# FINANCIAL STABILITY OVERSIGHT BOARD QUARTERLY REPORT TO CONGRESS

**For the quarter ending**
**June 30, 2009**

**Submitted pursuant to section 104(g) of the**
**Emergency Economic Stabilization Act of 2008**


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# I. INTRODUCTION

This report constitutes the third 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 March 31, 2009, through the quarter ending June 30, 2009 (the "quarterly period").

The Oversight Board was established by section 104 of the EESA to help oversee the Troubled Asset Relief Program ("TARP") and other emergency authorities and facilities granted to the Secretary of the Treasury ("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").

Through Oversight Board meetings and consultations between the staffs of the agencies represented by each Member of the Oversight Board, the Oversight Board has continued to review and monitor the development and ongoing implementation of the policies and programs under the TARP to restore liquidity and stability to the U.S. financial system.

The Oversight Board believes that Treasury's actions under the EESA continued to provide meaningful support to core financial markets during the second quarter of 2009. The steps that have been taken by Treasury to bolster financial stability, reinforced by other actions taken by the United States and foreign governments to assist financial markets, improved capital positions at larger bank holding companies ("BHCs") and conditions in short-term funding markets and likely had positive effects on bank and nonbank lending activity. The financial system continued to experience significant strains during the second quarter because of the financial crisis and an associated sharp decline in economic activity, which tended to dampen both the demand for and supply of credit. The TARP has been a key stabilizing factor for the financial system and has likely prevented a greater deterioration in the availability of credit to households, businesses, and communities. In particular, the release of the Supervisory Capital Assessment Program ("SCAP") for the nation's 19 largest BHCs has helped improve investors' sentiment towards banking organizations and financial markets more generally. The Oversight Board also believes that actions taken by Treasury under the TARP and under other authorities, together with those taken by the Federal Reserve, continued to aid the housing market and mortgage borrowers during the period by further relieving strains in the functioning of credit markets and aggressively supporting the demand for mortgage-backed securities ("MBS").

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 3 times during the quarterly period, specifically on April 6, May 28, and June 25, 2009. During these meetings, Members focused attention on the significant actions taken by Treasury to establish, expand, or enhance programs under the TARP and the Financial Stability Plan ("FSP"). As reflected in the minutes of the Oversight Board's meetings,[1] the Oversight Board received presentations and briefings from Treasury officials and, where appropriate, other government officials, including officials from the other agencies represented by the Members of the Oversight Board, concerning recent developments with respect to these initiatives. For example, as reflected in the minutes of the May 28, 2009, meeting, Steven Rattner, Lead Adviser to the Secretary on the Automotive Industry and Member of the Presidential Task Force on the Auto Industry ("Auto Task Force"), met with and provided the Oversight Board an update on actions taken by Treasury and the Auto Task Force to assist the automotive industry in becoming financially viable, as well as the actions taken by the Treasury under the Automotive Industry Financing Program ("AIFP").

### A. Key Initiatives and Developments

The following highlights some of the key initiatives and actions taken under TARP and the FSP during the quarterly period, which were reviewed and discussed by the Oversight Board.

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

- Supervisory Capital Assessment Program and Capital Assistance Program. The Federal Reserve and other Federal banking agencies ("FBAs") completed and released the results of the SCAP, a comprehensive capital assessment exercise designed to ensure that the largest U.S. BHCs have a capital buffer sufficient to withstand losses and sustain lending even in a significantly more adverse economic environment than is currently anticipated. After taking account of potential resources to absorb those losses, supervisors determined that 10 of the 19 institutions participating in the SCAP should collectively

[1] Approved minutes of the Oversight Board's meetings are made available on the internet at http://www.financialstability.gov/about/oversight.html.

add some $75 billion to their capital buffers by November 9, 2009. These 10 firms already have raised more than $34.5 billion of new common equity, with a number of their offerings of common shares being over-subscribed. In addition, these firms already have announced actions that would generate up to an additional $12 billon of common equity and each has submitted capital plans that, if implemented, would provide sufficient capital to meet the required buffer under the assessment's more-adverse scenario. The substantial progress these firms have made in building these capital buffers, and their success in raising private capital, suggest that investors are gaining greater confidence in the banking system.

- Capital Purchase Program. Treasury continued to actively take measures to expand participation by financial institutions of all types and sizes in the Capital Purchase Program ("CPP") as part of its commitment to make capital available to institutions across the country. Notably, in May, Treasury announced the re-opening and expansion of the CPP, with new terms to support small and community banks, and banks and holding companies organized in mutual form. Treasury also continued, on a weekly basis, to approve and fund new investments in financial institutions that had submitted their applications under the original terms of the CPP and were pre-approved by the appropriate FBA. These include small, community, regional, and large banks, as well as Community Development Financial Institutions ("CDFIs"). In addition, Treasury announced the pre-approval of a number of insurance companies that qualified under the original terms of the CPP. As of the close of the quarterly period, Treasury had provided more than $203 billion in capital to 649 institutions in 48 states under the CPP. Moreover, as of June 30, 2009, 32 institutions had repaid approximately $70 billion in principal under the CPP, of which more than $68 billion was received from the10 largest financial institutions participating in the CPP.

- Public-Private Investment Partnership Program. Treasury released additional guidance for potential investors in the securities portion of the Public-Private Investment Partnership ("PPIP") program, extended the deadline for applications by fund managers to the program, and clarified the criteria Treasury will use to evaluate potential participants in the program. The PPIP, which Treasury announced in March 2009, is designed 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.

***Restoring the Flow of Credit to Consumers and Businesses***

- Term Asset-Backed Securities Loan Facility. Treasury and the Federal Reserve significantly expanded the Term Asset-Backed Securities Loan Facility ("TALF") to include as eligible collateral both newly-issued and legacy commercial mortgage-backed securities ("CMBS"), as well as securities backed by insurance premium finance loans. The extension of eligible TALF collateral to include legacy CMBS is intended to promote price discovery and liquidity for legacy CMBS. The resulting improvement in legacy CMBS markets should facilitate the issuance of new CMBS, thereby helping borrowers finance new purchases of commercial properties or refinance existing commercial mortgages on better terms. Likewise, the inclusion of insurance premium finance asset-backed securities ("ABS") as TALF-eligible collateral is expected to continue to facilitate the flow of credit to consumers and small businesses. In the aggregate, more than $23.9 billion in loans had been extended under the TALF, as of June 30, 2009, which has supported the issuance of approximately $32.9 billion of ABS.

***Preventing Avoidable Foreclosures***

- Home Affordable Modification Program. Treasury announced additional details and new program components under the Home Affordable Modification Program ("HAMP"), including –
  - A new program providing incentives to servicers and lenders to facilitate the modification or extinguishment of second lien financing, thereby providing a comprehensive affordability solution for at-risk homeowners;
  - The implementation of foreclosure alternatives for eligible borrowers who are unable to retain their homes through a HAMP modification in order to provide families and servicers alternative incentives to avoid a costly foreclosure process and to minimize the negative impact of foreclosures on borrowers, financial institutions, and communities;
  - A home price decline protection program, which will make up to $10 billion in payments to provide additional incentives to lenders for modifications where home price declines have been the most severe; and

    - A requirement that all participating servicers in HAMP evaluate a borrower's eligibility for refinancing under the HOPE for Homeowners program, which may provide a more attractive solution for certain borrowers and lenders.

***Supporting the Orderly Restructuring of the Domestic Auto Companies***

- Treasury took several key steps under the AIFP during the quarter to assist the domestic automotive industry in becoming financially viable. For example --

    - As agreed to on March 30, 2009, Treasury provided additional working capital to General Motors ("GM") to support the company's effort to develop and implement a more aggressive and viable restructuring plan, and additional working capital to Chrysler Holding ("Chrysler") as it pursued a partnership with Fiat S.p.A. ("Fiat") in order to achieve financial viability.

    - On April 30, 2009, Chrysler announced an alliance with Fiat, which would allow Chrysler to obtain Fiat's technological platform and expertise in exchange for ownership in the company. Chrysler also filed for Chapter 11 bankruptcy protection in order to facilitate the alliance with Fiat and effectively pursue financial viability. Treasury also announced that it would provide up to $3.8 billion in debtor-in-possession financing and up to approximately $6.6 billion in exit financing in connection with this restructuring and to help Chrysler achieve financial viability.

    - On May 21, 2009, Treasury provided $7.5 billion to GMAC LLC ("GMAC") to support GMAC's ability to originate new loans to Chrysler dealers and consumers and to help address GMAC's capital needs as identified through the SCAP.

    - On June 1, 2009, GM filed for Chapter 11 bankruptcy protection in order to pursue the company's restructuring plan. Treasury also announced that it would provide debtor-in-possession financing of up to $30.1 billion to support GM through its bankruptcy proceeding and its efforts to achieve financial viability.

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

### B. Aggregate Level of Commitments, Disbursements and Repayments

As part of its oversight activities, the Oversight Board also reviewed and discussed the aggregate level and distribution of commitments and disbursements under the TARP, repayments of TARP funds, and the level of resources that remain available under the TARP. The chart in Figure 1 summarizes TARP commitments, disbursements and repayments as of June 30, 2009.

Figure 1

**TARP/Financial Stability Plan Budget Table**
(Status as of 6/30/09)

| (*All dollars in billions) | Planned Allocation | Face Value Obligations | Face Value Disbursed/ Outlays[1] |
|---|---|---|---|
| Capital Purchase Program (CPP) | 218.00 | 203.19 | 203.19 |
| Systemically Significant Failing Institutions (SSFI) | 70.00 | 69.84 | 41.15 |
| Targeted Investment Program (TIP) | 40.00 | 40.00 | 40.00 |
| Automotive Industry Financing Program (AIFP)[3] | 82.59 | 84.97 | 54.26 |
| Guarantee Program (Citigroup loss share agmt. w/ USG) | 5.00 | 5.00 | 0.00 |
| Guarantee Program (Bank of America loss share agmt. w/ USG) | 7.50 | 0.00 | 0.00 |
| *Subtotal - - Asset Guarantee Program* | 12.50 | 5.00 | 0.00 |
| Home Affordable Modification Program (HAMP) | 50.00 | 18.66 | 0.00 |
| Consumer & Business Lending Initiative (CBLI) | | | |
| 1) TALF 1.0 | 20.00 | 20.00 | 0.10[2] |
| 2) SBA Securities Purchase | 15.00 | 0.00 | 0.00 |
| 3) TALF Asset Expansion (New Issuance) | 35.00 | 0.00 | 0.00 |
| *Subtotal - - Consumer Business Lending Initiative* | 70.00 | 20.00 | 0.10 |
| Public-Private Investment Program | 100.00 | 0.00 | 0.00 |
| Capital Assistance Program (CAP) | TBD | TBD | TBD |
| Helping Families Save Their Homes Act[4] | 1.26 | 1.26 | 1.26 |
| PROGRAM TOTALS: | 644.35 | 442.92 | 339.96 |
| *Available Funds:* | 55.65 | | |
| *Actual Redemptions / Repayments :* | 70.12 | | |
| *Loan Principal Repaid:* | 0.13 | | |
| *Remainder of $700 billion (total accessible):* | 125.90 | 257.08 | 360.04 |
| *Percentage of $700 billion (total accessible):* | 18% | 37% | 51% |
| *Dividends Received To Date:* | 6.61 | | |
| *Proceeds from the sale of Warrants and Preferred Stock: (received as a result of Exercised Warrants)* | 0.02 | | |

[1] Represents TARP cash that has left the Treasury.
[2] Term Asset Backed Securities Loan Facility (TALF-1): Up to $20B may be disbursed as credit protection for the $200B Federal Reserve Loan Facility. TARP
[3] The face value obligations exceed the expected program usage amount for the AIFP because the final amount expected to be spent out of the Chrysler DIP and Exit financing is expected to be lower than originally obligated.
[4] Reduction of $1.244B in TARP Funds to offset costs of program changes for the Helping Families Save Their Homes Act of 2009, Public Law No: 111-22, Section 202 (b). Funds are not apportioned and an additional $15M is allocated for administrative expenditures relating to the Special Inspector General (SIGTARP) for the Troubled Asset Relief Program.

Note: Redemptions are made under the provisions of the Emergency Economic Stabilization Act of 2008 (EESA) and repayments under the provisions of the American Recovery and Reinvestment Act (ARRA)

### C. Office of Financial Stability and Coordination with Other Oversight Bodies

During the quarterly period, the Oversight Board also monitored Treasury's progress in hiring staff, establishing a system of internal controls, and monitoring contractors and agents for the Office of Financial Stability ("OFS"). As part of this effort, Treasury--

- increased substantially the number of permanent staff in the OFS;
- engaged 5 additional private sector firms to assist with the significant volume of legal and transactional work associated with the TARP;
- published several reports during the quarterly period, which detail the objectives, structure, and terms of each TARP program and investment; and
- continued to put in place the system of internal controls across all program areas.

Members also reviewed the steps taken by Treasury to develop new guidelines that would implement the restrictions on executive compensation applicable to TARP recipients, including those enacted as a result of the American Recovery and Reinvestment Act of 2009 ("ARRA").[2] For example, on June 25, 2009, the Oversight Board met with Kenneth Feinberg, Special Master for TARP Executive Compensation, to review and discuss the standards set forth in Treasury's interim final rule on executive compensation and corporate governance, which Treasury published on June 15, 2009.

As part of its oversight activities, the Oversight Board also has continued to monitor Treasury's effort to assess the lending and intermediation activities of recipients of TARP funds through monthly Lending and Intermediation Snapshots. The Oversight Board also has received periodic updates regarding the work being performed by Treasury, in conjunction with the Federal Reserve and other banking agencies, to develop a more in-depth report and analysis of the lending and intermediation activities of recipients of TARP funds using the comprehensive loan and other data reported quarterly by banks and BHCs.

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"). 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

[2] Pub. L. No. 111-005 (2009).

Board 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."[3] Utilizing this authority, Treasury has implemented or announced an extensive 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 part provides an early evaluation of the effects of Treasury's efforts under EESA, building on the assessment made in the Oversight Board's two previous quarterly reports.

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

The Treasury's actions under the EESA continued to provide meaningful support to core financial markets during the second quarter of 2009. The steps taken by the Treasury to bolster financial stability continued to be reinforced by other actions taken by the United States and foreign governments to assist financial markets and financial institutions. Taken together, these actions improved capital positions at BHCs and conditions in short-term funding markets and likely had positive effects on bank and nonbank lending activity. However, the magnitude of the beneficial effects of Treasury 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 actions on financial markets.

Conditions and sentiment in financial markets showed noticeable signs of improvement during the second quarter of 2009. Pressures in short-term funding markets eased considerably, broad stock price indexes increased, on net, and risk spreads on corporate bonds narrowed significantly, as economic data suggested the contraction may be abating and programs funded by TARP reduced uncertainty. However, strains in many financial markets persisted during the second quarter, with a deterioration of creditworthiness and increasing default rates for some borrowers and the outlook for residential and commercial real estate valuations still cloudy. In addition, lending by banks tapered off as both the financial crisis and the economic downturn weighed on both the demand and the supply of credit.

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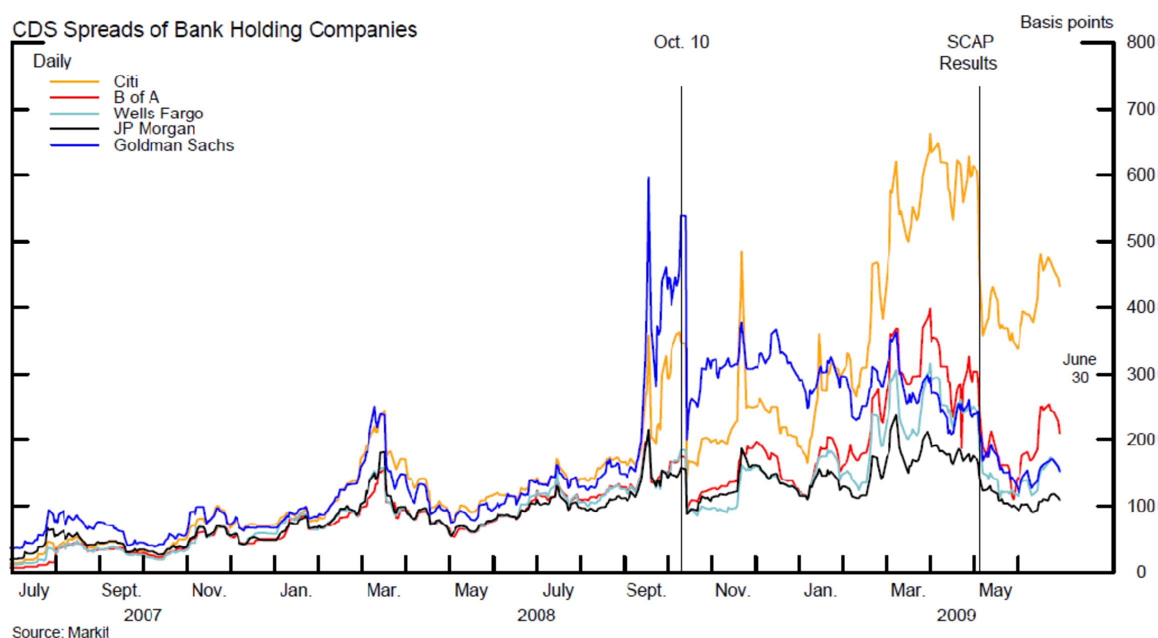
[3] 12 U.S.C. § 5201(1). For an overview of the conditions in the financial markets prior to passage of the EESA, see Part V of the Oversight Board's First Quarterly Report to Congress for the quarter ending December 31, 2008 ("First Quarterly Report").

