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Congressional Oversight Panel Releases Oversight Report on TARP Repayments and Repurchase of Stock Warrants

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For Immediate Release

So Far Treasury Has Sold Warrants Back at 66 Percent of Panel's Best Estimate of Fair Market Value

WASHINGTON, D.C. – The Congressional Oversight Panel (COP) released its July oversight report today, "TARP Repayments, including Repurchase of Stock Warrants."

In late 2008, the economy faced an exceptional crisis, and Congress created the Troubled Asset Relief Program (TARP) in an effort to stabilize the financial system. When Congress authorized the commitment of \$700 billion to rescue the financial system, it decided that taxpayers should have the opportunity to share in a potential upside if the banks returned to profitability.

The opportunity to profit from TARP investments comes through special securities called warrants. Banks that received financial assistance were required to give the government warrants for the future purchase of some of their common shares. If the value of the bank stock rose above the warrant price, Treasury could make a profit for the taxpayers.

Currently many banks want to exit the TARP program by repaying their financial assistance and repurchasing their warrants from Treasury. Any exit from the TARP system implicates an important policy question: If the banks give up federal support prematurely, will the economy suffer as a result? The Panel discussed this issue in its June report examining whether the stress tests were rigorous enough to test the strength of the banks.

Now that Treasury has decided that some banks can repay, it is the Panel's mandate to determine whether the taxpayer is receiving maximum benefit from TARP. Because the warrants that accompanied TARP assistance represent the only opportunity for the taxpayer to participate directly in the increase in the share prices of banks made possible by public money, the price at which the warrants are sold is critical. To determine whether Treasury is valuing the warrants in a way that maximizes the taxpayers' investment in the financial institutions, the Panel conducted its own detailed technical valuation of the warrants Treasury holds.

The Panel report offers a range of estimates based on high, low, and best estimate assumptions for certain key variables and it compares its estimates with other valuations. The Panel was aided in its valuation efforts by three renowned finance experts, Professor Robert Merton, Professor Daniel Bergstresser and Professor Victoria Ivashina, all of the Harvard Business School. The professors independently reviewed both the mathematical model and the assumptions that were built into the model; they concluded that the Panel's approaches were reasonable and produced reliable estimates.

The Panel first applied its model to the warrant repurchases that Treasury has already approved.

Eleven banks have repurchased their warrants from the Treasury for a total amount that the Panel estimates to be only 66 percent of its best estimate of their value. If the warrants had been sold for the Panel's best estimate of their current market value, taxpayers would have recovered \$10 million more.

Treasury is just beginning its warrant repurchase program. Banks have bought back only a fraction of one percent of all warrants issued, and the prices paid thus far may not be representative of what is to come. The report further analyzes how Treasury is constrained by the provisions of the contracts governing the TARP investments in the banks and recognizes that the Panel's valuations do not include the liquidity discounts and other adjustments contemplated by Treasury. In reaching a judgment with the bank supervisors to allow a particular bank to repay its TARP assistance and in determining the price, time and manner at which it will sell the warrants it holds in that bank, the Panel found that Treasury must balance the public interests in financial stabilization and economic growth. The Panel emphasized it is critical that Treasury make the process – the reason for its decisions, the way it arrives at its figure, and the exit strategy from or future use of TARP – absolutely transparent.

The full report can be found at www.cop.senate.gov. The Panel held a hearing on June 24 with Herbert M. Allison, Jr., Assistant Secretary of the Treasury for Financial Stability that further informed the analysis and findings of this report. Materials from the hearing can be found on the Panel's website.

The Congressional Oversight Panel was created to oversee the expenditure of the Troubled Asset Relief Program (TARP) funds authorized by Congress in the Emergency Economic Stabilization Act of 2008 (EESA) and to provide recommendations on regulatory reform. The Panel members are: Congressman Jeb Hensarling (R-TX), Richard H. Neiman, Superintendent of Banks for the State of New York, Damon Silvers, Associate General Counsel of the AFL-CIO, former U.S. Senator John E. Sununu (R-NH) and Elizabeth Warren, Leo Gottlieb Professor of Law at Harvard Law School.