November and December 2008. The results of this initial survey were released on February 17, 2009. On March 15, 2009, Treasury released the results of the second monthly survey covering January 2009. Additional snapshots will be conducted for each succeeding month, with the results published on the 15th of the following month.

The demand for credit by consumers and businesses typically falls during an economic downturn, reflecting caution by both lenders and borrowers to take on new risk during uncertain economic times. Therefore, the Snapshot cannot, but itself, answer what lending levels would have been without the CPP. However, the survey and Snapshot of the 20 largest CPP participants, which account for more than two-thirds of banking assets, illustrated that the level of loan originations largely held steady from October to December 2008, the 3 months following the launch of the CPP. Given the severe dislocation in the credit markets during this time, these lending levels would have likely been lower absent CPP capital.

In March 2009, Treasury also announced that it would initiate an additional Monthly Lending Report for all CPP recipients. Like the Monthly Intermediation Snapshots, the Monthly Lending Report is designed to provide insights into the lending and intermediation activities of the recipients of capital under the CPP. However, in light of the small size of many CPP recipients and the burden a detailed report would introduce on such institutions, the Monthly Survey Report will obtain a more streamlined set of information from participants than the Monthly Intermediation Snapshots. The first Monthly Lending Report, responses to which are due by April 30, 2009, requested data from CPP participants for the months of February and March 2009. The results of this and future Monthly Survey Reports will be made public.

In addition to these efforts, Treasury continues to work actively with the Federal Reserve and other Federal banking agencies to develop a more in-depth report and analysis of the lending and intermediation activities of recipients of TARP capital using the comprehensive loan and other data reported quarterly by banks on their regulatory Call Reports and by bank holding companies on their Federal Reserve “Y” series reports.

card loans, other consumer loans, commercial and industrial loans and leases, and commercial real estate loans and leases. Beginning with the April 2009 survey, information also will be collected regarding small business lending. Intermediation activities for which data are collected are purchases of mortgage-backed and asset-backed securities, secured lending activities (repurchase and reverse repurchase agreements and margin lending), and underwriting of equity and debt securities.
iv. *Withdrawal of CPP Applications and Repayment of CPP Investments*

During the quarterly period, a significant number of institutions chose to withdraw their CPP applications after receiving preliminary approval from Treasury. As of March 27, 2009, more than 250 institutions that had received such preliminary approval subsequently withdrew their applications for CPP capital. To the extent that such withdrawals reflect a wariness of qualifying financial institutions to seek or receive capital under the TARP, the actions run counter to the purposes of the CPP, which are to make capital available to broad segments of the banking industry in order to promote stability, public confidence in the financial system and support lending to households and businesses.

On February 17, 2009, the American Reinvestment and Recovery Act ("ARRA") was enacted.18 Section 7001 of the ARRA allows QFIs that received capital under the CPP to redeem such capital with funds obtained from any source without having to comply with any contractually required waiting period. Section 7001 also requires the Treasury to liquidate the warrants acquired in connection with a CPP investment if the institution redeems the capital provided by Treasury. On February 26, 2009, Treasury issued Frequently Asked Questions to help institutions understand the changes made by section 7001 of the ARRA and the process for requesting redemption of CPP capital.19 Capital provided under the CAP is not eligible for redemption under the ARRA. As provided in the ARRA, Treasury will consult with the institution’s appropriate Federal banking agency regarding any proposed redemption of CPP capital to ensure that any proposed redemption is consistent with the safety and soundness of the relevant banking organization. As of March 31, 2009, five organizations had redeemed an aggregate principal amount of approximately $353 million in CPP capital.20

---


20 As part of these redemptions, the organizations also paid approximately $2.26 million in accrued but unpaid dividends to Treasury.
e. **Capital Assistance Program**

The Capital Assistance Program (“CAP”) announced by Treasury on February 25, 2009, is an important component of the Financial Stability Plan. The CAP is intended to further bolster confidence in the resilience of financial institutions by helping to ensure that these financial institutions have sufficient capital to sustain their role as intermediaries and continue to provide loans to creditworthy borrowers even if economic conditions suffer a severe and extended deterioration. Providing financial institutions access to such capital resources should help maintain confidence in the strength and viability of the country’s financial institutions and allow institutions to play their critical role as intermediaries in promoting economic recovery.

The CAP consists of two core elements. The first component is a one-time, forward looking assessment or “stress-test” that is being conducted by the Treasury, in conjunction with the Federal banking agencies, on the 19 largest bank holding companies (“BHCs”), each of which has consolidated risk-weighted assets of at least $100 billion. The purpose of this stress-test is to assess whether these BHCs have the capital to continue lending and absorb potential losses that could result from a more severe decline in economic conditions than currently projected by economic forecasters. As part of this exercise, participating BHCs will analyze their loan and securities portfolios, as well as off-balance sheet commitments and contingencies, to estimate future losses under both a baseline scenario and a more adverse scenario of future economic conditions. The BHCs also will forecast the internal resources available to absorb such losses, should they occur.

Based on the results of this review, other supervisory information available to the agencies relating to the specific institution, and discussions with the institution’s management, the agencies will determine whether a participating organization has sufficient regulatory capital to remain well capitalized under the more adverse economic scenario. Should this assessment indicate the need for additional capital, the BHC will be provided a six month period to raise the capital from private sources. The BHCs also will have the ability to obtain the additional capital through the CAP, either on a stand-alone basis or in conjunction with any private capital raises.

The second aspect of the CAP is the availability of “contingent” common equity to eligible banking organizations. Market participants pay particular attention to common equity as a measure of health in stressed environments, and regulators have long believed that common equity should be the dominant component of a banking organization’s capital. Accordingly, the capital provided by the CAP will take the form of convertible preferred stock. These preferred shares will be convertible, at the organization’s option and subject to the approval of the appropriate Federal banking agency, into common stock of the banking organization at a 10 percent discount from the 20-day trailing average of the organization’s common stock price on February 9, 2009. The shares also
would mandatorily convert into common stock at such conversion price after 7 years. The convertible preferred shares will carry a 9 percent annual dividend.\(^2\)

An eligible financial institution may apply under the CAP to issue to Treasury convertible preferred stock equal to no less than 1 percent of its risk-weighted assets and no more than 2 percent of its risk-weighted assets. An eligible institution also may apply to obtain CAP convertible preferred capital to replace (i.e., redeem) any non-convertible preferred shares previously issued to Treasury under the CPP and, if applicable, the TIP. A participating institution that needs capital in excess of these amounts may qualify for “exceptional assistance,” to be determined by the Treasury in consultation with the appropriate Federal banking agency. Any “exceptional assistance” may be subject to additional organization-specific conditions. The eligibility criteria and application process for the CAP is similar to those established for the CPP.

The terms of the CAP also include several provisions designed to protect the interests of taxpayers. For example, in connection with investments under the CAP and as required by EESA, Treasury will receive warrants to purchase common stock of the banking organization with a market value equal to 20 percent of the convertible preferred amount on the date of the investment.\(^2\) In addition, for so long as any convertible preferred shares are outstanding and owned by the Treasury or the Treasury owns any common stock of the banking organization, the organization may not declare or pay any dividends on its common stock in excess of $0.01 per share per quarter without Treasury’s consent. A banking organization receiving capital through the CAP will be required to submit: (i) a plan describing how the organization intends use the capital received to support its lending activities and (ii) monthly reports to Treasury on its lending activities that include a comparison of actual lending activities to a baseline. Recipients also will be required to abide by Treasury’s regulations and guidance relating to executive compensation and other matters.

U.S. government ownership is not an objective of the CAP, although the government has the potential to acquire a substantial portion of the outstanding common shares of a participating institution. To the extent that the U.S. government acquires any ownership stake in a participating institution, Treasury will maintain the goal of keeping the period of government ownership as temporary as possible and encourage the return of private capital to replace the government investment. Treasury will use reasonable efforts to sell at least 20 percent of any common equity it acquires each year. In addition, any capital investments made by Treasury will be placed in a separate trust (the Financial

\(^2\) The annual dividend will increase to 20 percent per annum if shareholder approval is necessary for the banking organization to issue the common stock to the Treasury upon conversion and the organization has not received such approval within 6 months of issuance of the convertible preferred.

\(^2\) The exercise price of the warrants will be adjusted downward (subject to a maximum reduction of 45 percent) if shareholder approval is necessary to allow the exercise of the warrants and such approval is not received.
Stability Trust) set up to manage the government’s investments in U.S. financial institutions. The objective of the Trusts will be to protect and create value for the taxpayer as a shareholder over time.

The deadline to apply to the CAP is May 25, 2009. While the CAP currently is available only to publicly-traded institutions on standardized terms published on February 25, 2009, Treasury is working to develop equivalent, standardized terms for privately held organizations.23

f. Public-Private Investment Program

To promote financial stability and improve the functioning of the financial system, Treasury, in conjunction with the Federal Reserve and the FDIC, announced the Public-Private Investment Program (“PPIP”) on March 23, 2009. A part of the Financial Stability Plan, the PPIP is designed to improve the condition of financial institutions by facilitating the removal of legacy assets from their balance sheets, which should help financial institutions make new loans available to households and businesses and better support economic recovery. The PPIP also should help increase the liquidity and functioning of the markets for legacy assets. As a general matter, the term “legacy assets” refers to loans, asset-backed securities and other types of assets that were originated or issued before the financial markets for these types of assets deteriorated significantly in 2008. As explained further below, the PPIP seeks to draw new private capital into the market for legacy assets through the provision of government equity co-investment and attractive public financing. The program has two major components, each of which is structured to protect taxpayers and encourage participation by a broad range of financial institutions.

i. Legacy Securities Program

The Legacy Securities Program initially will target commercial mortgage-backed securities and residential mortgage-backed securities that were issued prior to 2009 and that had a AAA (or equivalent) rating upon issuance. Under the principal terms of the Legacy Securities Program, Treasury will partner with approved asset managers. Treasury will evaluate applications from prospective fund managers based on a number of criteria, including the applicant’s capacity to raise private capital and the applicant’s performance track record in managing eligible asset classes. Asset managers whose proposals have been pre-approved will have a certain period of time, estimated to be twelve weeks, within which to raise private capital for a public-private investment fund (“PPIF”) to target the designated asset classes. Treasury will invest equity capital from the TARP in the PPIF on a dollar-for-dollar basis with participating private investors. In addition, fund managers will have the option to obtain debt financing for the fund from Treasury in an amount up to 100 percent of the fund’s total equity capital, subject to

23 Eligibility requirements are available at: http://www.financialstability.gov/roadtostability/capitalassistance.html.
certain restrictions on leverage, withdrawal rights, cash flow priority, disposition priorities and other factors that Treasury deems appropriate.24

PPIFs participating in the Legacy Securities Program may also obtain financing for the purchase of eligible assets through the TALF (if, as discussed above, the TALF is expanded to include legacy assets), through other Treasury programs or through debt raised from private sources, provided that Treasury’s equity capital and the private investors’ equity capital must be leveraged proportionately from such other debt financing sources. Treasury will participate pro rata in any profits or losses of a fund alongside the private investors, and Treasury will receive warrants in each PPIF as required by the EESA. Each PPIF will seek to generate attractive returns through a predominately long-term buy and hold strategy, although Treasury will consider other strategies that involve limited trading.