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 a greater deterioration in the availability of credit to households, businesses, and communities. For example, TARP capital investments in banking organizations, in conjunction with TALF and other government programs, have contributed to the easing of liquidity pressures at banking organizations since late 2008.

Figure 2




In particular, the release on May 7, 2009, of the results of the SCAP exercise undertaken for the nation's 19 largest BHCs has helped improve investors' sentiment towards banking organizations and financial markets more generally. Nearly all the BHCs evaluated were found to have enough Tier 1 capital to absorb the higher losses envisioned under the hypothetical more adverse economic scenario, thanks, in part, to the more than $200 billion of capital that these institutions had received through the CPP from the government since last fall. However, 10 firms were determined under SCAP to need to augment their capital to meet the SCAP capital buffer requirement or improve the quality of the capital from the level of the fourth quarter of 2008; the combined amount totaled $185 billion, nearly all of which was required to meet the target Tier 1 common to risk-weighted assets ratio. Credit default swap ("CDS") spreads for banking organizations (figure 2), a key measure of investors' concerns about the health of these institutions, had increased, on net, throughout the first quarter of 2009. However, spurred by the release of the SCAP results, CDS spreads for these banking institutions dropped, and bank stock prices (figure 3) increased in early May.

Figure 3

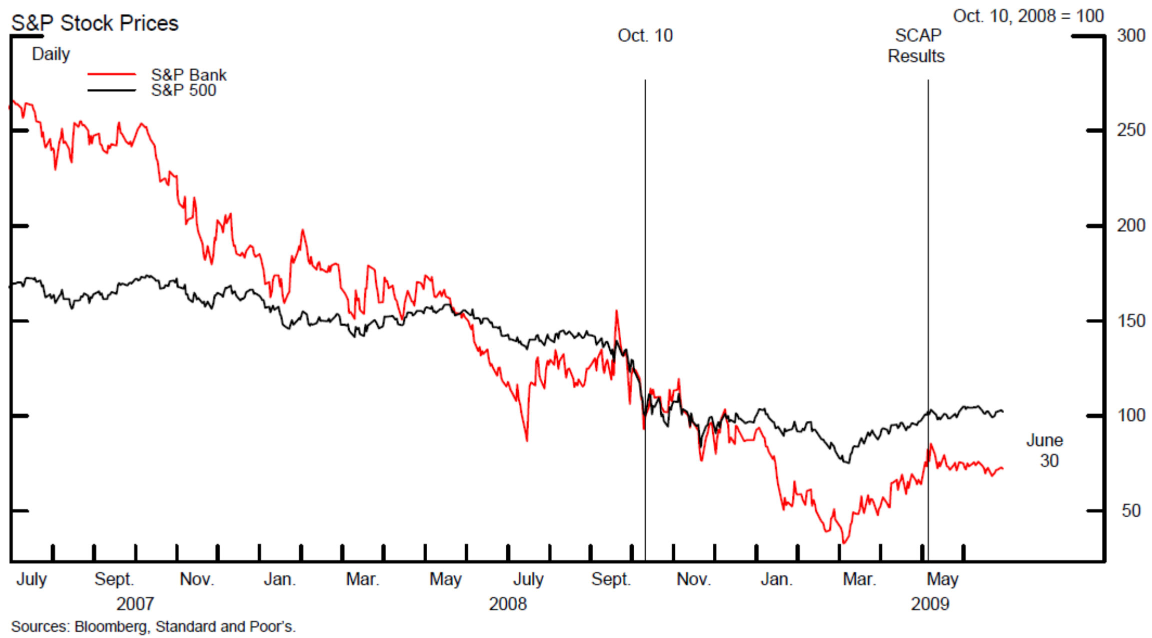
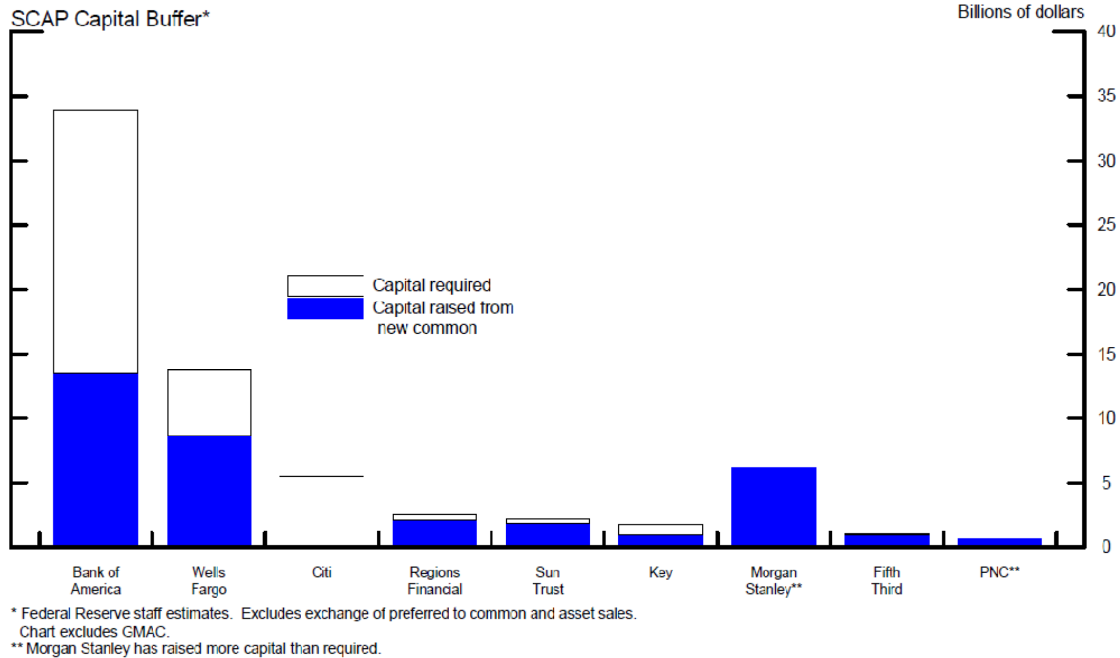


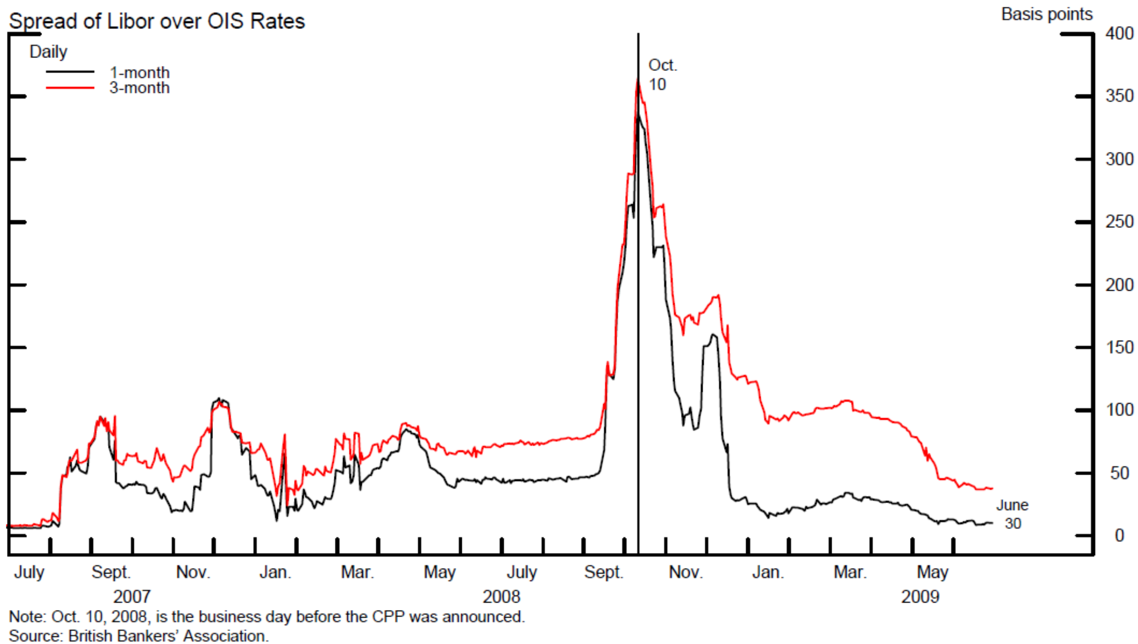

Figure 4



The evaluated BHCs have subsequently been able to raise a significant amount of capital from new common equity (figure 4). BHCs that were required to raise capital raised more than $34.5 billion in public common share offerings in May and June 2009. Including asset sales and exchanges of preferred for common shares, most of the firms are now at or near their required capital buffers. Firms that do not meet their buffer requirement can issue mandatory convertible shares to the Treasury under the CAP, in an amount up to 2 percent of the institution's risk-weighted assets (or higher on request) as a bridge to private capital. Those BHCs participating in the SCAP exercise that did not need to raise additional capital to meet the SCAP buffer also were able to raise new equity in private markets in May and June. Most of these firms (along with others participating in the CPP) applied for and received approval from their respective federal banking supervisors to repay their outstanding CPP preferred stock. On June 17, 2009, ten of the largest U.S. BHCs – all but one of which participated in the SCAP exercise – repaid about $68 billion to the Treasury.

The institutions participating in the SCAP also have issued more than $25 billion in non-FDIC-guaranteed debt and roughly $10 billion of debt under the FDIC's Temporary Liquidity Guarantee Program ("TLGP"). The ability to raise private capital and issue non-FDIC-guaranteed debt indicates increased investor confidence in the prospects of large banking institutions. Still, some unease persists and CDS spreads for large banks remain elevated.

Figure 5



Note: Oct. 10, 2008, is the business day before the CPP was announced.
Source: British Bankers' Association.

Consistent with the overall reduction in concerns about the health of large banking organizations, conditions in interbank markets have continued to improve. The spreads of LIBOR rates to overnight index swap ("OIS") rates (figure 5), a useful measure of banks' short-term borrowing costs, have continued to decline in the second quarter. The spread of the one-month LIBOR over OIS has narrowed to levels close to those prevailing before the financial crisis, and the spread of the three-month LIBOR over OIS, while still elevated, has declined to levels not seen since early 2008. In line with these improvements in bank funding markets, the use of the Federal Reserve liquidity facilities directed at depository institutions has declined.

Debt growth for nonfinancial businesses and households, however, has continued to be weak in recent months. To put the current lending trends in historical perspective, data from the Flow of Funds Accounts published by the Federal Reserve Board show that, aggregating across banks and other sources of debt, growth in borrowing by households and nonfinancial businesses has tended to slow significantly in periods of economic weakness, and generally has not strengthened until after the trough in economic activity (figures 6 and 7 respectively). Viewed against that backdrop, data through the first quarter of 2009 (the latest data available for the Flow of Funds Accounts) 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 6

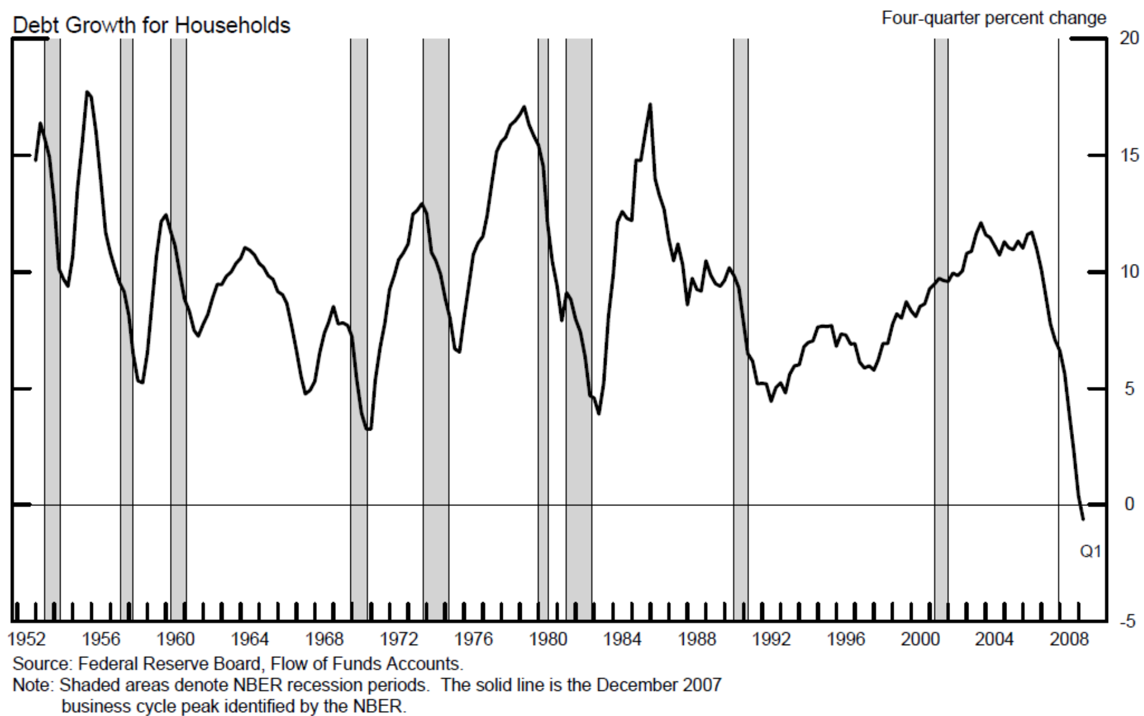
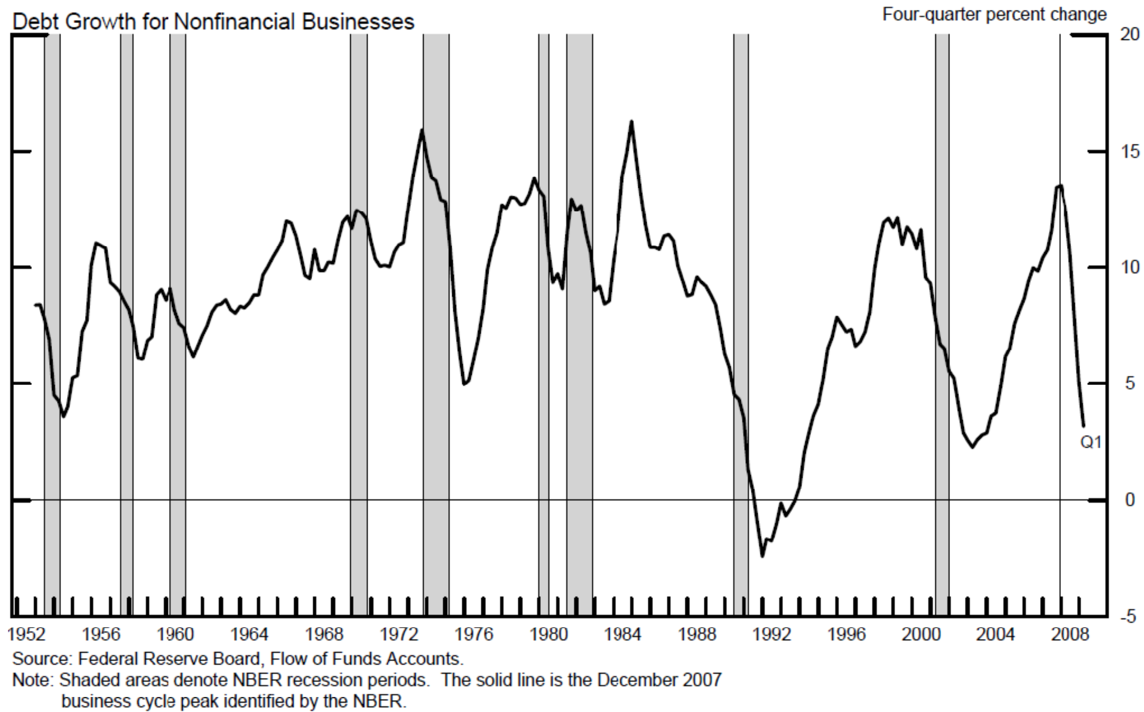


Figure 7




Identifying the effects of EESA programs on lending 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. The onset of significant repayments of CPP funds during the quarter presents further analytical challenges as the panel of CPP recipients and their characteristics shift over time.