**ii. Legacy Loans Program**

To help remove troubled legacy loans from bank balance sheets and, thus, reduce the overhang of uncertainty associated with such assets, the FDIC and Treasury established the Legacy Loans Program. This program seeks to attract private capital to purchase eligible legacy loans and other assets from participating banks through the availability of FDIC debt guarantees and Treasury equity co-investments. Under the program, PPIFs will be formed to purchase and manage pools of legacy loans and other assets held by U.S. banks and savings associations.

Interested banks will work with their primary federal regulator to identify and evaluate eligible asset pools. The FDIC will oversee auctions through which such asset pools would be sold to PPIFs in which eligible private investors hold at least a 50 percent equity stake. A third party valuation firm will analyze the value of the eligible asset pools and advise the FDIC on the supportable leverage for each pool, which is not anticipated to exceed a 6-to-1 debt-to-equity ratio. The FDIC will provide a guarantee of the debt issued by the PPIF and collect a guarantee fee, and the Treasury intends to provide up to 50 percent of the equity capital for each PPIF. Treasury will participate pro rata in any profits or losses of a fund alongside the private investors, and Treasury will receive warrants in each PPIF as required by the EESA.

The FDIC and Treasury will enter into an agreement governing the allocation of costs and responsibilities with respect to the PPIFs. The FDIC will be responsible for overseeing the formation, funding and operation of PPIFs and for overseeing and managing the debt guarantees it provides to the PPIFs. In its oversight, the FDIC will ensure that the same information is provided to both the FDIC and Treasury and will be reimbursed for related oversight expenses. The Treasury will be responsible for overseeing and managing its equity contributions to the PPIFs.

---

Each PPIF must agree to take such actions as the Treasury and the FDIC may require to protect against waste, fraud and abuse, and must provide certain representations, warranties and covenants regarding the conduct of their business and compliance with applicable law. In addition, the terms of the program prevent private investors from participating in any PPIF that purchases assets from sellers that are affiliates of such investors or that represent ten percent or more of the aggregate private capital in the PPIF. The FDIC requested public comment on the Legacy Loan Program and this comment period closed on April 10, 2009. The exact requirements and structure of the Legacy Loans Program will be determined following consideration of the comments received through this process.25

g. Targeted Investment Program and Asset Guarantee Program

Treasury established the Targeted Investment Program (“TIP”) and the Asset Guarantee Program (“AGP”) under the TARP during the fourth quarter of 2008. The TIP provides the Treasury with the necessary flexibility to provide additional or new funding to financial institutions that are critical to the functioning of the financial system. The TIP is designed to prevent a loss of confidence in critical financial institutions, which could result in significant financial market disruptions, threaten the financial strength of similarly situated financial institutions, impair broader financial markets, and undermine the overall economy.

Treasury established the AGP pursuant to section 102 of the EESA and with the same objective of financial market stability.26 As with the TIP, the AGP is a targeted program aimed at maintaining the stability of systemically important financial institutions and, thereby, reducing the potential for problems at such an institution to “spillover” to the broader financial system and economy. More specifically, the AGP may be used to provide “insurance” against the risk of significant loss in a pool of assets held by a systemically significant financial institution that faces a risk of losing market confidence due in large part to its holdings of distressed or illiquid assets. By helping limit the institution’s exposure to losses on illiquid or distressed assets, the AGP can help the institution maintain the confidence of its depositors and other funding sources and continue to meet the credit needs of households and businesses.

Eligibility to participate in the TIP and AGP is determined on a case-by-case basis based on a number of factors described in the guidelines that Treasury has established for the programs.27 The AGP will be applied with extreme discretion and Treasury does not


26 Section 102 of the EESA required that the Secretary establish a program to guarantee troubled assets originated or issued prior to March 14, 2008, if the Secretary purchased troubled assets under the TARP. See 12 U.S.C. § 5212.

27 Additional details regarding the eligibility requirements for the TIP are available at: http://www.financialstability.gov/roadtostability/targetedinvestmentprogram.html.
anticipate that the program will be made widely available. All participants in the TIP and AGP must comply with all applicable executive compensation and warrant requirements of the EESA and Treasury regulations, as well as any additional restrictions or conditions that may be applied as part of the investment or guarantee agreement.

During the first quarter of 2009, Treasury took actions under the TIP or AGP to help stabilize Bank of America and Citigroup, two institutions that are critical to the U.S. and global financial system.

i. *Actions relating to Bank of America Corporation*

As part of the CPP, on October 28, 2008, Treasury acquired $15 billion of preferred stock of Bank of America and committed to purchase $10 billion of preferred stock of Merrill Lynch, with the settlement deferred pending completion of the firm’s planned acquisition by Bank of America, which was consummated on January 1, 2009. Prior to consummation of the transaction, however, ongoing strains in financial markets and a weakening of economic conditions placed additional stress on Merrill Lynch and Bank of America during the fourth quarter of 2008.

On January 16, 2009, Bank of America reported net losses of $1.8 billion for the fourth quarter of 2008, and Merrill Lynch reported net losses of $15.3 billion for the same period. These losses had the potential to weaken materially investor and counterparty confidence in the combined entity and to hamper its ability to continue to obtain funding in the fragile credit markets then prevailing. If left unaddressed, this situation could have posed risks to financial stability and increased the already strong downward pressures on the economy. For example, as of the end of the third quarter of 2008, Bank of America had more than $940 billion in loans and leases outstanding and controlled more than $776 billion in domestic deposits.

In light of these and other factors, on January 16, 2009, Treasury, the FDIC and the Federal Reserve agreed to provide Bank of America with a package of capital, guarantees and liquidity access. As part of this package, Treasury acquired an additional $20 billion of preferred stock of Bank of America carrying an 8 percent dividend under the TIP. As part of the transaction, Treasury also received warrants to purchase common stock of Bank of America with an aggregate exercise value of $2 billion.

The terms of the investment include several provisions designed to protect the interests of the taxpayer. For example, under the terms of the preferred stock agreement, Bank of America is required to abide by enhanced executive compensation and corporate expenditure standards. In addition, Bank of America is prohibited from paying dividends on common stock in excess of $0.01 per share per quarter for three years without the consent of Treasury. Bank of America also must continue to maintain a policy requiring oversight and approval of major corporate expenses, including those involving conferences and events, travel, corporate aircraft usage and entertainment. In addition, Bank of America must maintain a policy regarding lobbying, government ethics and political activity, which includes, among other things, restrictions on governmental gifts, lobbying and political contributions.
As part of this package of supports, Treasury and the FDIC also agreed to share with Bank of America losses on a designated pool of up to $118 billion of loans, securities backed by residential and commercial real estate loans and corporate debt, derivative transactions that reference such securities, and other financial instruments. The terms of this asset-guarantee arrangement and related Federal Reserve financing (see below) are being finalized and documented and the arrangements had not closed as of March 31, 2009. The designated pool of financial instruments will represent primarily assets of Merrill Lynch that are now held by Bank of America and will remain on Bank of America’s consolidated balance sheet. Bank of America is required to manage the assets in the designated asset pool in accordance with a foreclosure mitigation policy acceptable to Treasury. Treasury participated in these loss-sharing arrangements under the AGP.

Under the terms of the loss protection arrangement, Bank of America will absorb the first $10 billion in future losses on the asset pool (the “first loss position”). Treasury, the FDIC and Bank of America will share any additional losses (the “second loss position”). Bank of America will bear 10 percent of the second loss position, and the remaining 90 percent portion of the second loss position would be allocated between Treasury (75 percent) and the FDIC (25 percent), up to a maximum of $7.5 billion for Treasury and $2.5 billion for the FDIC. These loss-sharing arrangements will be in effect for up to 10 years for the residential mortgage-related assets in the designated asset pool and 5 years for the other assets in the pool. As compensation for these guarantees, Treasury and FDIC will receive $3 billion and $1 billion in preferred stock, respectively, along with accompanying warrants. The amount of preferred stock and warrants received by Treasury as compensation for the guarantee may be adjusted, as necessary, based on the results of an actuarial analysis of the final composition of the designated pool of financial instruments to ensure that the compensation fully protects the taxpayer as provided in section 102(c) of the EESA.28

In connection with these actions, the Federal Reserve agreed to provide Bank of America with certain non-recourse financing for the pool of financial instruments if and only if Bank of America incurs additional mark-to-market and credit losses in the pool that exceed $18 billion. The Federal Reserve’s credit exposure on the loan would be reduced by the Bank of America first loss position, the second loss position shared by the Treasury, FDIC and Bank of America, and a continuing 10 percent loss sharing agreement between the Federal Reserve and Bank of America. The Federal Reserve’s credit exposure would be further limited by Bank of America’s pledge of U.S. Treasury securities or other assets eligible for the Federal Reserve to purchase.29

28 Additional information concerning the capital investment and loss protection provided by Treasury is available at: http://www.financialstability.gov/latest/hp1356.html.

29 Additional details concerning these financing arrangements are available at: http://www.federalreserve.gov/monetarypolicy/files/129bofa.pdf.
On October 28, 2008, the Treasury acquired $25 billion of preferred stock of Citigroup, as well as related warrants, as part of the first tranche of capital purchases made under the CPP. In the weeks following Treasury’s investment, however, investors became increasingly concerned about Citigroup’s financial prospects and viability, which threatened the company’s ability to obtain funding. In light of these continuing pressures and other factors, including conditions in the financial markets and the state of the U.S. economy, on November 23, 2008, Treasury agreed to acquire an additional $20 billion of preferred shares of Citigroup and related warrants under the TIP. In addition, Treasury, the FDIC and Federal Reserve agreed to provide Citigroup with certain loss protection and liquidity supports with respect to a designated asset pool of up to $306 billion of loans and securities backed by residential and commercial real estate and other assets.