Figure 8

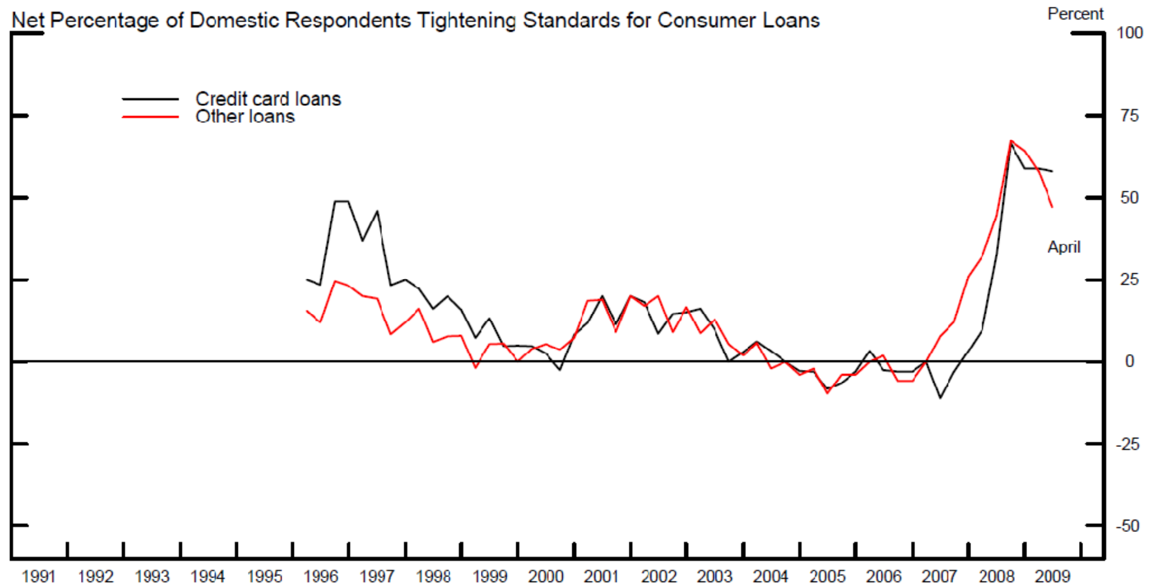
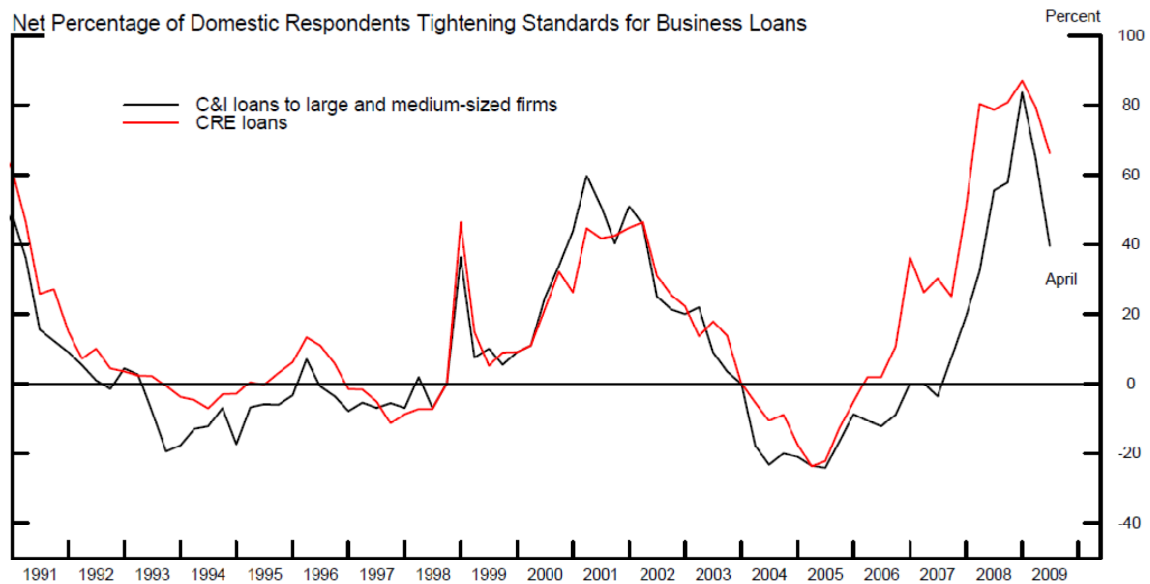
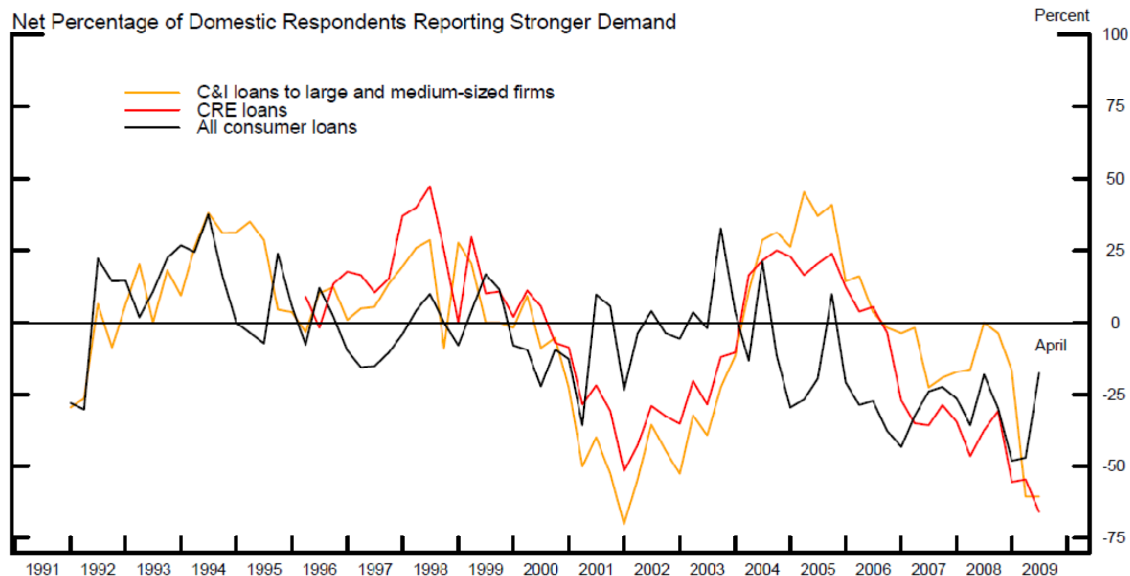



Figure 9



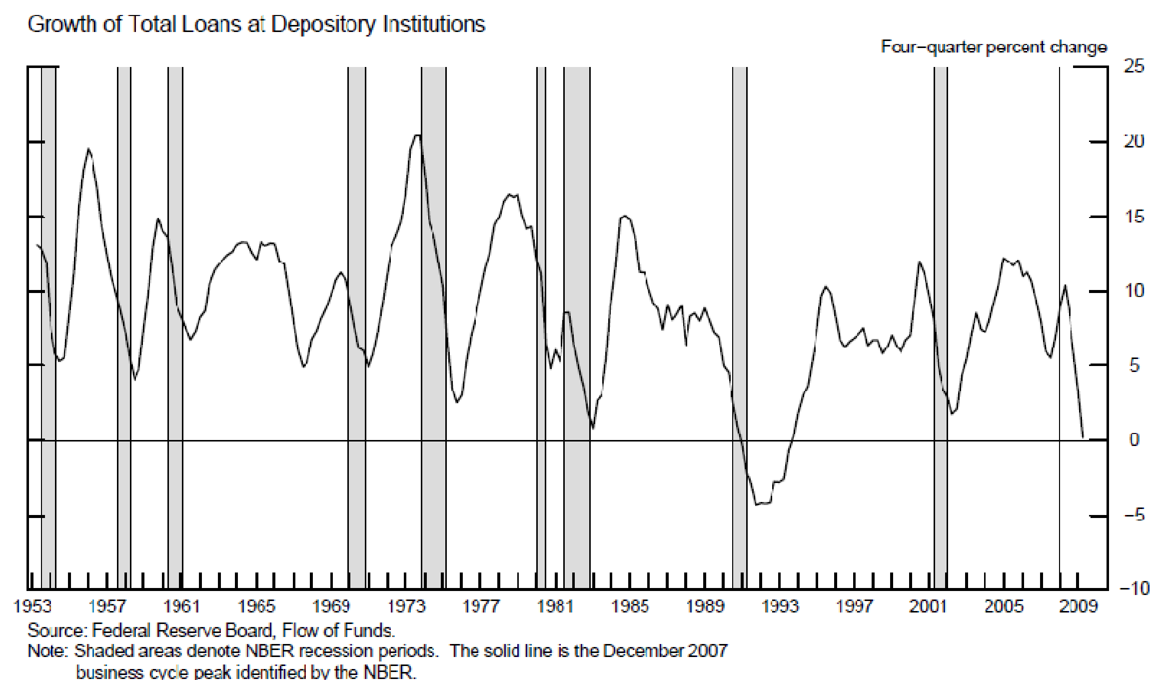
Data from the April 2009 Federal Reserve survey of senior loan officers at banks provide useful insight into the salience and direction of these various influences on bank lending. The April survey results once again appear to support the hypothesis that both supply and demand factors recently have acted as a brake on bank lending activities. For example, domestic banks have been tightening standards since early 2008 for consumer (figure 8), commercial and industrial ("C&I"), and commercial real estate ("CRE") loans (figure 9), although the net percentage of banks that tightened standards has eased a bit in recent months, especially for C&I loans to businesses. Almost all of the banks that tightened standards indicated that concerns about a weaker or more uncertain economic outlook were important in their decision to do so. Less than one-third of the banks cited concerns about current or future deterioration in their own capital position as an important reason for raising loan standards, which suggests that the availability of TARP capital injections may have helped prevent an even greater tightening of lending standards. Banks also reported a further decrease in the demand for loans (figure 10), indicating that weak demand is a relevant factor to explain weaker borrowing, in particular for C&I and CRE loans.[4]

Figure 10




[4] The answers to survey questions about loans to small firms, not explicitly shown in figures 8, 9, and 10, are very close to the data about loans to large and medium-sized firms reported in those figures.

Figure 11




Consistent with these trends in supply and demand for bank credit, Flow of Funds data for total loans at depository institutions (figure 11) show that growth in loans has fallen off since the most recent business cycle peak in December 2007, and was negligible in the first quarter of 2009. Data from the weekly survey of banks summarized in the Federal Reserve's H.8 Statistical Release provides evidence that growth in bank credit to households and to nonfinancial businesses has remained weak during the second quarter. As discussed further below, some of this weakness, however, reflects a substitution from loans on banks' balance sheets to other forms of credit, which were in part made available through the TALF.

Monthly reports collected by Treasury from CPP recipients provide similar indications. Treasury's Monthly Lending and Intermediation Snapshot reports for February, March, and April 2009 show some acceleration in the pace of new loan originations at the 21 banking organizations that had received the largest amounts of capital under the CPP. There were some indications that this increased growth could in part reflect seasonal patterns. Residential mortgage originations grew particularly sharply. The stock of loans at these organizations, however, declined about 2 percent over the three-month interval ending in April. Treasury's new CPP Monthly Lending Report, which provides total outstanding loan balances for all other CPP recipients (roughly 500 institutions), indicated that total loans declined in the month of April, although the consumer loan portion of the total rose slightly once the data were adjusted to exclude CPP recipients who repaid the Treasury.

Figure 12

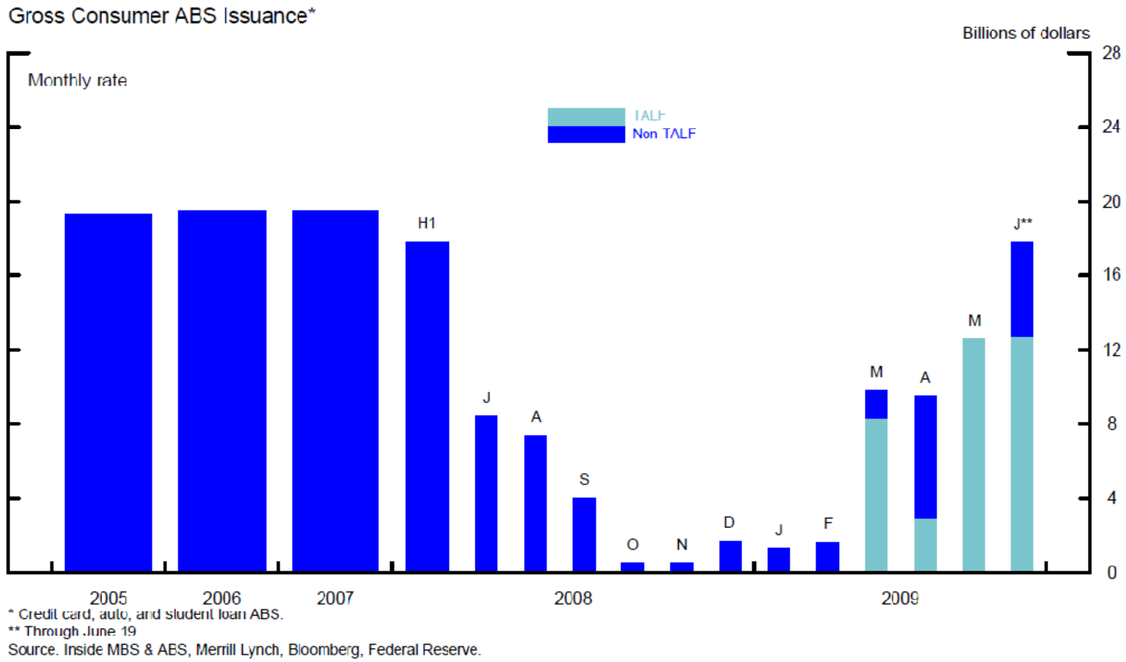
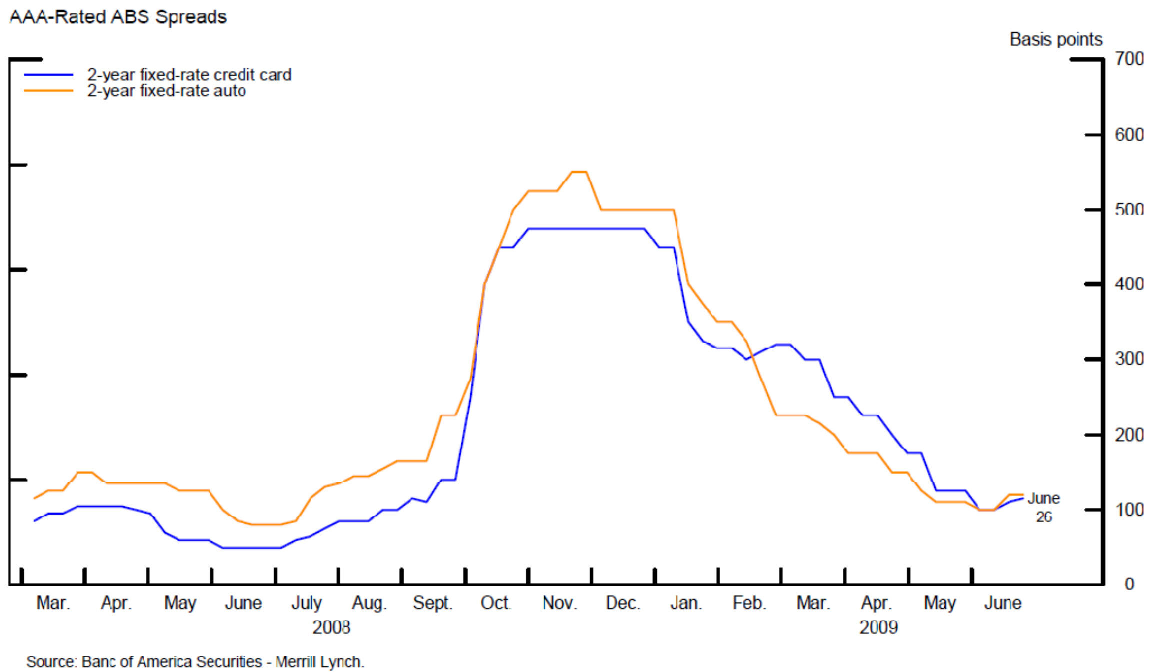
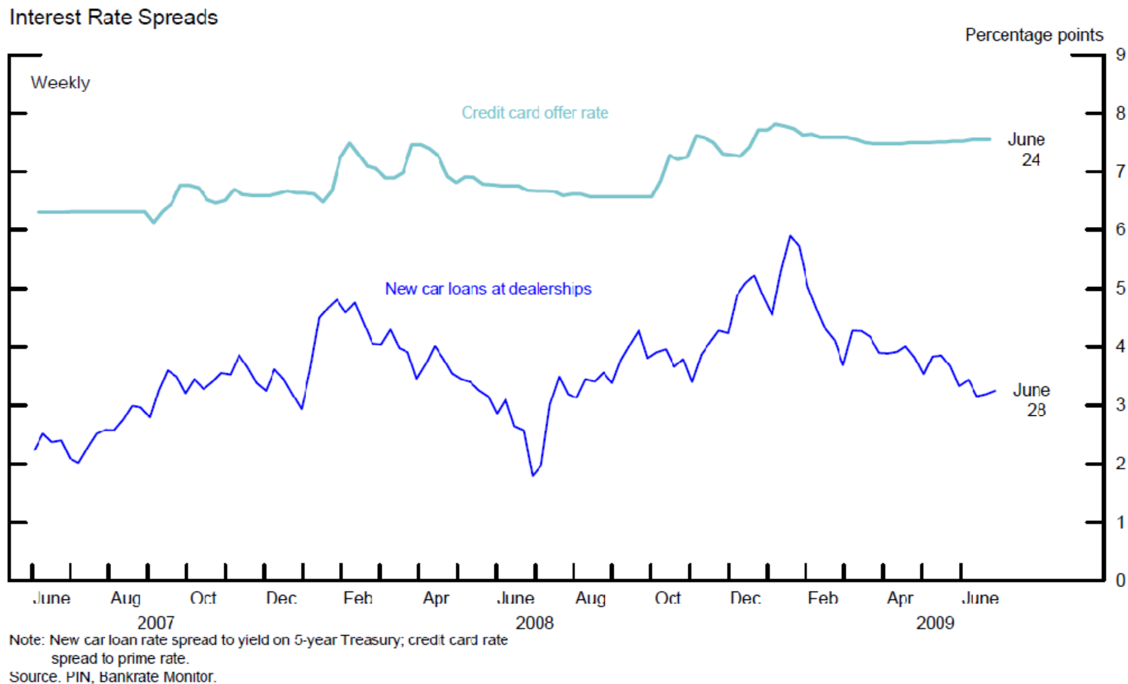



Figure 13



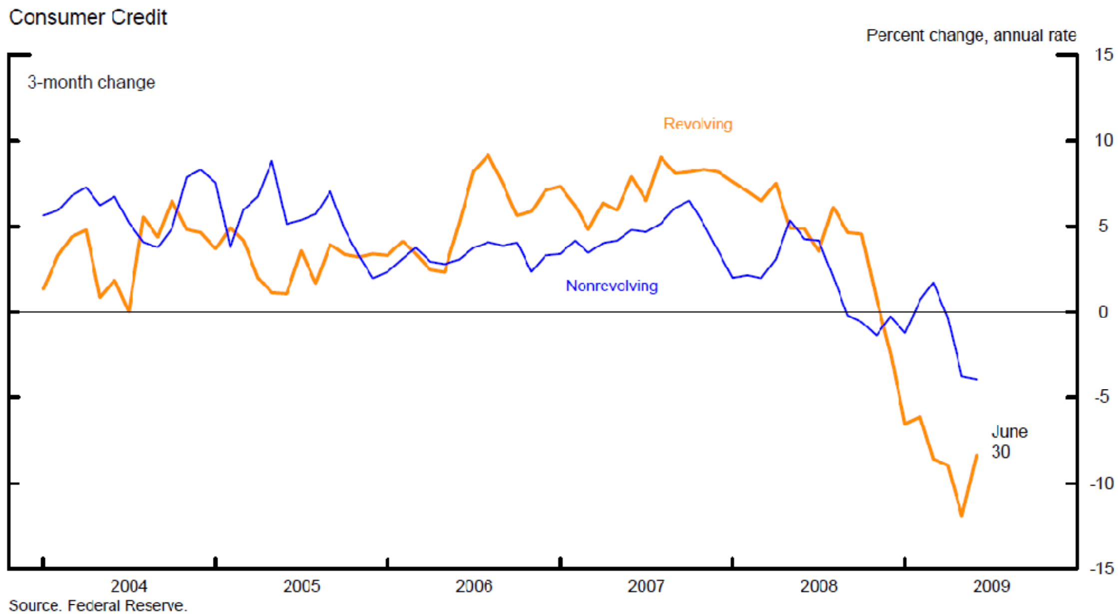
The TALF program has successfully facilitated consumer credit ABS issuance and has led to an improvement in conditions in the secondary market for securitized consumer credit. Issuance of consumer credit ABS ramped up starting in March 2009, after having shut down in the fall of 2008. TALF-financed issues totaled about $30 billion from March to June 2009, and issuance without TALF financing also has risen (figure 12). Spreads in the secondary market on AAA-rated consumer ABS (both on credit card debt and on auto loans) have narrowed further and have now reversed a large fraction of the run-up from mid-2007 to their peaks at year-end 2008 (figure 13). In late June, the spreads fell to close to 100 basis points. Since the rate on most TALF loans for consumer credit ABS is set at 100 basis points above the relevant LIBOR, the spreads are now close to a level at which investors will not find it economical to finance their purchases with TALF. Therefore, as financial strains ease, the reliance on this program will, by design, begin to dissipate.

Figure 14



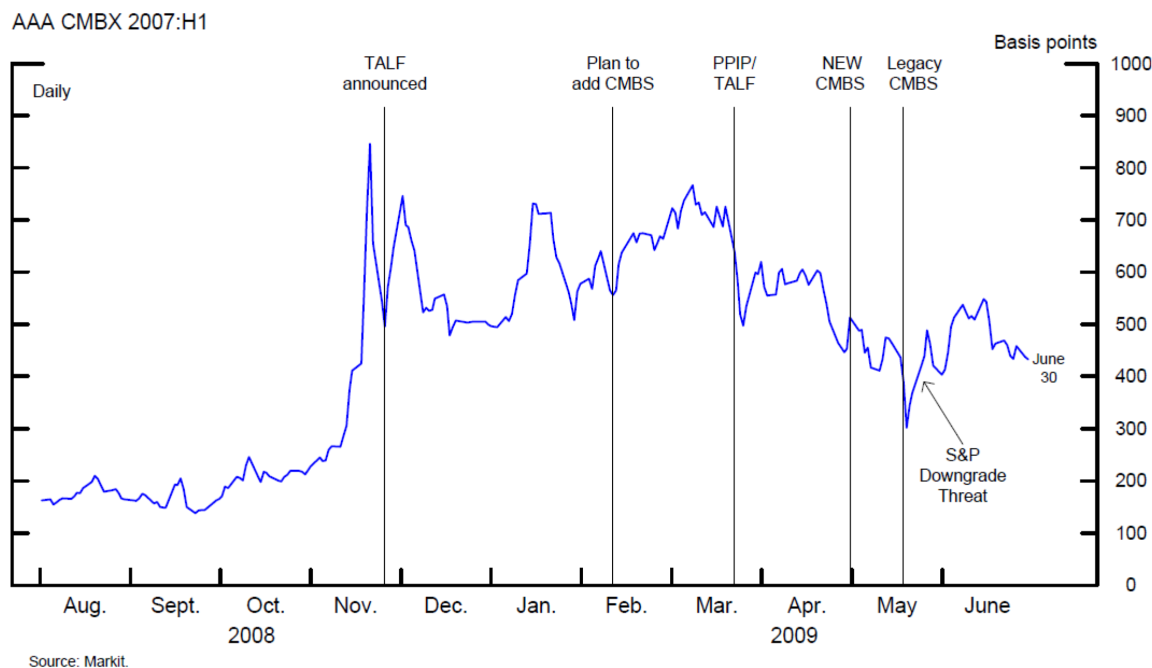

The effects of the improvements in ABS markets on the interest rates paid by households are more difficult to gauge, given that credit quality also has deteriorated and delinquency rates on consumer loans have risen. On net, interest rate spreads on new car loans at dealerships have declined, while spreads on credit card interest rates for prime borrowers have remained about flat (figure 14).

Figure 15




Overall, consumer credit continued to contract at a rapid pace in recent months (figure 15), held down by a combination of sluggish consumer spending and limited credit availability. In particular, the April data on the 3-month change in revolving credit was the weakest on record. In addition, first quarter bank data from call reports collected by the Federal Reserve System show that unused commitments for credit cards fell at a 45 percent annual rate. These developments indicate that credit card debt remains extremely tight, reflecting a deterioration in household credit quality. In contrast to the credit card market, conditions in the auto finance market are not as tight as they were last fall, thanks, in part, to the support provided by government programs. For instance, lending at GMAC, a recipient of government assistance, continued to rebound in March and April, and the company is expanding its operations to include loans against cars sold by Chrysler.

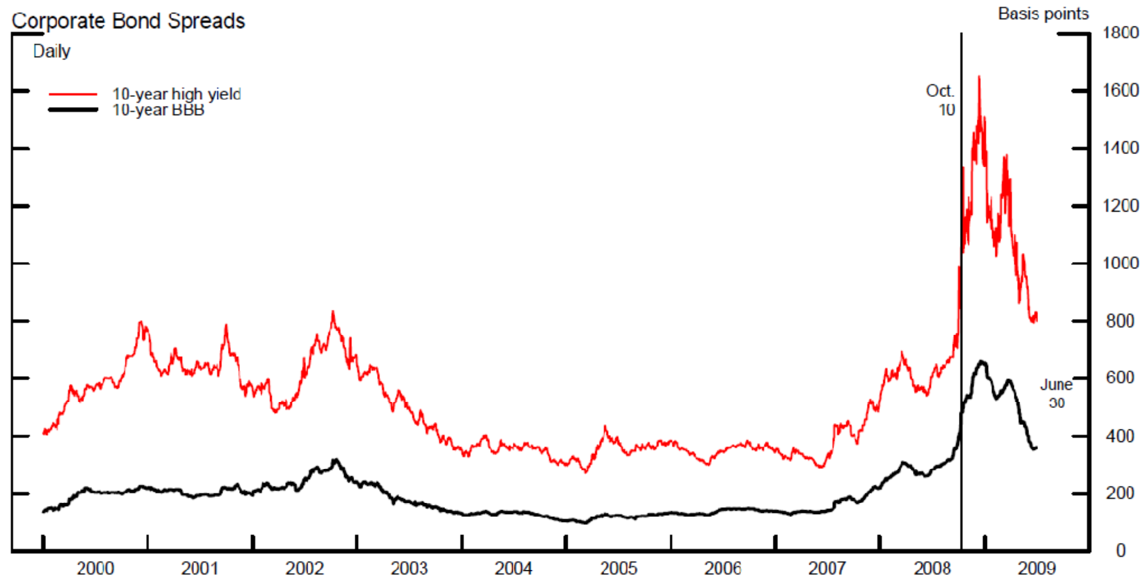
Figure 16




In commercial mortgage markets, the expansion of the TALF program to CMBS appears to have reduced, on net, the interest rate spreads on CMBS. As can be seen in quotes of the AAA CMBX index (figure 16), the declines from the peaks in March were especially noticeable around the dates of some of the announcements about the TALF program expansion. However, the spreads recently have widened, after S&P, on May 26, warned of changes to its rating methodology for CMBS—CMBS downgrades would make some of the currently AAA-rated paper ineligible for TALF.

Overall, commercial real estate markets have remained under considerable stress, with commercial property prices falling and delinquency rates rising. Industry analysts' reports and Federal Reserve staff estimates forecast that more than $500 billion of commercial mortgages are to mature in 2009, with the majority of those mortgages held by commercial banks. In the current environment, some borrowers may have trouble refinancing their loans at maturity, especially shorter-term loans on construction properties. While CMBS typically fund only longer-term loans on existing properties, the expansion of the TALF program will inject some needed liquidity into this market, and, through additional transactions, help to reduce uncertainty about valuations. In addition, it can ease balance sheet pressures at banks by providing a vehicle for them to securitize their longer-term loans. However, concerns remain because many of the construction loans that are expected to mature this year were originated in the elevated real estate markets of 2006 and 2007 and are on new properties that do not have a regular stream of rental payments. Potential refinance lenders may be less willing to provide the same financing amounts and terms for properties whose values have fallen and for which the amounts of incoming cash flow are subject to significant uncertainty.

Figure 17




Note: Spread to comparable-maturity Treasury securities.

In credit markets for corporate borrowers, corporate bond spreads (figure 17) have dropped sharply in recent months and yields have declined. Gross bond issuance by nonfinancial corporations, both investment and speculative grade, (figure 18) has been robust in the second quarter. Speculative grade issuance, which had been minimal in the second half of 2008, rose to its highest levels since June 2007, reflecting increased investors' appetite for risk. With declining yields, firms have reportedly used the proceeds of some of the newly issued bonds to pay down shorter-term debt, notably bank loans, which helps to explain, in part, the decline in C&I loans. Gross public equity issuance by nonfinancial firms (figure 19), mostly from seasoned offerings, has surged in the second quarter. These developments indicate that nonfinancial businesses have taken advantage of some of the easing of financial strains and issued long-term debt and equity to improve their financial positions.