On December 31, 2008, Treasury consummated its acquisition of the additional preferred shares and related warrants of Citigroup under the TIP.30 In addition, on January 16, 2009, Treasury announced finalization of the terms of the loss protection arrangements with Citigroup. Following valuation adjustments, these loss sharing arrangements will provide Citigroup certain protections against additional losses on a designated pool of approximately $301 billion in assets, including loans and securities backed by residential and commercial real estate, consumer loans and other assets. Under these arrangements, Citigroup will first bear responsibility (the “first loss position”) for any losses on the designated asset pool up to $39.5 billion (of which $9.5 billion was composed of the company’s existing loan loss reserve). In the event the covered losses exceed Citigroup’s first loss position, the losses will be shared among Citigroup, Treasury, and the FDIC. Citigroup will bear responsibility for the first 10 percent of the additional losses and the remaining portion will be allocated first to the Treasury, up to a maximum of $5 billion (the “second loss position”), and then to the FDIC, up to a maximum of $10 billion (the “third loss position”). These loss-sharing arrangements will be in effect for 10 years for residential mortgage-related assets in the designated asset pool and 5 years for other assets in the pool. As compensation for these guarantees, the Treasury and FDIC received $4.034 billion and $3.025 billion, respectively, of preferred stock. Treasury also received warrants to acquire approximately 66.5 million shares of common stock at a strike price of $10.61 per share. The terms of the preferred stock and warrants acquired by Treasury as part of these guarantees are substantially similar the terms of the preferred stock and warrants acquired by Treasury under the TIP.

As part of these arrangements, the Federal Reserve also agreed to provide certain financing to Citigroup if the covered losses exceed Citigroup’s first loss position, plus

---

approximately $16.7 billion (of which $15 billion will have been absorbed by Treasury and the FDIC). Such financing would be provided in an amount equal to the aggregate value of the assets remaining in the designated asset pool, subject to certain adjustments. If additional losses on the assets are incurred, Citigroup must immediately repay 10 percent of such losses to the Federal Reserve, thus continuing its 10 percent loss sharing obligation with respect to the assets. The loan would be secured by the remaining assets in the pool, and would be non-recourse to Citigroup, except with respect to these loss-sharing repayments and interest payments.\(^{31}\)

On February 27, 2009, Treasury also announced that it would participate in a planned exchange offering announced by Citigroup. Treasury’s participation in the exchange offering will bolster Citigroup’s tangible common equity capital (a key financial metric), thus improving its ability to withstand ongoing market turbulence without requiring any new commitment of TARP funds. Under the terms of the exchange, which the Oversight Board reviewed and considered, Treasury would have the ability to convert the $25 billion of Citigroup preferred stock acquired under the CPP into a new security that will convert into common shares, pending a shareholder vote to amend the Citigroup charter to allow for an increase in the number of authorized common shares. Treasury also would exchange the Citigroup preferred shares received under the TIP and the AGP for trust preferred shares of greater structural seniority with the same 8 percent dividend rates as the existing preferred shares. Treasury’s participation in the exchange transactions is subject to certain conditions designed to protect the interests of taxpayer and promote Citigroup’s efforts to attract private capital. For example, Treasury will participate in the exchange offering only if at least $11.5 billion in privately held preferred stock is converted and will convert only the amount of Citigroup preferred shares that Citigroup’s private preferred shareholders are willing to convert. In addition, under the conditions established, Treasury must receive the most favorable terms and price offered to any other preferred shareholder.

h. American International Group, Inc.

AIG is a systemically important financial institution that, as of December 31, 2008, reported consolidated total assets of approximately $860 billion. In the U.S., AIG has approximately 30 million customers and 50,000 employees, and provides insurance to approximately 180,000 small businesses and other corporate entities, which employ approximately 106 million people in the United States. AIG conducts insurance and finance operations in more than 130 countries and jurisdictions and has more than 74 million individual and corporate customers and 116,000 employees globally.

AIG operates in four general business lines through a number of subsidiaries: (i) general insurance; (ii) life insurance and retirement services; (iii) financial services; and (iv) asset management. In 2007, AIG’s U.S. life and health insurance businesses ranked first in the United States in terms of net premiums written ($51.3 billion) and third...
in terms of total assets at year-end ($364 billion). For the same period, AIG's U.S.
property and casualty insurance businesses ranked second in the U.S. in terms of net
premiums written ($35.2 billion) and third in terms of total assets at year-end
($124.5 billion).

In addition to its on-balance-sheet positions, AIG is a major participant in a wide
range of derivatives markets through its Financial Services division, and particularly
through its AIG Financial Products business unit (“AIGFP”), and is a significant
counterparty to a number of major national and international financial institutions. AIG
also is a major provider of protection to municipalities, pension funds, and other public
and private entities through guaranteed investment contracts and products that protect
participants in 401(k) retirement plans. A significant portion of the guaranteed
investment agreements and financial derivative transactions entered into by AIGFP
include provisions that require AIGFP, upon a downgrade of AIG's long-term debt
ratings, to post additional collateral or, with the consent of the counterparties, assign or
repay its positions or arrange a substitute guarantee of its obligations by an obligor with
higher debt ratings.

Since September 2008, the Federal Reserve and Treasury have taken a series of
actions related to AIG in order to protect financial stability, a necessary prerequisite to
the resumption of economic growth. These measures focused on addressing the liquidity
and capital needs of AIG, thereby helping to stabilize the company and prevent a
disorderly failure, which would have severely disrupted financial markets and contributed
to a further worsening of economic conditions. As part of these coordinated financial
stability actions, Treasury in November 2008, acquired $40 billion in newly issued senior
preferred stock of AIG under the Systemically Significant Failing Institutions Program
(“SSFI”) established under the TARP.32

The SSFI program is designed to permit the Treasury to provide targeted
assistance to prevent the failure of systemically significant financial institutions. In an
environment of substantially reduced confidence, severe strains, and high volatility in
financial markets, the disorderly failure of a systemically significant institution could call
into question the financial strength of other similarly situated financial institutions,
disrupt financial markets, raise borrowing costs for households and businesses, and
reduce household wealth. The resulting financial strains could threaten the viability of
otherwise financially sound businesses, institutions, and municipalities, resulting in
adverse spillovers on employment, output, and income.

Despite these coordinated actions, AIG continued to face strong liquidity and
capital pressures in the fourth quarter of 2008. As a consequence of increased economic
weakness and market disruption, the insurance subsidiaries of AIG, like many other
insurance companies, recorded significant losses on investments in the fourth quarter of

32 For a discussion of this restructuring, see the Oversight Board’s First Quarterly
Report, which is available at: http://www.financialstability.gov/docs/FSOB/FINSOB-
Qrtly-Rpt-123108.pdf.
2008. At the same time, general economic weaknesses along with a tendency of the 
public to pull away from a company that it viewed as having an uncertain future, hurt 
AIG’s ability to generate new business during the second half of 2008 and caused a 
oticeable increase in policy surrenders. In addition, the severe financial and economic 
conditions that existed during the fourth quarter greatly complicated and delayed AIG’s 
plans to divest significant parts of the company in order to repay the U.S. government for 
its previous support. On Monday, March 2, 2009, AIG announced a loss of 
approximately $62 billion for the fourth quarter of 2008, ending a year in which AIG 
suffered approximately $99 billion in total net losses.

In the context of this backdrop, on March 2, 2009, Treasury and the Federal 
Reserve announced a restructuring of the government’s assistance to AIG in order to help 
stabilize this systemically important company and the financial system, enhance the 
company’s capital and liquidity, and facilitate the orderly completion of the company’s 
global divestiture program. These restructuring actions also begin to separate the major 
non-core businesses of AIG.

Under the terms of the restructuring, Treasury will create a new equity capital 
facility for AIG under the SSFI program pursuant to which AIG may obtain up to 
$30 billion of capital as needed over the 5-year life of the facility in exchange for newly-
issued non-cumulative preferred stock. The preferred stock issued to Treasury under this 
facility will pay a non-cumulative dividend of 10 percent per year, and will provide 
Treasury the right to elect two directors of AIG’s board of directors if AIG does not pay 
dividends for four quarterly periods, regardless of whether the periods are consecutive. 
Treasury also will receive warrants that will entitle Treasury to purchase common stock 
of AIG.33

Treasury also will exchange the $40 billion of cumulative perpetual preferred 
shares in AIG, previously acquired in November 2008, for preferred shares with revised 
terms that more closely resemble common equity. The new preferred stock provides non-
cumulative dividends and limits AIG’s ability to redeem the preferred, except with the 
proceeds from the issuance of equity capital. AIG must continue comply with the 
executive compensation and corporate governance requirements of EESA, as 
implemented Treasury, including the most stringent limitations on executive 
compensation as required under the newest amendments to the EESA. Additionally, AIG 
must continue to maintain and enforce newly adopted restrictions put in place by the new 
management on corporate expenses and lobbying as well as corporate governance 
requirements.

33 Under the terms of the Federal Reserve’s initial credit facility provided to AIG in 
September 2008, AIG issued shares of perpetual, non-redeemable convertible 
participating preferred stock to a trust that holds the stock for the benefit of Treasury. 
This preferred stock will convert into 79.9 percent of AIG’s common stock on a fully 
diluted basis, less the percentage of common stock that may be acquired by or for the 
benefit of Treasury as a result of warrants or other convertible preferred stock held by 
Treasury.
In connection with the actions taken by the Treasury, the Federal Reserve also authorized a number of additional actions to reduce and restructure AIG’s outstanding debt to the Federal Reserve under the revolving credit facility established in September 2008, which debt stood at approximately $43.2 billion as of March 25, 2009. Additional details of the actions authorized by the Federal Reserve in connection with the March restructuring are available in the report filed by the Federal Reserve Board with Congress on March 9, 2009, under section 129 of the EESA.  

i. Automotive Industry Financing Program

The Treasury established the Automotive Industry Financing Program (“AIFP”) on December 19, 2009, to prevent a significant disruption to the American automotive industry. Such a disruption could pose a risk to financial market stability and have a serious negative effect on the real economy of the United States. The program requires, among other things, that participating companies implement a plan to achieve long-term viability. Participating companies also must adhere to rigorous executive compensation standards and other measures to protect the taxpayers’ interests, including limits on the company’s expenditures and other corporate governance requirements.

During the last quarterly period, Treasury provided or committed to provide GM and Chrysler $13.4 billion and $4 billion of loans under the AIFP to prevent the disorderly bankruptcy of the companies. The terms of the loan agreements require that each company develop and submit to the U.S. government a restructuring plan and take other actions designed to assist each company in achieving and sustaining long-term viability, international competitiveness, and improved energy efficiency.

On February 17, 2009, GM and Chrysler submitted their restructuring plans. The Presidential Task Force on the Auto Industry (“Auto Task Force”) established by Treasury and the National Economic Council reviewed these restructuring plans and on March 30, 2009, determined that the plans would not result in long-term viability. For

---


35 Additional information on the eligibility standards for the AIFP are available at: [http://www.financialstability.gov/roadtostability/autoprogram.html](http://www.financialstability.gov/roadtostability/autoprogram.html).

36 Treasury provided the $13.4 billion of funding to GM on December 31, 2009. On January 2, 2009, Treasury fully funded the $4 billion loan commitment to Chrysler, which had been announced during the preceding quarter. Additional details on the terms of the assistance provided by the TARP to GM and Chrysler are available at: [http://www.financialstability.gov/roadtostability/autoprogram.html](http://www.financialstability.gov/roadtostability/autoprogram.html).