Figure 18

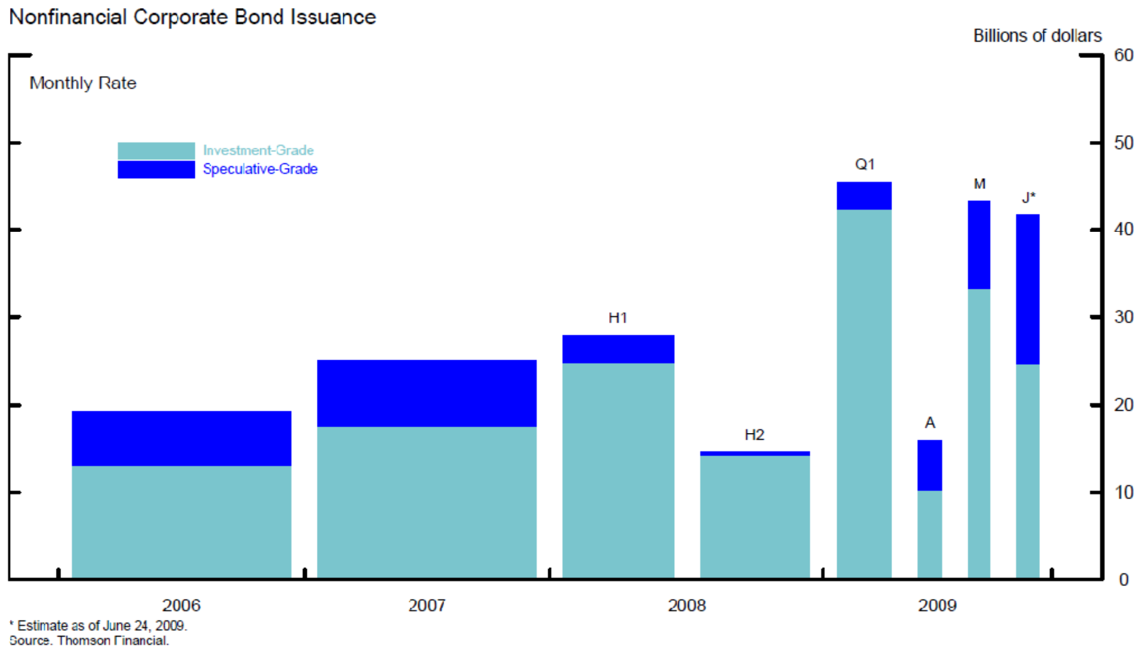
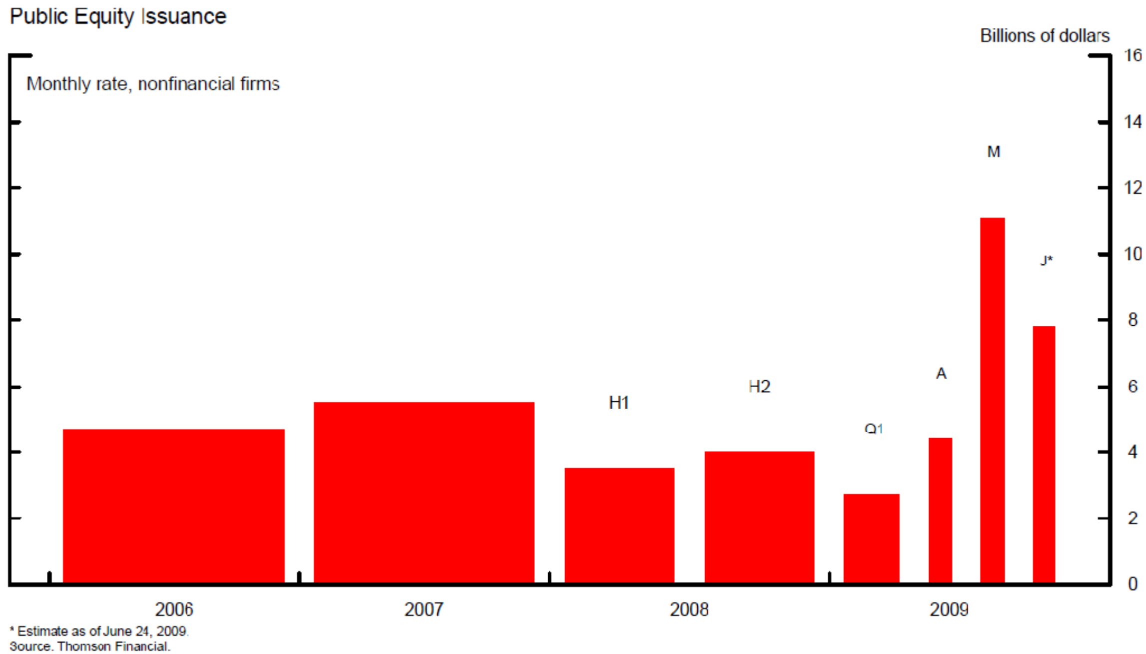


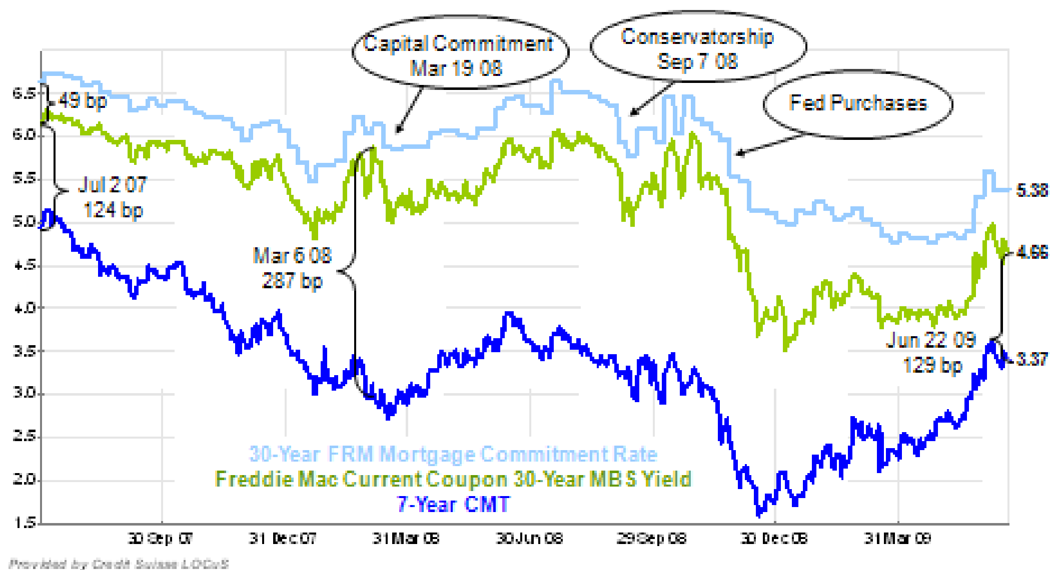

Figure 19



b. 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 second quarter of 2009 by further relieving strains in the functioning of credit markets and aggressively supporting the demand for MBS. Purchases of those securities by the Federal Reserve and the Treasury held down the rise in interest rates on 30-year fixed-rate mortgages during the quarter to roughly 60 basis points, despite larger increases in yields on reference Treasury securities. The resulting narrowing of mortgage-Treasury yield spreads continues a trend beginning last November that has brought them down from extraordinary widths to magnitudes much closer to historical norms (figure 20).

Figure 20

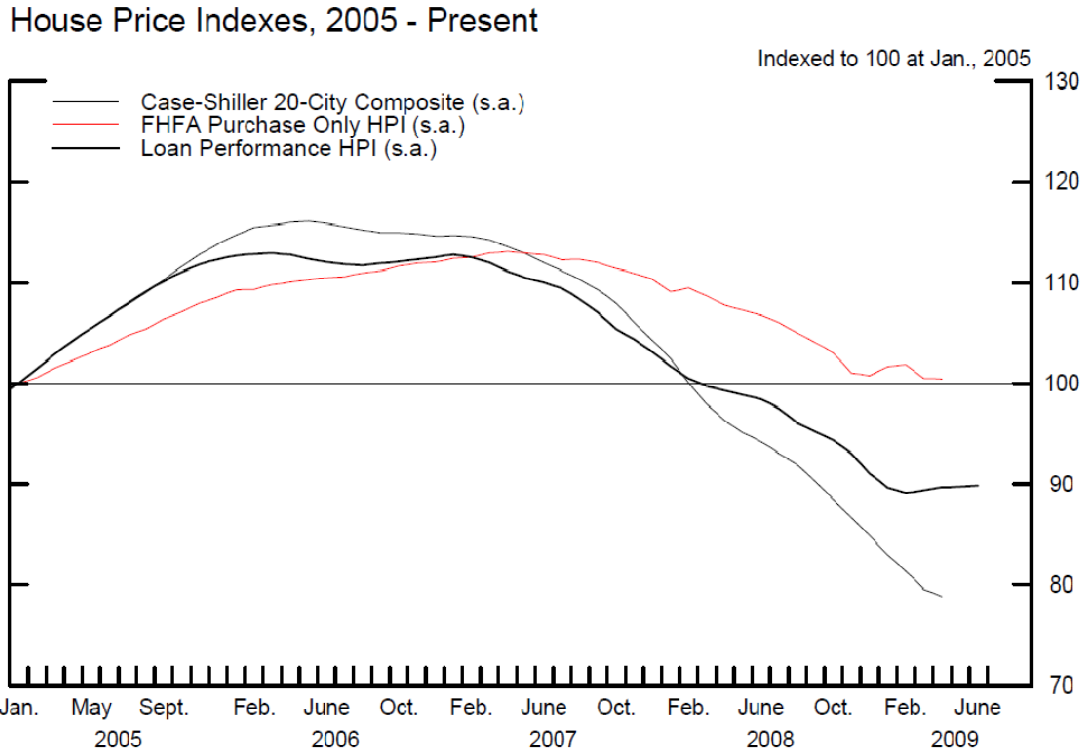



Sources: Credit Suisse, Freddie Mac, and Federal Reserve Board H15.

Higher borrowing costs have reduced the attractiveness of refinancing existing mortgages for many homeowners, reversing the earlier jump in the pace of refinance activity, as measured by the Mortgage Bankers Association. The higher mortgage rates appear to have had little effect on demand for home purchase loans, which have been stable, as rates remained near their historical low points and the tax credit for first-time homebuyers provided additional encouragement for buyers. Also encouraging is the report from the National Association of Realtors that its Pending Home Sales Index rose for the fourth month in a row in May. Moreover, according to Census Bureau and HUD data, the month's supply of unsold, new, one-family houses at current sales rates declined from almost 12 and one-half months to 10 months between January and May, still high by historical standards, but the first reversal in the current housing downturn. These data

are suggestive of some future slowing in the decreases of house prices, and indeed the FHFA House Price Index and that of Loan Performance showed some leveling off in house prices during the period. However the S&P/Case-Shiller index continued to fall sharply (figure 21).

Figure 21

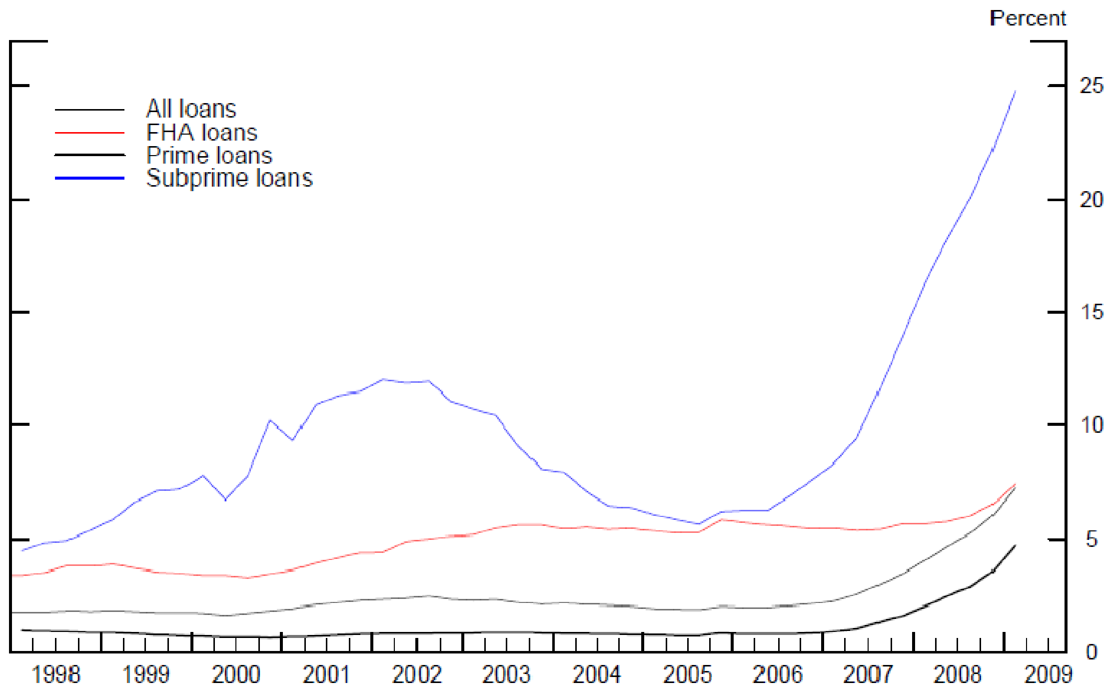



The combined effects of weak underwriting, falling house prices, and rising unemployment continue to have a powerful impact on mortgage delinquency rates. Data through April show no abatement of the soaring shares of loans whose borrowers are seriously behind on their payments (figure 22). A contributing factor, in addition to those cited above, is the range of foreclosure moratoriums offered by many servicers. Their restraint will permit more careful evaluation of the suitability of loans currently in default for modifications that in many cases should obviate the need for foreclosure and ultimately return the loans to current status.

At the end of May, the seriously delinquent rate on FHA loans stood at 7.69 percent. The in-foreclosure component of the seriously delinquent rate first rose above 1.50 percent last December, and stood at 1.87 percent in May. Insurance claims paid in the first eight months of FY 2009 (Oct – May) are 16 percent above the number of claims paid during the same months of FY 2008. In April and May of this year, claims were 24 percent above the number seen in the year-earlier period.

The recent expansion of the Home Affordable Refinance Program will facilitate refinancing for borrowers whose loans are guaranteed by Fannie Mae or Freddie Mac and whose property values have fallen to the point where the ratio of their loan amount to property value is as much as 125 percent. Together with the HOPE for Homeowners Program, which is now systemically being considered as an alternative under the HAMP, homeowners whose home loans significantly exceed current property values have a range of alternatives available to assist them in finding a sustainable refinancing alternative that may help them to avert foreclosure.

Figure 22




The pace of modifications has expanded steadily in recent quarters at Fannie Mae and Freddie Mac, with volumes more than doubling since the establishment of the conservatorships. Perhaps even more importantly, the share of modifications with decreased monthly payments has also nearly doubled, and the share with payments reduced by more than 20 percent is nearly three times what it was. The Office of the Comptroller of the Currency and Office of Thrift Supervision reported similar increases in total modifications and reductions in monthly payments at large national banks and thrifts under their oversight that manage roughly two-thirds of all first-lien U.S. mortgages.

FHA continues to provide substantial support to credit flows in the housing market. After three straight quarters of single-family insurance volumes of over $72 billion, volumes increased in the second quarter of 2009 to $88 billion, which represents nearly 480,000 households. The largest growth was in the refinance portfolio, so that a majority of FHA-insured borrowers in the second quarter of 2009 obtained

refinance loans (53 percent). The total number of households served in the quarter was 50 percent higher than in the year-earlier quarter, and more than four times the number served in the second quarter of 2007.

FHA is confident in the quality of the new business it is taking on. Borrower credit quality remains high, and indeed average FICO scores and incomes among new borrowers have risen significantly over the past year. Further, refinance loans generally start with more initial equity than do purchase loans. There were virtually no insurance endorsements on loans with seller-funded down payment assistance in the quarter, as the ban took effect for loans closed on or after October 1, 2008. In addition, FHA reduced the maximum loan-to-value ratio on cash-out refinance loans earlier this year, which also strengthens the business going forward. As an early possible indication of credit quality, FHA 30- and 60-day delinquency rates peaked last November, and have come down measurably since then. Thus, it may be that FHA insurance claims will peak by the end of 2009 and decline in 2010.

## III. DISCUSSION OF THE ACTIONS TAKEN BY TREASURY UNDER THE EESA DURING THE QUARTERLY PERIOD

This part 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. Update on Capital Programs

The CPP is the largest and most significant financial stability program Treasury has established under EESA. The CPP, together with the CAP, are collectively referred to as the "capital programs." These programs recognize that broad economic recovery is not possible without reviving confidence in the strength of the U.S. financial system. With higher capital levels and reinforced confidence, financial institutions can continue to play their vital role in our communities. The steps taken by Treasury during the quarterly period with respect to the capital programs are described in greater detail below.

#### *i. Update on the Capital Assistance Program and the Supervisory Capital Assessment Program*

Capital plays a critical role in supporting confidence in the health of the banking system. While the vast majority of U.S. banking organizations have capital in excess of the amounts required to be considered well-capitalized, the uncertain economic environment has eroded confidence in the amount and quality of capital held by some organizations. In turn, market participants' concerns over the capital positions of some institutions is impairing the ability of the system overall to perform its critical role of credit origination and intermediation.

The CAP was established by Treasury in February 2009 to ensure that qualified financial institutions ("QFIs") have sufficient common equity to retain the confidence of investors and to meet supervisory expectations regarding the amount and composition of capital.[5] The capital provided to eligible banking organizations under the CAP will be in the form of a preferred security that is convertible into common equity.

As a complement to the CAP, the Federal Reserve, in conjunction with other FBAs, engaged in a comprehensive forward-looking Supervisory Capital Assessment Program ("SCAP"), or "stress test," of the 19 largest BHCs.[6] The primary purpose of this supervisory exercise was to determine how much of an additional capital buffer, if any, each of the 19 largest BHCs would need to establish now to ensure that they could withstand losses and continue lending in 2009 and 2010, even in a more challenging economic environment than the one currently projected for those years. Specifically, the FBA evaluated potential losses on loans, assets held in certain investment portfolios, and trading-related exposures for those firms with trading assets exceeding $100 billion, in addition to losses from off-balance sheet positions. The loan loss reserves available to absorb such losses for each of the 19 participating BHCs also were considered as a part of the analysis.[7] The supervisory assessment process used by the agencies is similar to the stress tests typically performed by banking institutions as part of their risk-management efforts, but differs in that they were conducted for all 19 BHCs on a simultaneous and streamlined basis with common assumptions to achieve a forward-looking assessment.

The FBAs evaluated two scenarios under the SCAP: (1) a baseline scenario which reflected the consensus expectation of private forecasters on the depth and duration of the current recession,[8] and (2) a more adverse scenario that analyzed the results for a longer

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[5] The terms and conditions of the CAP are detailed in the Oversight Board's prior quarterly report, which is available at:
http://www.financialstability.gov/docs/FSOB/FINSOB-Qrtly-Rpt-033109.pdf.

The CAP application guidelines are available at:
http://www.financialstability.gov/docs/CAP_App-Guidelines.pdf.

[6] These institutions, which collectively hold two-thirds of the assets and more than one-half of the loans in the U.S., are: American Express Company, Bank of America Corporation, BB&T Corporation, The Bank of New York Mellon Corporation, Capital One Financial Corporation, Citigroup, Inc., Fifth Third Bancorp, GMAC LLC, The Goldman Sachs Group, Inc., JPMorgan Chase & Co., KeyCorp, MetLife, Inc., Morgan Stanley, PNC Financial Services Group, Inc., Regions Financial Corporation, State Street Corporation, SunTrust Banks, Inc., U.S. Bancorp, and Wells Fargo & Company.

[7] By considering the sufficiency of reserves at the end of 2010, the SCAP necessarily takes into account expected losses in 2011.

[8] The baseline used the average of projections released in February 2009 by Consensus Forecasts, the Blue Chip survey, and the Survey of Professional Forecasters.

and more severe recession than the current consensus expectation.[9] As part of this analysis, the BHCs estimated the amount of existing capital available to absorb future losses, as well as the need to raise additional capital to meet these losses, should they occur. These estimates were reviewed and analyzed by the FBAs and then evaluated against independent benchmarks developed by the FBAs to arrive at the supervisors' loss estimates.

The results of the SCAP, which were released on May 7, 2009, and considered by the Oversight Board, indicated that the 19 participating BHCs could withstand up to $600 billion in losses during 2009 and 2010, if the economy were to track the more adverse scenario, with $455 billion of these losses resulting from the loan portfolios of these BHCs, and $135 billion resulting from trading-related exposures and securities held in investment portfolios. When combined with the losses already recognized by these firms since mid-2007, the SCAP results indicated that losses at these firms could total nearly $950 billion by the end of 2010, if the economy were to follow the more adverse scenario.

After taking account of losses, revenues and loan loss reserve needs, in the aggregate, the FBAs concluded that these firms needed to add $185 billion to their capital buffers to reach the target SCAP capital buffer at the end of 2010 under the more adverse scenario. Specifically, the FBAs determined that 10 of the 19 participating BHCs had insufficient capital and capital structures that were too strongly tilted toward capital other than common equity to get through the adverse scenario. Thus, each of these 10 firms needed to augment their capital as a result of this exercise, and must do so by raising common equity or preferred stock that is convertible to common equity. A number of these firms were able to substantially reduce the amount of capital needed to meet the target SCAP capital buffer by either completing or contracting for asset sales and restructuring existing capital instruments. Taking account of these transactions, the 10 institutions required a combined addition of some $75 billion in capital. A more detailed breakdown of these results is provided in Part III above (figure 4).

The 10 BHCs determined to be in need of additional capital to meet the requirements set out in the SCAP had until June 8, 2009, to develop a detailed capital plan and have until November 9, 2009, to implement that plan. In light of the potential for new commitments under the CAP or exchanges of existing CPP preferred stock and to correspond with the implementation deadline established under the SCAP, Treasury extended the application deadline for the CAP until November 9, 2009. Treasury and the FBAs encouraged these institutions to design a capital plan that, wherever possible, actively seeks to raise new capital from private sources. Each institution submitted its

[9] The adverse scenario is not a worst case scenario. Rather it represents a significantly deeper and longer recession than the current consensus view of professional forecasters. That said, under the adverse scenario, for aggregate two-year cumulative losses on total loans are estimated at 9.1 percent, losses would be higher than the highest losses experienced during the Great Depression.

plan by the deadline of June 8, 2009. The capital plans broadly consisted of three main elements --

- a detailed description of the specific actions the institution will take to increase the level of capital and/or to enhance the quality of capital consistent with the results of the SCAP;
- a list of steps to address weaknesses, where appropriate, in the BHC's internal processes for assessing capital needs and engaging in effective capital planning; and
- an outline of the steps the firm will take over time to repay any capital previously received under CPP, CAP or the Targeted Investment Program ("TIP"), and to reduce reliance on any guaranteed debt issued under the Temporary Liquidity Guarantee Program established by the Federal Deposit Insurance Corporation.

As of May 28, 2009, the 10 institutions determined to be in need of additional capital as a result of the SCAP had already raised more than $34.5 billion of new common equity through public offerings, with a number of these offerings of common shares being over-subscribed. In addition, as of that date, these firms had announced actions that would generate up to an additional $12 billon of common equity. Each institution also has submitted a capital plan that, if implemented, would provide sufficient capital to meet the required buffer under the assessment's more-adverse scenario.

*ii. Update on the Capital Purchase Program*

The CPP was established by Treasury in October 2008 to address severely deteriorated conditions in credit markets and to stabilize the financial system by providing capital to a broad range of viable U.S. financial institutions. Given the program's goals of financial stability, Treasury designed the CPP to include institutions of all sizes and types across the country and has, accordingly, issued a number of term sheets since October 2008 to accommodate the variety of institutions that make up the U.S. banking system. These include publicly-traded and private institutions, institutions that have elected to be taxed under Subchapter S of Chapter 1 of the Internal Revenue Code ("S-Corps"), and institutions organized in mutual form. As of June 30, 2009, Treasury had invested approximately $203 billion under the CPP in senior preferred shares or other senior securities of 649 financial institutions, in 48 states, with the goal of providing capital to both sustain losses and enable lending. A more detailed explanation of the recent activity relating to the CPP is provided below.

*a. The Re-opening and Expansion of the Capital Purchase Program for Small and Community Banks*

On May 13, 2009, Treasury announced the re-opening and expansion of the CPP with new terms to support small and community banks. The program is open to all QFIs

with total assets of less than $500 million. Under the new terms, the maximum subscription amount available for QFIs with total assets of less than $500 million is 5 percent of risk-weighted assets, whereas the maximum subscription limit established for larger QFIs is 3 percent of risk-weighted assets. Current participants in the CPP with total assets of less than $500 million may submit an application for an incremental investment by Treasury, which will be processed by Treasury and the appropriate FBA on an expedited basis. In order to encourage participation in the expanded program, Treasury will not require warrants for any investment in excess of 3 percent of the QFI's risk-weighted assets.[10] The new application deadline for small institutions under the reopened and expanded CPP program is November 21, 2009.

*b. Establishment of Terms Relating to Mutual Holding Companies and Mutual Banks*

Consistent with the goal of making capital available to institutions of all types through the CPP, Treasury released standardized terms for certain qualified bank holding companies and savings and loan holding companies that are organized in mutual form ("mutual holding companies") and their stock holding company subsidiaries. Treasury also released standardized terms for qualifying mutual banks and saving associations that are organized in mutual form and do not have holding companies ("mutual banks").[11] In order to account for, and accommodate, the special organizational structures of these firms, Treasury has established four different term sheets in connection with CPP applications by mutual holding companies and mutual banks: (1) a term sheet for the issuance of preferred stock at publicly-traded mid-tier subsidiary holding companies; (2) a term sheet for the issuance of preferred stock at privately-held mid-tier subsidiary holding companies; (3) a term sheet for issuance of subordinated debentures by top-tier mutual holding companies without mid-tier subsidiary holding companies; and (4) a term sheet for the issuance of subordinated debentures at mutual banks without a holding company. The application deadline for mutual holding companies and subsidiary holding companies with a mutual top-tier parent company was May 7, 2009, and the application deadline for mutual banks was May 14, 2009.

The program terms for publicly-traded and nonpublic subsidiary holding companies with a mutual top-tier parent company are similar to the term sheets for other publicly and privately held QFIs participating in the CPP. For example, the minimum and maximum subscription amounts are, respectively, 1 percent of risk-weighted assets and the lesser of 3 percent of risk-weighted assets or $25 billion. The preferred stock to be acquired by Treasury also is senior to the institution's common stock and pari passu with existing preferred shares other than those that rank junior to any preferred shares by their terms. Like other preferred shares issued under the CPP, those issued to publicly-

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[10] Additional information regarding the terms of the CPP are available at: http://www.financialstability.gov/roadtostability/capitalpurchaseprogram.html.

[11] These terms sheets can be found at: http://www.financialstability.gov/latest/tg-04072009.html.

and privately-held companies with a mutual top-tier parent company have a dividend coupon rate of 5 percent for the first 5 years and 9 percent thereafter, an attractive rate designed to encourage participation in the program.

Since top-tier mutual holding companies do not issue stock, Treasury will instead receive subordinated debentures in connection with each such investment. Similarly, since a mutual bank is one owned by its depositors, the term sheet for mutual banks, released on April 14, 2009, provides for these organizations to issue senior subordinated debentures to the Treasury. The terms for the senior debt securities issued to the Treasury by top-tier mutual holding companies and mutual banks are similar to those for subordinated debt issued by S-Corps to Treasury under the CPP and are intended to be as similar as possible to the terms for preferred stock issued to the Treasury. The senior securities would have a maturity of 30 years and would pay an annual interest rate of 7.7 percent for five years, and thereafter pay an annual interest rate of 13.8 percent.[12]

The term sheets for all institutions also include several provisions designed to protect the interests of the taxpayers. Mutual holding companies, their privately and publicly-held subsidiaries, and mutual banks must abide by the same restrictions on dividends and redemptions, including the disallowance of paying dividends on other securities or redeeming other securities, unless all accrued and unpaid dividends are fully paid up on the Treasury's securities. In addition, common dividends may not be increased without the consent of the Treasury for the first three years following the CPP investment. The failure to pay dividends to Treasury for six dividend periods, whether or not consecutive, would trigger Treasury's right to elect two directors to the institution's board of directors.

Treasury also will receive warrants in connection with each investment, as required by the EESA. For publicly-held companies with a mutual top-tier parent company, Treasury will receive warrants to purchase common stock in an amount equal to 15 percent of Treasury's investment. For privately-held companies with a mutual company parent, Treasury will receive warrants equal to 5 percent of Treasury's investment. Both types of warrants are immediately exercisable. Like all CPP participants, participating institutions also must comply with all executive compensation restrictions applicable under EESA and Treasury regulations and guidelines.

[12] On an after-tax basis, and assuming a 35 percent effective 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).

### c. *Insurance Company Participation in the CPP*

On May 14, 2009, Treasury notified a number of insurance companies that are QFIs that they had received preliminary approval to participate in the CPP. Insurance company pre-approvals do not constitute a new program under TARP. Rather, all pre-approved insurance company QFIs complied with the requirements to participate in the CPP under existing program terms as they are organized as bank or thrift holding companies and filed a CPP application within the initial application window deadline. To process these applications, Treasury worked with insurance regulators and the federal banking agencies to develop a robust analytical framework to assess the particular characteristics of insurance companies.

### d. *Repayment of CPP Investment, Dividends on CPP Investments, and Withdrawal of CPP applications*

Repurchases of Treasury investments under the CPP are subject to section 7001 of ARRA, which requires the Secretary to consult with the appropriate FBA of any QFI seeking to repay any investment provided under the CPP. In order to redeem a CPP investment, a financial institution must first obtain approval from its primary FBA, which then forwards approved applications to Treasury.[13] After the CPP capital is repaid, the QFI can opt to repurchase any other equity securities of the QFI held by Treasury, including warrants. Treasury published the process and terms for repayment of any CPP investment in March, followed by updated guidelines in May reflecting terms that apply to SCAP participants. As of June 30, 2009, 32 institutions repaid approximately $70 billion in principal under the CPP, of which more than $68 billion was received from the 10 largest financial institutions participating in the CPP.

Under the terms of the Securities Purchase Agreement, which apply to all CPP participants, after redemption of TARP capital in whole, the warrants held by Treasury can be repurchased at fair market value, subject to certain notice requirements. The terms also clarify a procedure for how the fair market value is to be calculated and thereby provides a means to resolve any valuation disputes, should they occur. According to these procedures, the board of directors of the QFI must first provide its fair market valuation to Treasury. The fair market value is to be determined by the board of directors in good faith in reliance on an opinion of a nationally recognized independent investment banking firm retained by the company to value the securities and certified in a resolution to the Treasury. Treasury then has 10 days from the date of receipt of the board of directors' fair market value determination to object in writing to the proposed valuation. If Treasury objects, an authorized representative of Treasury and the chief executive officer of the QFI must promptly meet to resolve the objection and try to agree upon the

[13] On June 1, 2009, the Federal Reserve announced the criteria it will use to process redemption applications for the 19 BHCs that participated in the SCAP, and any other BHCs that have received funds from Treasury under the TARP. Additional information regarding the Federal Reserve's criteria can be found at: http://www.federalreserve.gov/newsevents/press/bcreg/20090601b.htm.

fair market value. However, in the event that the chief executive officer and Treasury's authorized representative are unable to agree on a fair market value in the 10 days following the delivery of Treasury's objection to the board of directors' fair market value determination, an appraisal procedure may be invoked by either party. The appraisal procedure is triggered by delivery of written notification not later than the 30th day after the date of Treasury's objection. The company must bear the costs of appraisal.

Under the terms of the Securities Purchase Agreement, the QFI and Treasury each must choose an independent appraiser to arrive at fair market value, if the appraisal procedures is invoked, and must deliver a notice to the other party appointing its appraiser. However, if within 30 days after the appointment of the two appraisers, the two appraisers cannot agree on the fair market value, within 10 days a third independent appraiser must be chosen by mutual consent of the first two appraisers. The third appraiser then has 30 days after his or her selection to estimate fair market value. An average of the three determinations of the three appraisers shall be the fair market value that is binding on the company and Treasury, unless one of the appraisals is extremely out of line with the other two. More specifically, if one appraisal deviates from the middle determination by more than twice the amount that the third appraisal differs from the middle determination, then the deviant appraisal shall be excluded and the other two averaged. The average of the two appraisals is binding on Treasury and the company.

*e. Withdrawal of CPP applications*

During the quarterly period, a number of institutions chose to withdraw their CPP applications after receiving preliminary approval from the Treasury. As of June 30, 2009, at least 450 institutions, representing more than $33.6 billion in requested funds, subsequently withdrew their applications for a CPP investment, a notable increase in the number of withdrawals observed during the preceding quarterly period.

*f. Results of Monthly Intermediation Snapshots and Lending Reports*

To measure lending and intermediation activities at financial institutions that have received funds through the CPP, Treasury initiated the Monthly Lending and Intermediation Snapshot (the "Snapshot") in January 2009. The monthly Snapshot covers lending and intermediation activities at the 21 QFIs receiving the largest amount

of capital under the CPP.[14] In addition to these efforts, Treasury also initiated a Monthly Lending Report (the "Report"), in March 2009, which is designed to provide insights into the lending and intermediation activities of all recipients of capital under the CPP, regardless of size. The Report surveys consumer and commercial loans outstanding for all financial institutions in the CPP.[15] During the quarterly period, Treasury released 3 new Snapshots, covering the period extending from February through April 2009, and two monthly lending Reports, covering the period from February through April 2009.[16] In addition to the releases described above, Treasury continues its work with banking regulators to obtain quarterly regulatory call report data on CPP participants. This data will be analyzed to determine changes in the balance sheets, loan provisioning, and intermediation activities of institutions in which TARP investments have been made. OFS will compare the activities of these institutions to equivalent data for comparable institutions that have not received TARP capital investments. The first report based on such quarterly call report data is planned for publication in July 2009.

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[14] These institutions, which accounted for half of outstanding depository institutions loans in December 2008, 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. Additional details regarding the Snapshot are available in the Oversight Board's prior quarterly report, which is available at: http://www.financialstability.gov/docs/FSOB/FINSOB-Qrtly-Rpt-033109.pdf.

[15] Under the Monthly Lending Report, CPP participants provide data to Treasury regarding: (1) average consumer loans outstanding; (2) average commercial loans outstanding; and (3) total loans outstanding which should be the sum of consumer and commercial loans outstanding. The category of consumer loans includes loans used for personal, family, or household uses including residential mortgages, home equity, U.S. credit card, and other consumer loans such as auto and student loans. The commercial loan category consists of loans for commercial and industrial purposes to sole proprietorships, partnerships, corporations, and other business enterprises, whether secured or unsecured, single payment, or installment.