37 The restructuring reports are available at: [http://www.financialstability.gov/roadtostability/autoprogram.html](http://www.financialstability.gov/roadtostability/autoprogram.html).
GM, the Auto Task Force determined that a path to viability for the company was possible only through a more significant operational and financial restructuring. The Auto Task Force set a deadline for GM to complete this restructuring by June 1, 2009. The Treasury has agreed to provide GM additional funding for continued operations until that date. For Chrysler, the Auto Task Force determined that a path to viability for the Company was possible only through a partnership or alliance with another large automotive manufacturer, with the most likely alliance partner being Fiat, S.p.A., a European automobile manufacturer. The Auto Task Force set a deadline of May 1, 2009, for Chrysler to enter into a binding deal with Fiat or another partner and submit a viable business plan for the alliance. The Treasury has agreed to provide additional funding to Chrysler for continued operations until that date.

In addition to these actions, on January 16, 2009, Treasury made a $1.5 billion loan to a special purpose entity created by Chrysler Financial to finance the extension of new consumer auto loans as part of a broader program to assist the domestic automotive industry in becoming financially viable. Under the terms of this loan, which the Oversight Board reviewed and considered, the loan will have a five year term and will pay interest at a rate of one month LIBOR plus 100 basis points for the first year and one month LIBOR plus 150 basis points for years two to five. Treasury’s loan will be secured by a senior secured interest in a pool of newly originated consumer automotive loans, and Chrysler will serve as a guarantor for certain covenants of Chrysler Financial.

Under the agreement Chrysler Financial must be in compliance with the executive compensation and corporate governance requirements of Section 111 of EESA, as well as enhanced restrictions on executive compensation. The special purpose entity created by Chrysler Financial will issue warrants to Treasury in the form of additional notes in an amount equal to 5 percent of the total size of the loan. The additional notes will vest 20 percent on the closing date and 20 percent on each anniversary of the closing date and will have other terms similar to the loan.38

j. **Auto Supplier Support Program**

Since the onset of severe dislocation in the credit markets during October 2008, and due to the recent decline in auto sales, many auto parts suppliers have been unable to access credit on reasonable terms and are facing growing uncertainty about the prospects for their businesses. On March 19, 2009, Treasury announced the Auto Supplier Support Program ("ASSP"), under which Treasury will allocate $5 billion under the TARP to provide qualified automotive supply companies with financial protection on the receivables owed to these companies by domestic auto manufacturers, and to provide auto supply companies with immediate access to liquidity, thus giving domestic auto manufacturers reliable access to the parts they need.

---

38 Additional details on the agreement between TARP and Chrysler are available at: [http://www.financialstability.gov/roadtostability/autoprogram.html](http://www.financialstability.gov/roadtostability/autoprogram.html).
Although the ASSP is open to all domestic auto manufacturers, only GM and Chrysler have decided to participate in the program as of March 31, 2009, and these companies are presently working to establish operational purchase programs. Decisions about which auto parts suppliers are eligible for the program and which receivables are eligible to receive protection will be made by the participating auto manufacturer. However, all receivables financed under the program must have been created after March 19, 2009, and must be made on qualifying commercial terms between the auto parts supplier and the participating auto manufacturer. Once approved by the auto manufacturer, the eligible auto parts supplier will be able to receive the protection on their receivables by selling them to a special purpose vehicle formed and initially capitalized by the auto manufacturer that has financing from Treasury. The sale of the receivables will be discounted by the appropriate fee for the program, which is slightly higher if the supplier takes advantage of the option to receive immediate liquidity instead of payment at maturity of the receivable.

k. Warranty Commitment Program

On March 30, 2009, Treasury announced a Warranty Commitment Program designed to give consumers who are considering new car purchases from domestic manufacturers the confidence that warranties on those cars will be honored regardless of the outcome of the current restructuring process. The program will cover all warranties on new vehicles purchased from participating auto manufacturers during the finite period in which those manufacturers are restructuring. Both GM and Chrysler have agreed to participate, and each is presently working to implement the program.39

Under the program, each participating manufacturer will contribute cash to a separate special purpose company whose sole purpose is to pay covered warranty claims in the event the participating manufacturer is unable to do so. The total amount of cash to be contributed will be equal to 125 percent of the estimated cost of paying for warranty service on the covered vehicles. The manufacturer will contribute 15 percent of the projected cost from its own funds, and Treasury, through TARP, will provide additional funds to cover 110 percent of the projected cost. In the event of a failure of a participating auto manufacturer, Treasury will appoint a program administrator who either will fund covered warranty expenses out of the contributed funds or will, together with Treasury, identify a third party to assume warranty liabilities in exchange for transfer of the assets of the special purpose company, including the contributed funds. It is expected that the contributed funds will cover a 120-day restructuring period in the case of GM and a 90-day restructuring period in the case of Chrysler.

39 Additional details on the agreement between TARP and Chrysler are available at: http://www.financialstability.gov/roadtostability/autoprogram.html.
1. **Executive compensation**

Shortly after passage of the EESA in October 2008, Treasury issued an interim final rule to immediately implement the important provisions of the EESA governing executive compensation at institutions that sell assets to, or receive asset guarantees from, Treasury under the TARP.

On February 4, 2009, Treasury announced a set of new proposed restrictions on executive compensation that would supplement those established in the EESA and implemented by the interim final rule ("Compensation Guidance"). These new restrictions were developed to help ensure that public funds are directed towards the public interest – by strengthening the economy and stabilizing the U.S. financial system – and not toward inappropriate private gain. In addition, the new proposed measures were designed to ensure that the compensation of top executives at financial institutions receiving assistance under the TARP is properly aligned with the interests of shareholders and the long-term health of the financial institution, as well as with the interests of taxpayers. Importantly, these proposed measures also sought to strike a balance between, on the one hand, the need for controls on executive pay at financial institutions receiving assistance under the TARP and, on the other hand, the need for such financial institutions to fully function and attract and retain qualified management and staff in order to continue providing credit and other services to consumers and businesses, promote financial recovery and stability, and maximize the chances of taxpayers being paid back on their investments.

The proposed Compensation Guidance would subject all financial institutions receiving assistance under the TARP to new reporting and recordkeeping requirements. For example, the chief executive officers of such institutions would be required to certify annually the institution’s compliance with all executive compensation restrictions imposed by the EESA, Treasury rules or guidelines, or under the contractual terms of their agreement with Treasury. In addition, the Compensation Guidance would require the compensation committees of financial institutions receiving assistance to provide a narrative disclosure on how senior executive officer ("SEO") compensation arrangements do not encourage excessive and unnecessary risk-taking.

The proposed Compensation Guidance also imposed additional, but varying, limits on firms that participate in generally available capital access programs under the TARP (such as the CAP), and those that receive exceptional assistance in individually negotiated transactions (such as the transactions entered into under the TIP and AGP). These provisions would apply only to programs announced after February 4, 2009. For institutions participating in an exceptional assistance program under the TARP after such date, the proposed Compensation Guidance:

1. Limits the compensation of senior executives to $500,000, and requires that any additional pay be in the form of restricted stock or other similar long-term incentive arrangements;
(2) Requires the vesting schedule of this restricted stock be based on factors that include the degree to which the institution has met its government repayment obligations, protected the interests of taxpayers, and met lending and stability standards;

(3) Mandates full disclosure of executive compensation structure and strategy and a non-binding shareholder resolution on this disclosure;

(4) Requires institutions to implement provisions allowing the "clawback" of bonuses and incentive compensation awarded to –

(i) SEOs, if such compensation or bonuses are based on materially inaccurate financial statements or performance metrics; or

(ii) any of the next twenty executive officers, if such compensation or bonuses were based on materially inaccurate financial statements or performance metrics and if the executive officer knowingly engaged in providing inaccurate information relating to the financial statements or performance metrics used to calculate their incentive pay;

(5) Prohibits the institution from making any golden parachute payments to its SEOs and the next five executive officers;

(6) Prohibits the institution from making any golden parachute payment greater than one year’s compensation to any of the institution’s next twenty-five executive officers; and

(7) Requires the board of directors of the institution to adopt a luxury expenditures policy.

For institutions participating in a generally available capital access program under the TARP announced after February 4, 2009, the proposed Compensation Guidance:

(1) Limits SEO compensation to $500,000, and requires that any additional pay be provided in the form of restricted stock or other similar long-term incentive arrangements carrying the same restrictions as for entities participating in an exceptional assistance program, unless SEO compensation is subject to a non-binding shareholder resolution;

(2) Requires the institution to implement provisions to “clawback” bonuses and incentive compensation awarded to the institution’s –

(i) SEOs that are based on materially inaccurate financial statements or performance metrics; or
(ii) next twenty executive officers if such compensation or bonus was based on materially inaccurate financial statements or performance metrics and if the executive officer knowingly engaged in providing inaccurate information relating to the financial statements or performance metrics used to calculate compensation;

(3) Prohibits the institution from making any golden parachute payments greater than one year’s compensation to the institution’s SEOs; and

(4) Requires the institution’s board of directors to adopt a luxury expenditures policy.

Shortly after the announcement of these proposed new executive compensation restrictions, Congress passed and President Obama signed into law the ARRA. In light of the enactment of these amendments, as of March 31, 2009, the proposed Compensation Guidelines had not been implemented for any new program and Treasury was continuing to work towards the development of rules to implement the executive compensation provisions of the ARRA and the Compensation Guidance, as appropriate. Title VII of Division B of the ARRA amended the executive compensation provisions in the EESA that apply to recipients of financial assistance under the TARP. These amendments require Treasury to establish new executive compensation and other standards, which must include:

(1) A limitation on claims for federal income tax deduction of compensation for SEOs;

(2) A limitation on compensation that excludes incentives for SEOs to take unnecessary and excessive risks that threaten the value of the TARP recipient;

(3) A provision for the recovery of any bonus, retention award, or incentive compensation paid to a SEO or the next 20 most highly compensated employees based on materially inaccurate statements of earnings, revenues, gains, or other criteria;

(4) A prohibition on any golden parachute payment to a SEO or any of the next five most highly compensated employees;

(5) A limitation the payment or accrual of any bonus, retention award, or incentive compensation to certain highly compensated employees and/or SEOs;
(6) A prohibition on any compensation plan that would encourage earnings manipulation at the TARP recipient in order to enhance an employee’s compensation;

(7) A requirement that each TARP recipient establish a compensation committee of independent directors to meet semi-annually to review compensation plans and the risks posed by these plans to the TARP recipient;

(8) The adoption of a luxury and excessive expenditures policy; submission of non-binding shareholder resolution on SEO compensation; and

(9) A certification of the TARP recipient’s compliance with these standards by the chief executive officer and chief financial officer for each TARP recipient.

m. Administrative Activities of the Office of Financial Stability

The Oversight Board has continued to review and monitor the progress made by Treasury’s Office of Financial Stability (“OFS”) in hiring staff and establishing the necessary infrastructure, internal controls and compliance and monitoring programs for the TARP. The OFS is charged with designing and implementing all programs established under the EESA. The following highlights some of the important developments and actions taken by Treasury in these areas during the quarterly period. In overseeing the administrative activities of the OFS, the Oversight Board has taken into account the activities of the GAO and SIGTARP and recommendations of the GAO and SIGTARP with respect to these matters. In this regard, the Oversight Board notes that the GAO recently concluded that Treasury had taken steps to address several previous recommendations of the GAO relating to staffing, contracting, monitoring and the development of an internal control framework.40 Treasury’s progress in this area is particularly noteworthy, as it has simultaneously established a new department while simultaneously developing and implementing programs to address the financial crisis under the TARP.

i. Staffing

During the quarterly period, OFS continued to make considerable progress in building up its staff. As of March 16, 2009, the number of OFS staff increased had to 113 employees. The number and percentage of permanent staff increased significantly during the period, with permanent staff comprising 77 of the 113 employees as of March 16, 2009, and the remaining 36 employees being detailees from other offices of Treasury or other federal agencies. Treasury expects to increase overall staffing levels

40 See GAO, Troubled Asset Relief Program: March 2009 Status of Efforts to Address Transparency and Accountability Issues, GAO-09-504 (March 2009).
for OFS to approximately 195 full-time employees, and is developing a formal Workforce Plan that balances the need for high performing, long-term personnel with the temporary nature of TARP and, potentially, the OFS. Under the plan, Treasury has created a bimonthly review process to address competencies, staffing needs, gaps, and changes in program direction.

ii. Procurement

During the quarterly period, Treasury continued to engage private sector firms to assist with the significant volume of legal and transactional work associated with the TARP. The firms of Squire, Sanders & Dempsey LLP and Hughes Hubbard & Reed LLP continued to furnish legal services in support of the CPP. The firm Sonnenschein Nath & Rosenthal continued to furnish legal services in support of the TALF and in support of auto industry loans. Ennis Knupp & Associates continues to provide Treasury with investment and advisory services, including consultation regarding executive compensation. Pricewaterhouse Coopers, LLP continues to support Treasury’s internal control processes, Ernst & Young, LLP provides accounting services, and Lindholm & Associates continues to furnish human resources support services. The Bank of New York Mellon continues to serve as Treasury’s custodian for the securities acquired by Treasury under the TARP.

In addition, during the quarterly period, Treasury engaged several private sector firms to assist with the design and implementation of new and evolving initiatives under the TARP. In January 2009, Treasury retained Cadwalader, Wickersham and Taft LLP to provide bankruptcy-related legal services. In February, Treasury retained Locke, Lord, Bisell & Liddell LLP to support expansion of the CPP to include S-Corporations; retained Simpson, Thatcher & Bartlet LLP to support the CAP, the additional TIP investment in Citigroup, and the development of the PPIP program; and retained Venable LLP to perform a variety of legal services in support of Treasury’s efforts to make the CPP available to institutions organized in mutual form and to advise Treasury regarding the Auto Supplier Support Program. In addition, in February, Treasury hired Pat Taylor and Associates to provide program support services for OFS, including document support services and assistance with requests for information under the Freedom of Information Act. The Treasury also entered into financial agency agreements with Fannie Mae and Freddie Mac to support the Home Affordable loan modification program.

In March, Treasury retained the firms of Haynes and Boone LLP to provide legal services in connection with the Auto Industry Financing Program. Treasury also retained the firm Cadwalader, Wickersham & Taft LLP to provide bankruptcy analysis in support of investments in the automobile industry, the firm Sonneschein Nath & Rosenthal to provide legal services related to the auto industry loan and warranty programs, and the firm McKee Nelson LLP to provide legal services related to the Small Business Initiative. In addition, Treasury retained The Boston Consulting Group to provide consulting and advisory services relating to the AIFP, and the firm FI Consulting to provide support relating to credit reform modeling and analysis. Also in March, Treasury entered into a
financial agency agreement with Earnest Partners, an independent investment manager, to assist with the Unlocking Credit for Small Businesses program.

The OFS implemented several key procurement-related initiatives and activities during the reporting period. In February, the OFS hired a Contract Administration Manager to apply contract management best practices to TARP contracts and financial agency agreements, and provide leadership and guidance to Contracting Officer Technical Representatives ("COTRs") and financial agent managers. The OFS implemented a Contract and Agreement Review Board comprised of program executives to monitor contracts and financial agency agreements to ensure sufficient and effective planning, administration, and management. The OFS implemented a COTR Roundtable, developed targeted COTR Training, and invited contracting experts from across the federal government to brief COTRs and OFS Staff on lessons learned and contracting best practices.

On October 6, 2008, Treasury published interim final regulations designed to address actual or potential conflicts of interest among contractors performing services in conjunction with the TARP. These regulations describe, among other things, the formal steps for identifying, monitoring, and mitigating conflicts of interest during the procurement process and over the contract’s term. As the comment period for the interim final rule ended on March 23, 2009, Treasury currently is analyzing the rule in light of the comments received and will amend the rule as appropriate after such review is completed.

Conflicts issues that arise with new and existing contracts and financial agency agreements are principally handled through the OFS Compliance Office. When a potential conflict does arise in an existing contract, the Compliance Office takes a standard approach to evaluating the potential conflict and feasibility of mitigation measures. During the quarterly period, the Compliance Office reviewed all of the existing contracts and financial agency agreements Treasury entered into that pre-date the interim final rule. OFS identified six contracts that required renegotiation to bring them into conformity with the interim final rule on conflicts of interest. As of April 6, 2009, this process resulted in renegotiation of two contractor mitigation plans with the remaining four mitigation plans in the process of renegotiation. It is anticipated that the remaining four mitigation plans will be completed within the next few months coinciding with the finalization of the rule. Treasury also is in the process of formalizing procedures to monitor conflicts of interest with contractors and financial agents.

### iii. Reporting

Besides the initiatives discussed earlier in this report that Treasury has taken to increase the level and quality of information provided the public concerning actions taken under the EESA Treasury also discloses information relating to the objectives, structure, and terms of each TARP program and investment on its website and through a series of publicly available reports. As of March 31, 2009, Treasury had filed –
- 25 transaction reports, in accordance with section 114 of the EESA, which include key details of the acquisition and, as of March 31, 2009, the disposition of TARP investments;

- 5 tranche reports, in accordance with section 105(b) of the EESA, which outline the details of transactions that relate to each $50 billion incremental investment made under the TARP, along with the pricing mechanism for each relevant transaction, a description of the challenges that remain in the financial system, and an estimate of the additional actions that may be necessary to address such challenges; and

- 5 monthly reports, in accordance with section 105(c) of the EESA and, describing among other things, financial data concerning administrative expenses, projected administrative expenses and a detailed financial statement with respect to TARP investments.

Treasury has met each of its reporting requirements under the EESA on time. In addition to these reports, Treasury continues to make available information concerning the objectives and terms of programs established under the TARP and recent and upcoming initiatives through numerous press releases, testimonies and speeches.

   i.  Governance and Internal Controls

During the quarterly period, Treasury has made progress in the area of governance and taken steps to build a system of internal controls. For example, Treasury has formed two governance committees to discuss and prioritize internal control objectives and provide oversight of Treasury's internal control program. The first governance committee is the Executive Committee (“EC”), which serves as the primary management vehicle for OFS and provides a link via the Assistant Secretary for Financial Stability between the Treasury and OFS policy makers and the operational capabilities within OFS. The second committee is the Senior Assessment Team (“SAT”), which is designed to assist OFS in meeting its statutory and regulatory requirements. Treasury also has formed a New Program Implementation Team (“NPIT”) to support the implementation of new TARP programs and facilitate communication and internal controls. This cross functional team serve as a bridge between the governance committee structure of the EC and the SAT as well as the business and support functions that perform the control activities on a daily basis. PricewaterhouseCoopers and Ernst & Young continue to support Treasury in the design of Treasury’s internal controls framework.

In addition, the internal controls program office within OFS has taken steps to review and improve the controls Treasury has established for the TARP. For example, the internal controls program office has begun an internal OMB Circular A-123 assessment for Fiscal Year 2009, which is designed to assess the adequacy of
management controls established for the various TARP programs, identify needed improvements to these controls, and guide OFS in taking any corresponding corrective action that may be needed to ensure the effective functioning of the TARP. The results of this assessment will be reported through an Annual Assurance Statement, which will be signed by the Assistant Secretary for Financial Stability. The internal controls program office also is in the process of planning an assessment of information technology controls within OFS, and is working with the Bank of New York Mellon to define the requirements of this assessment. These efforts demonstrate OFS’s commitment to meeting Treasury and other federal requirements for a sustainable and effective system of internal controls.
APPENDIX A

Minutes of Financial Stability Oversight Board Meetings
During the Quarterly Period
Minutes of the Financial Stability Oversight Board Meeting
January 8, 2009

A meeting of the Financial Stability Oversight Board ("Board") was held at 4:15 p.m. (EST) on Thursday, January 8, 2009, at the offices of the Department of the Treasury ("Treasury").

MEMBERS PRESENT:

Mr. Bernanke, Chairperson
Mr. Paulson
Mr. Cox
Mr. Preston
Mr. Lockhart

STAFF PRESENT:

Mr. Treacy, Executive Director
Mr. Fallon, General Counsel
Mr. Gonzalez, Secretary

AGENCY OFFICIALS PRESENT:

Mr. Kashkari, Interim Assistant Secretary of the Treasury for Financial Stability and Assistant Secretary of the Treasury for International Economics and Development
Mr. Hoyt, General Counsel, Department of the Treasury
Mr. Albrecht, Counselor to the General Counsel, Department of the Treasury
Mr. Lambright, Chief Investment Officer, Office of Financial Stability, Department of the Treasury
Mr. Morse, Chief Counsel, Office of Financial Stability, Department of the Treasury
Mr. Wolfteich, Chief Compliance Officer, Office of Financial Stability, Department of the Treasury
Mr. Alvarez, General Counsel, Board of Governors of the Federal Reserve System
Ms. Liang, Associate Director, Division of Research & Statistics, Board of Governors of the Federal Reserve System
Mr. Slifman, Senior Associate Director, Division of Research & Statistics, Board of Governors of the Federal Reserve System
Mr. Scott, Senior Advisor to the Chairman, Securities and Exchange Commission
Mr. Vollmer, Deputy General Counsel, Securities and Exchange Commission
Mr. Montgomery, Assistant Secretary for Housing and Commissioner of the Federal Housing Administration, Department of Housing and Urban Development
Mr. Borchert, Senior Advisor to the Secretary of the Department of Housing and Urban Development
Mr. DeMarco, Chief Operating Officer and Deputy Director for Housing Mission and Goals, Federal Housing Finance Agency
GUESTS PRESENT:

Mr. Barofsky, Special Inspector General, Troubled Asset Relief Program

Mr. Puvalowski, Chief of Staff, Office of the Special Inspector General, Troubled Asset Relief Program

Chairperson Bernanke called the meeting to order at approximately 4:15 p.m. (EST).