[16] The Snapshots issued by Treasury during the quarterly period are available at: http://www.financialstability.gov/latest/tg_041509.html; http://www.financialstability.gov/latest/tg_05282009.html; and http://www.financialstability.gov/docs/surveys/SnapshotAnalysisApril2009.pdf.

The Reports issued by Treasury during the quarterly period are available at: http://www.financialstability.gov/latest/tg_05282009.html; and http://www.financialstability.gov/latest/tg_05282009.html.

### b. Term Asset-Backed Securities Loan Facility

The TALF is a component of the Consumer and Business Lending Initiative under the FSP that seeks to increase credit availability and promote economic activity by catalyzing the issuance of eligible consumer and business ABS at more normal interest rate spreads. During the quarterly period, several updates were announced in connection with the TALF program, as Treasury, working in conjunction with the Federal Reserve, continued to carefully consider and successively implement key expansions of the program.[17]

#### *i. Subscriptions during the quarterly period*

The TALF, which became operational in March, had three non-mortgage backed ABS subscriptions during the quarterly period in April, May and June. In the April subscription, $1.7 billion in loans were requested, representing a decrease from the $4.7 billion in loans requested in the first subscription held in March.[18] As in the March subscription, the collateral pledged to the facility in April included ABS backed by auto and credit card loans.[19] The amount of loans requested in May under the program increased substantially to $10.6 billion. Collateral for the May subscription included auto, credit card, student loan, small business, and equipment loans. In the June subscription, $11.5 billion in loans were requested under the TALF based on ABS backed by loans including auto, credit card, equipment, premium finance, servicing advances, small business, and student loans. Overall, the $23.9 billion in TALF loans extended during the quarterly period supported the issuance of $32.9 billion in ABS.

The first CMBS subscription also occurred during the quarterly period at the end of June, although no loans backed by such collateral were requested, which was expected given the relatively longer timeframe necessary to assemble CMBS transactions. Only newly-issued CMBS were eligible for this subscription (not legacy CMBS which will be included in CMBS subscriptions beginning in the month of July).

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[17] Detailed terms and conditions for the TALF are made available on the website of the Federal Reserve Bank of New York at: http://www.newyorkfed.org/markets/talf_terms.html.

[18] In both March and April, borrowing under the TALF was less than expected due to the difficulty that eligible borrowers encountered in working out the details of borrowing agreements with the primary dealers who are acting as the lending agents for the TALF. Furthermore, investors initially may have been reluctant to participate in the programs, but these concerns have apparently been allayed based on the higher levels of TALF borrowing that occurred in subsequent subscriptions.

[19] For more specific information on subscription results, please see http://www.newyorkfed.org/markets/talf_operations.html. Other ABS backed by eligible loans, including student, small business, equipment, floorplan and servicing advances, did not have any subscribers.

*ii. Revisions to Interest Rates and Maturities*

In April, Treasury and the Federal Reserve announced new interest rates applicable to the TALF, which became effective for the May TALF subscription. The new interest rates apply to fixed-rate TALF loans secured by ABS that do not benefit from a government guarantee and have weighted average life to maturity ("WALM") of less than two years. In order to better match the duration of the ABS collateral, the new rates are based on one- and two-year LIBOR swap rates. For TALF loans secured by ABS with a WALM of less than one year, the interest rate would be 100 basis points over the one-year LIBOR swap rate. For loans secured by ABS with a WALM of more than one year but less than two years, the interest rate would be set at the two-year LIBOR swap rate plus 100 basis points. The interest rate on loans secured by ABS with a WALM of two years or more would continue to be the three-year LIBOR swap rate plus 100 basis points. Generally, the interest rates on TALF loans are set at a rate low enough to provide investors with an incentive to purchase eligible ABS -- meaning the rates are lower than the rates that have prevailed in the current market environment -- but are still higher than rates that would be available under more normal market conditions in order to encourage a return to private financing as market conditions improve.

In May, the Federal Reserve, in consultation with the Treasury, authorized TALF loans with maturities of five years, beginning with the June subscription. Previously, only TALF loans with maturities of three years were authorized. TALF loans with five-year maturities are available, at the borrower's election, to finance purchases of CMBS and ABS backed by student loans or loans guaranteed by the Small Business Administration ("SBA"). The interest rate for fixed-rate five-year loans is 100 basis points over the five-year LIBOR swap. Under certain circumstances, some of the interest on collateral financed with a five-year loan would be diverted toward an accelerated repayment of the loan, especially in the latter two years, to ensure that the investor does not receive all of its principal back before the government is repaid. Currently, up to $100 billion of loans funded under the TALF may have five-year maturities.

*iii. Newly-Issued CMBS*

The market for CMBS, which accounted for almost half of new commercial mortgage originations in 2007, virtually ceased functioning by mid-2008. On May 1, 2009, newly-issued U.S. dollar-denominated, cash (not synthetic) CMBS issued after January 1, 2009, were included as TALF-eligible collateral in order to minimize defaults on economically viable commercial properties, facilitate the sale of distressed properties, and increase the capacity of current holders of maturing mortgages to make additional loans.[20] The collateral eligibility requirements pertaining to CMBS have been designed

[20] The subscription and settlement period for legacy and newly-issued CMBS will occur at the end of each month, while the periods for other types of eligible collateral will remain at the beginning of the month.

to protect the interests of taxpayers to the maximum extent possible. For example, to be eligible for the TALF --

- the CMBS must not be junior to other interests with claims on the same pool of loans and must entitle its holders to payments of both principal and interest (not just one or the other);

- the CMBS must represent an interest in a trust fund consisting of fully-funded, first-priority mortgage loans that are current in payment, at the time of the securitization, and not other CMBS, other securities, or interest rate swaps or cap instruments or other hedging instruments;

- the mortgage loans underlying the CMBS must be fixed-rate loans originated on or after July 1, 2008, on a fee or leasehold interest in one or more income-generating commercial properties located in the U.S. or one of its territories;

- the CMBS must have a credit rating in the highest long-term investment-grade rating category from at least two eligible rating agencies that is not based on a third-party guarantee, and the CMBS must not be rated below the highest investment-grade rating category by any eligible rating agency;[21]and

- for each CMBS with an average life that is five years or less, there is a collateral haircut of 15 percent, which represents the amount of risk born by the investor in the form of an equity investment. For CMBS with an average life between 5 years and 10 years (the maximum average life for eligible CMBS), the collateral haircuts will increase by one percentage point for each additional year of average life beyond 5 years.

*iv. Legacy CMBS*

On May 19, 2009, Treasury and the Federal Reserve further expanded the TALF to include certain high-quality, U.S. dollar-denominated, cash (not synthetic) legacy CMBS issued prior to January 1, 2009, representing the first time legacy assets were made eligible for inclusion as TALF collateral. The inclusion of legacy securities is intended to stimulate the extension of new credit by easing balance sheet pressures on banks and other financial institutions, as well as to improve liquidity and promote price discovery of these securities. Legacy CMBS is eligible for inclusion as collateral beginning in the July TALF subscription. As with other types of eligible collateral under the TALF, the terms and conditions under which Legacy CMBS will be accepted by the TALF are designed to protect the interests of taxpayers. For example, to be eligible for the TALF –

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[21] The eligible rating agencies for CMBS collateral include DBRS, Inc., Fitch Ratings, Moody’s Investors Service, Realpoint LLC and Standard & Poor’s.

- legacy CMBS, like newly-issued CMBS, may not be junior to other security interests in the underlying pool of commercial mortgages;

- legacy CMBS must entitle its holders to payments of both principal and interest (not interest or principal only) and each CMBS must bear interest at a pass-through rate that is fixed or based on the weighted average of the underlying fixed mortgage rates;

- legacy CMBS must represent an interest in a trust fund consisting of fully-funded mortgage loans and not other CMBS, other securities, or interest rate swap or cap instruments or other hedging instruments;

- the underlying mortgage loans on the legacy CMBS must be on a fee or leasehold interest in one or more income-generating commercial properties, and 95 percent of such properties must be located in the U.S. or its territories;

- TALF loans secured by legacy CMBS are subject to a collateral haircut against the current market price (rather than par value) of the CMBS. These haircuts for legacy CMBS, like for newly-issued CMBS, are 15 percent of par for CMBS with an average life of five years or less, with haircuts increasing by one percentage point of par for each additional year of average life beyond five years;[22]

- any remittance of principal on the CMBS must be used immediately to reduce the principal amount of the TALF loan in proportion to the original haircut and, under certain circumstances, some of the interest on legacy CMBS financed with three- or five-year TALF loans would be diverted toward an accelerated repayment of the loan; and

- legacy CMBS must have a credit rating in the highest long-term investment-grade rating category from at least two eligible rating agencies and legacy CMBS must not be rated below the highest investment-grade rating category from any eligible rating agency.

[22] The average life of a CMBS will be the remainder of the original weighted average life determined by its issuer, with certain adjustments.

*v. ABS Backed by Insurance Premium Finance Loans*

On May 1, 2009, securities backed by insurance premium finance loans also were made eligible for inclusion as collateral under the TALF, beginning with the June subscription. Each year, more than 1.5 million insurance premium finance loans enable small businesses to obtain property and casualty insurance. As a result of the previously described strain in the ABS markets, these loans have become more expensive and difficult for small businesses to obtain. The inclusion of insurance premium finance ABS as TALF-eligible collateral is meant to increase the availability credit to small businesses. The terms and conditions for ABS backed by insurance premium finance loans are generally similar to the terms and conditions for other eligible ABS classes that are not mortgage-backed, with some adjustments made to address the difference between asset classes. For example –

- only loans originated for purposes of paying premiums on property and casualty insurance are eligible as collateral for the TALF;
- the issuer must own the entire loan, not just a participation or beneficial interest;
- a back-up servicer obligated to service the loans is required to be included as part of the securitization if for some reason the initial servicer resigns or terminates;
- eligible premium finance ABS must have an average life of no more than five years; and
- haircuts for ABS backed by insurance premium finance loans range from 5 percent to 9 percent, increasing one percentage point for each extra year of average life between 1 and 5 years.

*vi. Potential Future Modifications*

In addition to all the changes described above, the Federal Reserve and Treasury continually monitor performance of TALF subscriptions and consider ways to update and improve operations under the TALF. The agencies are also evaluating whether to make any further additions to the types of securities eligible to collateralize TALF loans.

### c. Making Home Affordable and the Home Affordable Modification Program

The HAMP, which Treasury announced in February 2009, 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 broader economy.[23] The HAMP promotes 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.

#### *i. Program Updates*

Several important developments with respect to the HAMP occurred during the quarterly period as the program moved into the implementation phase following the March announcement of detailed guidelines. On April 13, the first Servicer Participation Agreement was signed and, as of the end of the quarterly period, 23 servicers, including the five largest servicers, had signed contracts and begun modifications under the program. Between loans covered by these servicers and loans owned or securitized by Fannie Mae or Freddie Mac, more than 80 percent of all loans in the country were covered by the HAMP as of June 30, 2009. At the end of the quarterly period, the 23 participating servicers had extended trial modification offers to more than 240,000 borrowers, with tens of thousands of trial plans underway. In July, those loans in the first cohort of trial plans are expected to become final modifications. The first modification incentive payments and the first public reporting on trial period plans and modifications are planned for August.

During the quarterly period, Treasury also announced details on a number of additional program features designed to increase program participation, enhance borrower affordability, and promote alternatives to foreclosure for borrowers who are unable to retain their homes through a HAMP modification. These initiatives will be funded under the original $50 billion of TARP funds allocated to the HAMP.

#### *ii. Second Lien Program*

On April 28, Treasury provided further details regarding the Second Lien Program, which offers incentives for second lien holders to modify or extinguish a second lien mortgage when a Home Affordable Modification has been initiated on the first lien mortgage for the same property. Given that as many as 50 percent of at-risk borrowers are estimated to have second lien mortgages, the Second Lien Program is

[23] The introduction of the HAMP was described in the Oversight Board's last quarterly report which included a detailed discussion of program guidelines released on March 4, 2009. The report is available at: http://www.financialstability.gov/docs/FSOB/FINSOB-Qrtly-Rpt-033109.pdf.

designed to reduce total monthly mortgage payments and enhance the affordability and sustainability of the first lien modification for a substantial subset of the HAMP-eligible population. The Second Lien program is designed to reach up to 1.5 million homeowners and Treasury expects to launch the program in late July or early August.

The Second Lien Program will be complementary to the core first lien modification program and, like the first-lien program under the HAMP, participation will be voluntary for servicers. Participating servicers will be required to use a pre-set protocol to automatically reduce payments on any second lien mortgage when a HAMP first lien modification has been initiated on the associated first lien mortgage. Modification of a second lien will not delay the modification of the first lien. Alternatively, servicers will have the option to extinguish the second lien in return for a lump sum payment under a pre-set formula determined by Treasury, allowing servicers to target principal extinguishment to borrowers where extinguishment is most appropriate.

The pay-for-success structure of the Second Lien Program is similar to the first lien modification program under the HAMP. Servicers will be paid $500 up-front for a successful modification and then success payments of $250 per year for three years, as long as the modified first loan remains current. Borrowers receive success payments of up to $250 per year for as many as five years, and these payments will be applied to pay down principal on the first mortgage.

*iii. Support for HOPE for Homeowners*

On April 28, Treasury announced plans to incorporate the Federal Housing Administration's ("FHA") HOPE for Homeowners program into the HAMP framework. HOPE for Homeowners provides borrowers with another option to help them achieve an affordable and sustainable monthly mortgage payment. In particular, because HOPE for Homeowners requires principal write-downs to help homeowners increase their equity, the program may offer a superior solution for many underwater borrowers who face heightened risks of foreclosure. Under the new initiative, servicers participating in the HAMP will be required to consider a HOPE for Homeowners refinancing in tandem with a HAMP trial modification. If a HOPE for Homeowners refinancing is feasible and offers a better outcome for both the borrower and the investor, the servicer will be required to offer the HOPE for Homeowners refinancing opportunity to the borrower. To encourage refinancing under the HOPE for Homeowners program, servicers and lenders who chose this option will be eligible for pay-for-success incentives similar to those available for modifications under the HAMP.

*iv. Home Price Decline Protection Incentives*

On May 14, Treasury issued additional details on Home Price Decline Protection ("HPDP") incentives, an additional program feature designed to increase the number of modifications made under the HAMP by addressing investor concerns that recent home price declines may persist. Under this feature, each successful modification of a first mortgage in a geographic area that has experienced home price declines will be eligible

for a HPDP incentive payment, up to an aggregate cap for HPDP incentives of $10 billion. HPDP incentive amounts will be calculated based on a formula incorporating: (1) declines in average local market home prices over recent quarters prior to the quarter in which the loan was modified (determined using housing price indices); and (2) the average price of a home in each particular market, since the potential loss due to a given rate of home price decline will be larger in higher cost areas. If the trial modification remains successful, 1/24th of the HPDP incentive payment will accrue to the lender or investor each month for up to 24 months. These payments will be made at the end of the first and second year of the modification. The payments will give lenders additional incentive to perform modifications even where home price declines have been most severe and lenders fear these declines may persist (thereby increasing their potential loss due to a subsequent default on the modified loan). In doing so, they will encourage servicers to undertake more modifications by assuring that incremental investor losses will be partially offset. Implementation of HPDP is planned for July.

*v. Foreclosure Alternatives for Eligible Borrowers*

During the quarterly period, Treasury also implemented foreclosure alternatives for eligible borrowers who are unable to retain their homes through a HAMP modification. On May 14, Treasury provided details on its Foreclosure Alternatives Program. The program offers incentives to encourage servicers, borrowers, and junior lien holders to pursue alternatives to foreclosure such as short sales and deeds-in-lieu of foreclosure. In a short sale, a servicer agrees to accept the proceeds from the sale of the property at its current value in full payment of the mortgage, even if the sale nets less than the total amount owed on the mortgage. In a deed-in-lieu, the borrower voluntarily transfers ownership of the property to the servicer, provided title to the property is free and clear.

When a borrower meets the eligibility requirements for the HAMP, but does not qualify for a modification or cannot maintain payments during the trial period or modification, the servicer may consider first a short sale, and if that is unsuccessful, a deed-in-lieu. Prior to proceeding to foreclosure, participating servicers must evaluate each eligible borrower to determine if a short sale is appropriate by considering, among other things, the property condition and value, the average marketing time in the community where the property is located, the condition of the title including the presence of junior liens, and whether the net sales proceeds are expected to exceed the investor's recovery through foreclosure.