At the invitation of the Board, Mr. Barofsky and Mr. Puvalowski from the Office of the Special Inspector General (“OSIG”) for the Troubled Asset Relief Program (“TARP”) joined the meeting. Mr. Barofsky briefed the Board concerning the mission and operations of the OSIG, including the recent actions taken by the OSIG in furtherance of the OSIC’s three principal areas of focus: coordination, transparency, and oversight. Members and Mr. Barofsky also discussed ways of coordinating the activities of the Board and OSIC, interactions between OSIC and Treasury and the Office of Financial Stability, and methods of coordinating the roles and activities of the General Accountability Office (“GAO”) and the Congressional Oversight Panel (“COP”). Members and Mr. Barofsky also discussed how the OSIG could use its investigative and other powers most effectively to prevent fraud by contractors or institutions that receive TARP funds. Following this briefing and discussion, Mr. Barofsky and Mr. Puvalowski departed.

The Board then considered the minutes for the meeting of the Board held on December 19, 2008. After discussion of the minutes and potential modifications thereto, the Members agreed to circulate the minutes for approval by notation vote.

Members then received a briefing from, and engaged in a discussion with, Treasury officials concerning the programs, policies and financial commitments of the TARP. Members and officials discussed, among other things, the manner in which the terms and conditions of the TARP’s programs and investments had been tailored to the specific objectives, nature and circumstances of the program or investment, the current level of funding committed to TARP programs, the resources currently available to the TARP, and the controls that Treasury has established to monitor the amount of TARP funds requested and disbursed.

As part of this discussion, officials from the Treasury provided the Board with an update on the capital purchase program (“CPP”). Officials and Members reviewed and discussed, among other things, the number of applications received and approved by Treasury under the CPP, recently closed transactions, and the steps that Treasury has taken to promote transparency, including by publicly disclosing the standard forms of agreements for CPP transactions.

Treasury officials then provided a briefing on the Targeted Investment Program (“TIP”) recently established under the TARP to foster financial market stability and thereby strengthen the economy and protect American jobs, savings, and retirement security. Members and officials discussed, among other things, the guidelines and eligibility requirements for the program and the recent actions taken under the TIP to provide financial assistance to Citigroup,
Inc. (“Citigroup”) through the purchase of an additional $20 billion in preferred stock. In addition, officials and Members reviewed the dividends payable on the preferred stock, the warrants that would be received by TARP in connection therewith, and the additional executive compensation, lobbying and corporate expense limitations applicable to Citigroup under the program.

Treasury officials then provided a briefing on the Asset Guarantee Program (“AGP”) recently established under the TARP to promote financial stability by guaranteeing certain assets, in accordance with section 102 of the Emergency Economic Stabilization Act (“EESA”), held by systemically significant financial institutions that face a high risk of losing market confidence due to a portfolio of distressed assets. Members and officials reviewed and discussed, among other things, the principal terms of the program and the recent actions taken by the Treasury, in conjunction with the Federal Deposit Insurance Corporation (“FDIC”) and the Federal Reserve, to provide Citigroup with protection against the possibility of unusually large losses on a designated pool of approximately $306 billion in assets. In addition, Members and officials discussed the efforts by Treasury, its financial advisers and the Federal Reserve and FDIC to finalize the structure of the program and the asset pool that will be guaranteed, and the potential timeline for consummating the arrangements.

Treasury officials then provided a briefing on the Automotive Industry Financing Program (“AIFP”) recently established by the Treasury to promote financial stability by preventing significant disruption in the automotive industry. Members and officials reviewed and discussed, among other things, the terms and eligibility requirements under the program, the recent actions taken by the Treasury under the AIFP to provide financial assistance to General Motors Corp. (“GM”), Chrysler Holding LLC (“Chrysler”) and GMAC LLC (“GMAC”), and the standards for reviewing requests from the automotive or other industries for assistance under the TARP. Treasury officials reported, among other things, that the TARP had fully funded the $4 billion loan to Chrysler and the first $4 billion of the $13.4 billion facility established for GM. Members and officials also discussed the objectives, structure and timing of TARP’s purchase of $5 billion in senior preferred equity with an 8 percent dividend from GMAC and an additional loan of up to $1 billion to GM in support of GMAC’s reorganization as a bank holding company. Members and officials also reviewed the collateral for the loan of up to $1 billion to GM, which will be secured by the GMAC equity acquired by GM in the rights offering that GMAC will conduct, and which will be exchangeable at any time, at Treasury's option, for the GMAC equity acquired. In addition, the terms of the loan require that GM abide by substantially the same terms and conditions that apply under the $13.4 billion loan facility, including the provisions restricting executive compensation and requiring GM to provide the OSIG with access to corporate books and records. Members and officials also discussed the financial and other challenges facing the auto companies, and the certification that the President’s Designee is required to make, within 30 days of March 31, 2009, under the terms of the loan agreements regarding the efforts of the auto
companies to achieve and sustain long-term viability, international competitiveness and energy efficiency in accordance with the restructuring plan that each company must submit.

Members and officials also considered potential future liquidity and funding needs of the domestic auto-related companies and other institutions, and the ways that additional TARP resources could most effectively be used to achieve the objectives of the EESA. Members and officials also reviewed and discussed staffing and continuity of operations within the Office of Financial Stability. During the discussion, Mr. Paulson noted that Mr. Kashkari and Mr. Lambright had been asked to serve in their current capacities on a temporary basis to facilitate the transition that will occur following the inauguration of President-elect Obama.

Members and officials then engaged in a discussion regarding the first quarterly report to Congress that will be issued by the Board pursuant to section 104(g) of the EESA. As part of this discussion, officials from the Board provided an update on the progress of the report.

The meeting was adjourned at approximately 5:12 p.m. (EST).

[Electronically Signed]

_______________________________
Jason A. Gonzalez
Secretary
Minutes of the Financial Stability Oversight Board Meeting  
January 15, 2009

A meeting of the Financial Stability Oversight Board (“Board”) was held telephonically on Thursday, January 15, 2009, at 4:30 p.m. (EST).

MEMBERS PARTICIPATING:

Mr. Bernanke, Chairperson  
Mr. Paulson  
Mr. Cox  
Mr. Preston  
Mr. Lockhart

STAFF PARTICIPATING:

Mr. Treacy, Executive Director  
Mr. Fallon, General Counsel  
Mr. Gonzalez, Secretary

AGENCY OFFICIALS PARTICIPATING:

Mr. Kashkari, Interim Assistant Secretary of the Treasury for Financial Stability and Assistant Secretary of the Treasury for International Economics and Development  
Mr. Hoyt, General Counsel, Department of the Treasury  
Mr. Lambright, Chief Investment Officer, Office of Financial Stability, Department of the Treasury  
Mr. Wolfteich, Chief Compliance Officer, Office of Financial Stability, Department of the Treasury  
Mr. Cartwright, General Counsel, Securities & Exchange Commission

Mr. Scott, Senior Advisor to the Chairman, Securities and Exchange Commission

Mr. Borchert, Senior Advisor to the Secretary of the Department of Housing and Urban Development

Mr. DeMarco, Chief Operating Officer and Deputy Director for Housing Mission and Goals, Federal Housing Finance Agency

Ms. Anna Lee Hewko, Senior Project Manager, Division of Supervision and Regulation, Board of Governors of the Federal Reserve System

Chairperson Bernanke called the meeting to order at approximately 4:35 p.m. (EST).

The Members first discussed the Board’s report to Congress for the quarterly period ending December 31, 2008, pursuant to section 104(g) of the Emergency Economic Stabilization Act.

Officials from the United States Department of the Treasury (“Treasury”) briefed the Members regarding the package of capital purchases, loss-sharing guarantees and liquidity access that the Treasury, Federal Deposit Insurance Corporation (“FDIC”), and Federal Reserve proposed to provide Bank of America Corporation (“Bank of America”), which acquired Merrill Lynch & Co., Inc. on January 1, 2009. Members and officials reviewed and discussed, among other things, the principal terms of

1 Only participated in a portion of the meeting.
the investment to be made by the Treasury under the Targeted Investment Program in Bank of America as part of this package of supports, including, among other things, the dividend rate on the $20 billion in preferred stock that Treasury will acquire, associated warrants, and the dividend and executive compensation limits that would apply to Bank of America under the terms of the transaction. In addition, members and officials reviewed and discussed the principal terms and structure of the loss-sharing protections to be provided by the Treasury and the FDIC to Bank of America with respect to a designated pool of more than $110 billion in assets, including the projected composition and size of the asset pool, the timeframe and process for assessing the value and projected losses on the assets, and the preferred equity that would be received in consideration for these guarantees.2

Treasury officials also provided a briefing on the Automotive Industry Financing Program (“AIFP”) and recent actions taken by the Treasury under the program. Members and officials reviewed and discussed, among other things, the timing of the second tranche of funding for General Motors Corporation (“GM”) under the existing $13.4 billion senior loan agreement and of the loan of up to $1 billion to GM for the purchase of equity of GMAC LLC (“GMAC”) as part of the rights offering to be conducted by GMAC in connection with its reorganization as a bank holding company.

Treasury officials and Members also reviewed and discussed a $1.5 billion senior secured loan that Treasury expected to provide to Chrysler Financial LLC (“Chrysler Financial”) under the AIFP. Members and officials discussed, among other things, the purpose, structure and timing of the facility, the interest rate and term of the loan, and the executive compensation and corporate expense restrictions that will apply to the company as part of the transaction.

Treasury officials also provided an update on the recent actions taken with respect to the loss-protection guarantee provided to Citigroup, Inc. (“Citigroup”) by the Treasury and FDIC with respect to a designated pool of more than $300 billion of assets. Members and officials discussed, among other things, the date Treasury expected to make the guarantee operational, the composition of the assets in the designated pool, and the monitoring of the pool that Treasury expected to conduct in conjunction with its financial advisers.

Members and officials also reviewed the existing financial commitments of the TARP, and the level of uncommitted resources that remained available to the Treasury under the TARP.

The meeting was adjourned at approximately 5:30 p.m. (EST).

[Electronically Signed]

__________________________________________________________
Jason A. Gonzalez
Secretary

---

2 Mr. Scott then joined the meeting.
Minutes of the Financial Stability Oversight Board Meeting
February 25, 2009

A meeting of the Financial Stability Oversight Board (“Board”) was held at 4:15 p.m. (EST) on Wednesday, February 25, 2009, at the offices of the Department of the Treasury (“Treasury”).

MEMBERS PRESENT:

Mr. Bernanke, Chairperson
Mr. Donovan
Ms. Schapiro
Mr. Lockhart

STAFF PRESENT:

Mr. Treacy, Executive Director
Mr. Fallon, General Counsel
Mr. Gonzalez, Secretary

AGENCY OFFICIALS PRESENT:

Mr. Kashkari, Interim Assistant Secretary of the Treasury for Financial Stability and Assistant Secretary of the Treasury for International Economics and Development
Ms. Abdelrazek, Senior Advisor to the Assistant Secretary for Financial Stability and International Economics, Department of the Treasury
Mr. Albrecht, Counselor to the General Counsel, Department of the Treasury
Mr. Lambright, Chief Investment Officer, Office of Financial Stability, Department of the Treasury
Mr. Wolfteich, Chief Compliance Officer, Office of Financial Stability, Department of the Treasury
Ms. Liang, Associate Director, Division of Research & Statistics, Board of Governors of the Federal Reserve System
Mr. Nelson, Associate Director, Division of Monetary Affairs, Board of Governors of the Federal Reserve System
Mr. Herold, Deputy General Counsel, Department of Housing and Urban Development
Mr. Daly, Assistant General Counsel, Department of Housing and Urban Development
Mr. Apgar, Senior Advisor to the Secretary, Department of Housing and Urban Development
Mr. Becker, General Counsel and Senior Policy Director, Securities and Exchange Commission
Mr. Sirri, Director, Division of Trading and Markets Regulation, Securities and Exchange Commission
Mr. Scott, Senior Advisor to the Chairman, Securities and Exchange Commission
Mr. DeMarco, Chief Operating Officer and Deputy Director for Housing Mission and Goals, Federal Housing Finance Agency
Chairperson Bernanke called the meeting to order at approximately 4:18 p.m. (EST).

In light of the new Members on the Board, Chairperson Bernanke and the other Members of the Board first reviewed the functions of the Board under the Emergency Economic Stabilization Act ("EESA") and the activities undertaken by the Board in fulfillment of these duties. As part of this discussion, Members reviewed the governance and staffing of the Board and the Board’s interaction with, and the roles and responsibilities of, the Special Inspector General, Government Accountability Office, and Congressional Oversight Panel in overseeing the Troubled Asset Relief Program ("TARP").

Using prepared materials, Treasury officials then provided the Members with a briefing on recent TARP-related initiatives and an update concerning other programs recently established under the TARP. The briefing and discussion initially focused on various components of the Financial Stability Plan and the timing and terms of the Capital Assistance Program ("CAP") announced by Treasury on February 25, 2009, which is designed to restore liquidity and stability to the financial system and support lending to creditworthy borrowers.

Treasury officials reviewed and discussed the details of the CAP with the Members, including, among other things, the one-time forward looking assessment or “stress-test” that will be conducted by the Treasury, in conjunction with the appropriate Federal banking agencies, on the 19 largest bank holding companies ("BHCs"), whose risk-weighted assets total at least $100 billion. The purpose of the assessment will be to assess whether these BHCs have the capital necessary to continue lending and to absorb the potential losses that could result from a more severe decline in economic conditions than currently forecasted. Under the terms of the program, participating institutions would have 6-months to raise any additional capital deemed to be needed from private sources, and would also be eligible to obtain such capital under the TARP. The capital available from the TARP would be in the form of convertible preferred shares and could be issued in an amount equal to no less than 1 percent of risk-weighted assets and no more than 2 percent of risk-weighted assets. Institutions could also issue additional convertible preferred shares to Treasury if the proceeds of such additional shares are used to redeem any preferred shares issued under the Capital Purchase Program ("CPP") and, if applicable, the Targeted Investment Program ("TIP"). Any convertible preferred shares acquired by Treasury under the CAP would be convertible to common stock at a 10 percent discount from the institution’s prevailing stock price on February 9, 2009. As required by EESA, Treasury would also receive warrants to purchase up to 20 percent of the convertible preferred amount on the date of the investment. During the discussion, Members and officials discussed the potential for the U.S. government to acquire a substantial percentage of the total outstanding common shares of a participating institution.

Treasury officials then reviewed and discussed the restrictions established under the CAP to protect the interests of taxpayers, including restrictions on
dividends and executive compensation, as well as the additional requirements regarding transparency, accountability and monitoring that would apply under the program. Members and officials also discussed the effort underway by Treasury to establish the terms under which privately held financial institutions could participate in the program.

The briefing and discussion then turned to various components of Treasury’s proposed Homeowner Affordability and Stability Plan announced on February 19, 2009, including the expected objectives, terms and eligibility requirements of the Home Affordable Modification program being developed by Treasury. Officials noted that Treasury expected to commit $50 billion under the TARP to the loan modification program to prevent avoidable foreclosures and help responsible homeowners stay in their homes.

Members and officials noted and discussed, among other things, the importance of establishing clear and consistent guidelines under the program to ensure that servicers can appropriately determine when a default on a mortgage loan might be “reasonably foreseeable” in the absence of a modification.

Under the terms of the program, loan modifications would be available for first-lien loans on owner-occupied properties originated on or before January 1, 2009. Treasury would share, for up to five years, the cost of reducing the monthly payment on qualifying mortgages from a front-end debt-to-income ratio of 38 percent down to a ratio of 31 percent. Treasury officials also described the various incentive payments that Treasury would make under the program to servicers, borrowers and investors. Treasury officials noted that the terms of the programs were being crafted to protect taxpayers to the greatest extent possible, for example, by requiring participating servicers to provide certain documents for verification and compliance reviews.

Members and officials then discussed Treasury’s progress in hiring staff, establishing a system of internal controls, and monitoring contractors and agents for the Office of Financial Stability. As part of this discussion, Treasury officials reviewed and discussed the recent initiative by Treasury to bolster transparency and limit the potential for lobbyist influence in TARP-related decisions. During the discussion, Board officials also reminded the Members and agency staff participating in Board business to be mindful of potential conflicts of interests that may arise with respect to matters coming before the Board and to discuss any questions concerning potential conflicts of interest or other ethical issues with their agency’s ethics officials.

In addition, Members discussed the recent legislative changes to the executive compensation restrictions applicable to TARP recipients resulting from the American Recovery and Reinvestment Act (“ARRA”) and the impact of such changes on TARP programs to restore liquidity and stability to the financial system. During this discussion, Ms. Schapiro noted that the SEC had recently issued guidance relating to the ARRA.

Treasury officials then provided the Members with an update on the
capital purchase program ("CPP"). Treasury officials reviewed and discussed, among other things, the number of applications received and approved by Treasury under the CPP, as well as the amount of funds requested and disbursed. Members and officials also discussed the steps taken by Treasury, in conjunction with the Federal banking agencies, to monitor the use of TARP funds and changes in lending, including Treasury’s efforts to identify such changes through monthly lending and financial intermediation snapshots, which were designed to provide the public with more frequent and more accessible information regarding the lending and other activities of banks receiving TARP funds. Members and officials also discussed the increasing number of CPP applications being withdrawn and the reasons for such withdrawals.

Federal Reserve and Treasury officials then briefed the Members concerning the Term Asset-Backed Securities Lending Facility ("TALF"), which is designed to help market participants meet the credit needs of households and small businesses by providing financing to eligible owners to support the purchase of certain AAA-rated securities backed by newly and recently originated auto loans, credit card loans, student loans, and small business loans guaranteed by the Small Business Administration ("SBA"). Members discussed the important role that securitizations play in the credit markets, the significant reduction in securitization activity in 2008, and the potential role of the TALF in restarting these markets.

Federal Reserve officials briefed the Members on various aspects of the TALF, including the timing and terms of the TALF, the steps taken by the Treasury and the Federal Reserve to protect and minimize risk of loss to the taxpayer, and the potential for future expansion of the facility. During this discussion, Federal Reserve officials noted several revisions to the terms of the TALF, including a reduction in the interest rates and collateral haircuts for loans secured by asset-backed securities guaranteed by the SBA or backed by government-guaranteed student loans due to the minimal credit risk associated with these assets. Federal Reserve officials also noted that the facility was designed to be self-liquidating so that the facility should naturally wind down as financial markets conditions return to normal.

Using written materials, Treasury officials also reviewed and discussed the Automotive Industry Financing Program ("AIFP") and the actions taken under the program to prevent significant disruption in the domestic automotive industry. For example, Members and officials discussed, among other things, the purpose and terms of the financial assistance provided by the Treasury under the AIFP to General Motors Corp. ("GM") and Chrysler Holding LLC ("Chrysler"), and the progress being made by the newly formed Presidential Task Force in evaluating the viability plans that were submitted by GM and Chrysler on February 17, 2009.

Members and officials then provided an update on the status of the financial assistance packages provided by the Treasury, Federal Reserve and the Federal Deposit Insurance Corporation to Citigroup, Inc. and Bank of America Corporation. Members also discussed the potential additional assistance to be
provided to the American International Group, Inc. to help stabilize this systemically significant institution and prevent a disorderly failure, as well as the potential timing and need for a future meeting to review and discuss any such additional supports.

The meeting was adjourned at approximately 5:20 p.m. (EST).

[Electronically Signed]

Jason A. Gonzalez
Secretary
Minutes of the Financial Stability Oversight Board Meeting
March 1, 2009

A meeting of the Financial Stability Oversight Board ("Board") was held telephonically on Sunday, March 1, 2009, at 2:00 p.m. (EST).

MEMBERS PARTICIPATING:

Mr. Bernanke, Chairperson
Mr. Geithner
Mr. Donovan
Ms. Schapiro
Mr. Lockhart

STAFF PARTICIPATING:

Mr. Treacy, Executive Director
Mr. Fallon, General Counsel
Mr. Gonzalez, Secretary

AGENCY OFFICIALS PARTICIPATING:

Mr. Kashkari, Interim Assistant Secretary of the Treasury for Financial Stability and Assistant Secretary of the Treasury for International Economics and Development
Ms. Abdelrazek, Senior Advisor to the Interim Assistant Secretary of the Treasury for Financial Stability and Assistant Secretary of the Treasury for International Economics and Development
Mr. Lambright, Chief Investment Officer, Office of Financial Stability, Department of the Treasury
Mr. Knight, Assistant General Counsel, Department of the Treasury

Mr. Alvarez, General Counsel, Board of Governors of the Federal Reserve System
Mr. Ashton, Deputy General Counsel, Board of Governors of the Federal Reserve System
Mr. Wilcox, Deputy Director, Division of Research & Statistics, Board of Governors of the Federal Reserve System
Ms. Barger, Deputy Director, Division of Banking Supervision and Regulation, Board of Governors of the Federal Reserve System
Mr. Daly, Assistant General Counsel, Department of Housing and Urban Development
Mr. Scott, Senior Advisor to the Chairman, Securities and Exchange Commission
Mr. Becker, General Counsel and Senior Policy Director, Securities and Exchange Commission
Mr. Sirri, Director, Division of Trading and Markets Regulation, Securities and Exchange Commission
Mr. DeMarco, Chief Operating Officer and Deputy Director for Housing Mission and Goals, Federal Housing Finance Agency

Chairperson Bernanke called the meeting to order at approximately 2:05 p.m. (EST).
Using materials provided, officials from the Department of the Treasury ("Treasury") provided a briefing on the recent actions taken by Treasury to promote financial stability by strengthening the capital structure of Citigroup, Inc. ("Citigroup") through the exchange and conversion of certain preferred shares currently held by Treasury under the Troubled Asset Relief Program ("TARP") for other equity securities of Citigroup. Treasury officials noted that the exchange transactions would increase the company’s tangible common equity - a key financial measure - and would not involve any new outlay of TARP funds. During the briefing, Members and officials reviewed and discussed the terms and conditions of Treasury’s participation in the exchange offering announced by Citigroup on February 27, 2009. For example, Treasury officials noted that, as part of the transaction, certain private holders of Citigroup preferred stock would exchange up to $27.5 billion in preferred stock for common stock at $3.25 per share. Treasury officials also noted that Treasury would exchange its securities on terms that were at least as favorable as those offered to private investors.

Under the terms of the exchange, Treasury would convert up to $25 billion of the Citigroup preferred shares Treasury received under the Capital Purchase Program ("CPP") into a new security that will convert on a one-to-one basis to common shares, pending a shareholder vote to amend the Citigroup charter to allow for an increase in the number of authorized common shares. Additionally, Treasury would exchange the $20 billion in Citigroup preferred shares Treasury received under the Targeted Investment Program ("TIP"), as well as the preferred shares Treasury received under the Asset Guarantee Program ("AGP"), for trust preferred shares that would provide greater structural seniority for the taxpayer and would carry the same 8 percent cash dividend rate as the existing preferred shares. Officials also noted that Citigroup would remain eligible to participate in the Capital Assistance Program ("CAP") established by Treasury, and would be undergoing stress-testing as part of the program.

Using materials provided, Chairperson Bernanke, Mr. Geithner and other officials from the Board of Governors of the Federal Reserve System ("Federal Reserve") and Treasury then briefed and discussed with the other Members of the Board certain actions that Treasury and the Federal Reserve expected to announce the following morning to help promote financial stability by restructuring the U.S. government’s financial support to American International Group, Inc. ("AIG"). During the briefing, Members raised and discussed various matters related to AIG, its financial condition, and the terms and conditions of the expected actions.

As part of the briefing, Chairperson Bernanke and other Federal Reserve officials reviewed the steps taken by the Treasury and the Federal Reserve since September 2008 to address the significant liquidity and other pressures facing AIG and to prevent a disorderly failure of this systemically significant firm. Members reviewed and discussed, among other things, the situation at AIG and in the financial markets in September 2008, when U.S. Government assistance was first provided to AIG, the deterioration in the
financial markets in the fourth quarter of 2008, and the impact of such deterioration on AIG. Members also discussed the overall capital structure of AIG and the status of AIG’s global divesture program, including the status of AIG’s efforts to wind down its financial products unit. Members and officials also reviewed and discussed the harm to policyholders, taxpayers, the financial system and the broader economy that would result from a disorderly failure of the company, and the consideration given to these risks in developing the proposed actions.

Using the materials provided, Federal Reserve officials then described the changes that the Federal Reserve expected to announce with respect to the senior revolving credit facility that initially was established for AIG in September 2008. These changes included, among other things, a reduction of the total amount available under the credit facility from $60 billion to $25 billion after the planned restructuring actions, and a modification of the interest rate on the facility through the removal of the existing floor (3.5 percent) on the LIBOR component of the facility’s interest rate. Federal Reserve officials also reviewed with the Members the planned transactions under which the Federal Reserve would accept preferred interests in two special purpose vehicles (“SPVs”) that AIG would create to hold all of the outstanding common stock of American Life Insurance Company (“ALICO”) and American International Assurance Company Ltd. (“AIA”), two insurance subsidiaries of AIG, in return for a reduction in an equivalent amount of AIG’s borrowing under the existing revolving credit facility. Officials explained that ultimate valuation for the preferred stock interests, currently estimated to be approximately $26 billion, will be a percentage of the fair market value of ALICO and AIA determined based on valuations acceptable to the Federal Reserve.

Officials and Members also reviewed other aspects of the proposed restructuring, including the extension of up to approximately $8.5 billion in credit by the Federal Reserve to SPVs established by domestic life insurance subsidiaries of AIG. The SPVs would repay the loans from the net cash flows they receive from designated blocks of existing life insurance policies held by the parent insurance companies. The proceeds of the Federal Reserve’s loan would pay down an equivalent amount of outstanding debt under the revolving credit facility. Officials noted that the amounts lent, the size of the haircuts taken by the Federal Reserve, and other terms of the loans would be determined based on valuations acceptable to the Federal Reserve. Officials also noted that the proposed restructuring would facilitate AIG’s ongoing restructuring and that the revolving credit facility was expected to remain fully secured after the transactions.

Treasury officials then described the proposed actions that Treasury would take, in connection with the actions taken by the Federal Reserve, to improve AIG’s financial leverage and equity capital and facilitate separation of AIG’s non-core businesses. Members and officials reviewed and discussed the equity capital facility that Treasury proposed to create under the TARP for AIG, which would permit AIG to obtain up to $30 billion of new capital as needed over the 5-year life of the facility in exchange for newly-issued non-cumulative preferred stock.
Treasury officials reviewed and discussed the terms of the facility and the steps taken to protect the interests of taxpayers. As required by the Emergency Economic Stabilization Act ("EESA"), Treasury would also receive warrants to purchase AIG common stock as part of the transaction. Treasury officials also explained that, as part of the restructuring, Treasury would exchange the $40 billion of cumulative perpetual preferred shares that Treasury acquired in November 2008, under the Systemically Significant Failing Institutions Program ("SSFI"), for preferred shares with revised terms that more closely resemble common equity. The new terms would provide for non-cumulative dividends and limit AIG’s ability to redeem the preferred stock except with the proceeds from the issuance of equity capital.

Members and officials also discussed the impact of the proposed actions on the amount of funds available under the TARP, and the current allocation of funds by Treasury among TARP programs, including the CPP, and the timing and prospects of additional asset purchases, investments or other actions under the TARP.

The meeting was adjourned at approximately 2:40 p.m. (EST).

[Electronically Signed]

_______________________________
Jason A. Gonzalez
Secretary
Minutes of the Financial Stability Oversight Board Meeting
March 19, 2009

A meeting of the Financial Stability Oversight Board (“Board”) was held at 11:30 a.m. (EDT) on Thursday, March 19, 2009, at the offices of the Department of the Treasury (“Treasury”). Due to unanticipated scheduling demands, the meeting was not called to order by Chairperson Bernanke until approximately 11:45 a.m. (EDT) and was adjourned at 12:00 p.m. (EDT). Accordingly, the Members received an abbreviated briefing from Treasury officials on the recent and expected actions to be taken under the Troubled Assets Relief Program (“TARP”) and agreed to reconvene at a mutually agreeable date and time.

MEMBERS PRESENT:

Mr. Bernanke, Chairperson
Mr. Geithner
Ms. Schapiro
Mr. Lockhart

STAFF PRESENT:

Mr. Treacy, Executive Director
Mr. Fallon, General Counsel
Mr. Gonzalez, Secretary

AGENCY OFFICIALS PARTICIPATING:

Mr. Kashkari, Interim Assistant Secretary of the Treasury for Financial Stability and Assistant Secretary of the Treasury for International Economics and Development

Mr. Albrecht, Counselor to the General Counsel, Department of the Treasury
Mr. Scott, Senior Advisor to the Chairman, Securities and Exchange Commission
Mr. Becker, General Counsel and Senior Policy Director, Securities and Exchange Commission
Mr. Sirri, Director, Division of Trading and Markets Regulation, Securities and Exchange Commission
Mr. DeMarco, Chief Operating Officer and Deputy Director for Housing Mission and Goals, Federal Housing Finance Agency

Treasury officials first provided a briefing on the actions, which Treasury expected to announce that afternoon, to help stabilize and restore credit flows in the automotive industry by establishing an automotive Supplier Support Program (“SSP”). Treasury officials reviewed and discussed the key terms, conditions and eligibility requirements of the SSP, under which Treasury would commit up to $5 billion under the TARP to provide financial protection to qualified automotive supply companies in connection with the receivables arising from the provision of supplies to the domestic automotive manufactures, and potentially take other measures to provide these automotive supply companies with liquidity.

Treasury officials also reviewed and discussed with the Members the key components of the Public-Private
Investment Partnership (“PPIP”) program announced by Treasury on March 23, 2009, which is designed to draw new private capital into the market for legacy assets through the provision of government equity co-investment and public financing. The PPIP is also intended to repair the balance sheets of financial institutions that hold legacy assets, and help restore liquidity to the markets for these assets.

Treasury officials first reviewed and discussed with the Members the general terms, conditions and eligibility requirements of the legacy securities component of the PPIP, under which Treasury would use capital from the TARP to partner with private investors to support the market for certain legacy mortgage- and asset-backed securities originated prior to 2009 with a rating of AAA at origination. Treasury officials explained that Treasury would invest equity capital from the TARP on a dollar-for-dollar basis with participating private investors. In addition, the asset managers, which Treasury would select under the program, would have the ability, if their investment fund structures meet certain guidelines, to subscribe to senior debt for the investment fund from Treasury.

Treasury officials then reviewed and discussed with the Members the key terms, conditions and eligibility requirements of the legacy loans component of the PPIP, under which Treasury and the Federal Deposit Insurance Corporation (“FDIC”) proposed to establish several public-private investment funds to purchase and manage pools of legacy loans and other assets held by U.S. banks and savings associations. Members and officials discussed, among other things, the manner in which the investment funds would be chartered.

Treasury officials also noted that, in conjunction with the legacy securities program, Treasury was working with the Federal Reserve regarding potential expansion of the Term Asset-Backed Securities Loan Facility (“TALF”) to include certain types of legacy assets. Officials noted, among other things, that the agencies were considering whether to expand the facility to include certain non-agency residential mortgage-backed securities that were originally rated AAA, and outstanding commercial mortgage-backed securities and ABS that are rated AAA.

[Electronically Signed]

_________________________________
Jason A. Gonzalez
Secretary