To facilitate these types of transactions, the Foreclosure Alternatives Program will offer servicers up to $1,000 for successful completion of a short sale or deed-in-lieu for borrowers who met the basic eligibility criteria for HAMP, but were not offered a modification because the transaction failed the program's net present value ("NPV")

test.[24] The incentives can also be earned for short sales and deeds-in-lieu completed for borrowers who were unsuccessful in either a HAMP trial period or modification. In addition to servicer incentives, the Foreclosure Alternative Program will offer borrowers up to $1,500 to assist with relocation expenses. Treasury also will share the cost of paying junior lien holders to release their claims, matching $1 for every $2 paid to the lien holder, up to a total contribution of $1,000 by Treasury. Finally, because these are complex transactions involving careful coordination and close cooperation among a number of parties, the Foreclosure Alternative Program will simplify and streamline the process by providing a standard process flow, minimum performance timeframes, and standard documentation.

Eligible borrowers will be accepted into this program until December 31, 2012. Treasury is in the process of drafting and publishing streamlined and standardized documentation for these alternatives, including a Short Sale Agreement and an Offer Acceptance Letter. These documents will outline a specific set of standard terms that the industry can utilize, thereby reducing the complexity of these transactions and significantly facilitating the use of these options.

#### d. Public-Private Investment Partnership Program

To better support economic recovery and help financial institutions make new loans available to households and businesses, Treasury established the PPIP program in March 2009 as part of the FSP. The PPIP program is designed to improve the condition of financial institutions by facilitating the removal of legacy assets from their balance sheets. The PPIP program also should have the collateral effect of increasing the liquidity and functioning of the market for legacy assets. During the quarterly period, Treasury took steps to develop the key components of the PPIP program, which includes the Legacy Securities Program and the Legacy Loans Program.[25] The $75-$100 billion in TARP capital available to the PPIP program, when combined with capital and financing from private investors, and the potential for debt financing under the TALF, could generate as much as $1 trillion in purchasing power to buy legacy assets.

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[24] Servicers participating in the HAMP are required to apply a standardized NPV test on each eligible loan that is at least 60 days delinquent or at risk of imminent default. 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.

[25] Additional details regarding the PPIP program, including the terms for both the Legacy Loans Program and the Legacy Securities Program, are available at: http://www.financialstability.gov/roadtostability/publicprivatefund.html.

*i. Updates to the Legacy Securities Program*

Under the Legacy Securities Program or "S-PPIP," Treasury will partner with selected fund managers who raise a minimum of $500 million in private sector capital for public-private investment funds ("PPIFs"). The PPIFs may invest only in commercial mortgage-backed securities and non-agency residential mortgage-backed securities issued prior to 2009 that were originally rated AAA or an equivalent rating by two or more nationally recognized statistical rating organizations without ratings enhancement and that are secured directly by the actual mortgage loans, leases or other assets and not other securities ("Eligible Assets"). Treasury will invest equity capital in the PPIFs alongside private investors on a dollar-for-dollar basis and, in addition, fund managers may secure debt financing from Treasury in an amount up to 100 percent of the fund's total equity capital, subject to certain conditions.

During the quarterly period, Treasury released updated guidance on the Legacy Securities Program. Treasury selected pre-qualified fund managers on a holistic basis that met the following criteria, including --

- Headquartered in the United States;
- Demonstrated capacity to raise at least $500 million of private sector capital;
- Demonstrated experience investing in Eligible Assets, including through performance track records;
- Have a minimum of $10 billion of Eligible Assets under management; and
- Demonstrated operational capacity to manage PPIFs in a manner consistent with Treasury's stated investment objective while also protecting taxpayers.[26]

As of the close of the quarterly period, Treasury had received and reviewed 104 fund manager applications submitted prior to the application deadline for the program, which had been extended to April 24, 2009, to better accommodate increased interest in the program.[27] During the quarterly period, Treasury also established additional details

[26] The Term Sheet for the Legacy Securities Program is available at: http://www.treas.gov/press/releases/reports/legacy_securities_terms.pdf.

[27] On July 8, 2009, after the close of the quarterly period, Treasury announced that it had pre-qualified nine fund managers in the initial round of the program. Additional information on these selections and related actions will be provided in the Oversight Board's next quarterly report.

regarding the process that Treasury will use to evaluate and pre-qualify fund managers. This process, which was reviewed and considered by the Oversight Board, involved extensive review of applications by an evaluation committee, meetings with management, legal and operations due diligence and reference checks on all finalists, and completion of term sheets for Treasury's debt and equity investments in the PPIFs for all pre-qualified fund managers. Fund managers also underwent extensive due diligence of their governance, compliance and oversight policies and procedures and will be required to comply with the ethical standards and conflicts of interest rules Treasury will establish for selected S-PPIP fund managers.

Following pre-qualification, Treasury will perform additional confirmatory due diligence, including background checks and site visits, as well as complete definitive documentation with all pre-qualified fund managers. S-PPIP fund managers will have approximately 12 weeks to raise at least $500 million of private capital in the PPIF.[28] Treasury also will provide debt financing up to 100 percent of the fund's total equity capital. In addition, PPIFs will be able to obtain additional leverage through debt financing raised from private sector sources and, potentially, Legacy TALF, in which case Treasury will provide debt financing only up to 50 percent of the fund's total equity commitments and total indebtedness, subject to certain limits and covenants.

S-PPIP fund managers will retain discretion over the investments in areas such as selecting, purchasing, liquidating, trading and disposing of Eligible Assets, subject to general restrictions and investment guidelines outlined in the PPIF term sheets and definitive legal documentation. PPIFs are expected to pursue a long-term buy and hold strategy, may only invest in assets predominantly in the United States, and may only purchase Eligible Assets from financial institutions from which the Secretary of the Treasury may purchase assets pursuant to section 101(a)(1) of the EESA. Treasury will share pro rata any profits or losses alongside the private investor based on their respective equity capital investments. The term of a PPIF may be up to a maximum of 8 years, and may be extended for 2 additional 1 year periods with the consent of Treasury.

Treasury also has designed a robust set of conflicts of interest rules and ethical guidelines for the S-PPIP designed to protect taxpayers. In developing these requirements, Treasury researched best practices and received extensive outside feedback, including from the staff of the SIGTARP and the Federal Reserve. Treasury required S-PPIP fund manager applicants to identify all actual or potential conflicts of interest and propose how they would prevent or mitigate those conflicts. Treasury assessed each potential PPIP fund manager's responses and identified any deficiencies with respect to governance and conflicts mitigation controls. For those applicants selected as finalists, Treasury conducted due diligence to obtain additional information regarding governance and conflicts of interest issues, including information with respect to the proposed PPIF's: (i) internal audit methodology, accounting policies and

[28] Additional details regarding the types of financing available to PPIFs are provided in the Oversight Board's prior quarterly report, which is available at: http://www.financialstability.gov/docs/FSOB/FINSOB-Qrtly-Rpt-033109.pdf.

procedures and internal controls; (ii) mechanisms to identify, track, eliminate, mitigate, and monitor conflicts of interest; (iii) policies regarding affiliates, valuation, trade allocations and handling of material non-public/sensitive information; and (iv) Chief Compliance Officer's responsibilities, authorities and independence. Treasury benchmarked these responses across several key compliance and conflicts of interest metrics and then prepared follow-up due diligence questions for each finalist, as necessary. Finalists made in-person presentations to Treasury that provided additional opportunities for Treasury to seek more information.

This process allowed Treasury to develop conflicts of interest standards that will help ensure that the S-PPIP can protect taxpayers' interests while simultaneously attracting private capital and investment expertise to markets that have been substantially frozen for many months. All S-PPIP fund managers will be required to adopt, among others, the following provisions. S-PPIP fund managers may not, directly or indirectly, acquire assets from or sell assets to their affiliates or any other PPIF fund manager or private investor that has committed at least 10 percent of the aggregate private capital raised by such fund manager. Treasury will require each S-PPIP fund manager to invest a minimum of $20 million of firm capital in the PPIF they manage. S-PPIP fund managers must adopt policies and procedures that comply with the Investment Advisers Act of 1940 in all material respects. S-PPIP fund managers will also be required to maintain an independent compliance department that reports all positions in Eligible Assets (by PPIF and non-PPIF funds) to Treasury on an on-going basis. In addition, fund managers must submit regular monthly reports about assets purchased, assets disposed, asset values, and profits and losses. Treasury will require that all PPIFs maintain stringent policies related to the handling of material non-public information, personal trading, outside business affiliations, and the giving and accepting of gifts and entertainment. In addition, all key individuals of the S-PPIP fund manager must comply with an approved code of ethics and associated personal trading policy.

*ii. Updates to the Legacy Loans Program*

The FDIC and Treasury established the Legacy Loans Program to help remove troubled legacy loans from bank balance sheets by attracting private capital to purchase eligible legacy loans and other assets from participating banks through the use of FDIC debt guarantees and Treasury equity co-investments. This program would utilize PPIFs formed for the purpose of purchasing and managing pools of legacy loans and other assets held by U.S. banks and savings associations. The Oversight Board's prior quarterly report provides an overview of the initially proposed structure and terms of the Legacy Loans Program.

The FDIC requested public comment on the Legacy Loans Program and the comment period closed during the quarterly period on April 10, 2009. The FDIC received over 400 comments which are available on its website. These comments will be taken into account in connection with the development and implementation of the Legacy Loan Program. Treasury continues to work with the FDIC to establish standardized

procedures for the governance of Legacy Loan PPIFs including the management, servicing, financial and operation reporting requirements, and exit timing for such PPIFs.

On June 3, 2009, a planned pilot sale of legacy assets was postponed, at least partially due to the fact that banks had been successful raising capital without removing legacy assets from their balance sheets through the use of PPIFs. As a result, Treasury and FDIC and other banking supervisors planned to reevaluate the next steps for the Legacy Loans Program. The FDIC also announced that it plans to test the funding mechanism contemplated by the program in a sale of receivership assets during the summer of 2009.

### e. Automotive Industry Financing Program

#### *i. Automotive Industry Finance Program*

The Treasury established the 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 companies' expenditures and requirements relating to corporate governance.

Since the establishment of this program, Treasury has provided loans and other sources of funding to GM, GMAC, Chrysler, and Chrysler Financial, to enable these companies to implement restructuring plans and to prevent a disorderly bankruptcy.[29] In connection with these efforts, during the last quarterly period, Treasury made available to GM and Chrysler $36.5 billion and $8.8 billion, respectively, of loans under the AIFP, a portion of which has not yet been drawn.

As detailed in the previous quarterly report, the Presidential Task Force on the Auto Industry ("Auto Task Force"), established by Treasury and the National Economic Council, set a deadline of June 1, 2009, for GM to complete a more significant operational and financial restructuring.[30] To assist that restructuring, Treasury agreed to provide GM additional funding for continued operations until that date, funding a $2 billion loan on April 22, 2009, and a $4 billion loan on May 20, 2009. In addition, the Auto Task Force set a deadline of May 1, 2009, for Chrysler to enter into a binding deal with Fiat, a European automobile manufacturer, and submit a viable business plan for the alliance. In connection with that deadline, Treasury agreed to provide additional funding

[29] Additional details on the amounts and terms of the assistance provided by the TARP to these companies are available at: http://www.financialstability.gov/roadtostability/autoprogram.html.

[30] The Oversight Board's previous quarterly report is available at: http://www.financialstability.gov/docs/FSOB/FINSOB-Qrtly-Rpt-033109.pdf.

to Chrysler for continued operations until that date. Although Treasury committed to provide Chrysler $500 million in loans for these purposes, on April 29, 2009, ultimately these funds were not required.

On April 30, 2009, Chrysler announced its alliance with Fiat, and filed for Chapter 11 bankruptcy. Treasury committed to provide a $3 billion loan to Chrysler in its capacity as debtor-in-possession ("DIP"). Treasury increased its commitment in the DIP credit agreement by $800 million to $3.8 billion on May 20, 2009, of which it ultimately funded $1.9 billion. Subsequently, on June 1, 2009, a bankruptcy judge approved Chrysler's restructuring proposal, including the alliance with Fiat and the sale of assets to a newly-formed entity, Chrysler Group LLC ("new Chrysler").[31] The asset sale was finalized on June 10, 2009, and Treasury committed to provide new Chrysler a loan of up to $7.1 billion, which consists of new debt obligations of approximately $6.6 billion, and assumed debt of $500 million from Treasury's January 2, 2009, credit agreement with Chrysler. The debt obligations will be secured by a first priority lien on the assets of new Chrysler. In addition, Treasury obtained a 9.9 percent equity interest in new Chrysler and an additional note.

To complement the package of support provided to Chrysler, and to prevent interruptions in the wholesale and retail funding markets for Chrysler dealers and consumers, Treasury invested $7.5 billion in mandatorily convertible preferred interests in GMAC to support GMAC's ability to originate new loans to Chrysler dealers and consumers, as well as to help address GMAC's capital needs as identified through the Supervisory Capital Assessment Program.

During the quarterly period, GM also filed for a Chapter 11 bankruptcy, on June 1, 2009. In connection with that filing, on June 3, 2009, Treasury committed to provide a $30.1 billion DIP loan to GM. In addition, if the bankruptcy court approves GM's restructuring proposal, Treasury will exchange its prior loans to GM (including the amount of the DIP loan that is not assumed by the new GM or left for the old GM as it winds down in bankruptcy and the $19.4 billion in pre-bankruptcy funding) for approximately $7.1 billion of debt (the amount of the DIP loan assumed by the new GM), $2.1 billion in preferred stock in the new GM, and approximately 61 percent of the equity in the new GM that would be formed as a result of the restructuring.[32] The portion of the Treasury DIP financing from the Treasury that remains for old GM is approximately $986 million. At this time, Treasury does not plan to provide additional assistance to GM beyond this commitment.

[31] A Chrysler-Fiat Alliance Fact Sheet is available at: http://www.financialstability.gov/docs/AIFP/Chrysler-restructuring-factsheet_043009.pdf.

[32] Subsequently, on July 5, 2009, a bankruptcy court judge approved GM's restructuring proposal, including the sale of certain assets to a newly formed entity ("new GM"). The asset sale was finalized on July 10, 2009.

*ii. Warranty Commitment Program*

During the quarterly period, Treasury provided a $280 million loan to Chrysler on April 29, 2009, and a $360 million loan to GM on May 27, 2009, to finance their participation in the previously announced Warranty Commitment Program. The Warranty Commitment Program is designed to give consumers of domestic autos the confidence that warranties on those cars will be honored regardless of the outcome of the current restructuring process.[33]

### f. Executive Compensation

On June 15, Treasury issued its Interim Final Rule on TARP Standards for Compensation and Corporate Governance. The Interim Final Rule implements and expands upon Title VII of ARRA, which amended the EESA executive compensation provisions. The Interim Final Rule has three key components: (i) standards for executive compensation for certain executives and highly compensated employees at firms receiving TARP assistance; (ii) the appointment of a Special Master for TARP Executive Compensation, to ensure that compensation arrangements are consistent with the public interest; and (iii) corporate governance standards designed to improve accountability and disclosure at firms receiving TARP assistance. The Interim Final Rule aims to protect taxpayer investment through the TARP and maximize value for the firm's shareholders, including the government. The key components of the Interim Final Rule are as follows:

*i. Standards for Executive Compensation for Companies Receiving TARP Assistance:*

- ***Limits Bonus, Incentive and Retention Payments to Senior Executive Officers and Highly Compensated Employees***: The new regulation limits bonuses paid to certain employees – the senior executive officers, who are the "named executive officers" identified in the company's annual compensation disclosures, and a specified number of the most highly compensated employees to one-third of total compensation, and requires that such bonuses be paid in the form of long-term restricted stock, implementing the provisions passed by Congress.[34] The number of most highly compensated employees covered by the bonus limitation depends upon the amount of financial assistance the company has received under TARP. At the same time, the rule permits firms to pay salary in the form of stock, aligning executives' incentives with those of shareholders and taxpayers.

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[33] Additional details on the Warranty Commitment Program are available in the Oversight Board's previous quarterly report.

[34] The Interim Final Rule defines "most highly compensated" employees according to their total annual compensation for the last completed fiscal year, as calculated under the federal securities laws, in order to accurately reflect the amounts earned by these employees each year.

  - ***Prevents Abuse of the Exemption for Commissions*:** Although the rule contains an exception from the bonus limitation for payments of certain types of "commissions," as required by ARRA, the rule also minimizes the potential for abuse of the exception, limiting commissions to amounts payable under programs similar to commission programs already in place as of February 17, 2009. At firms receiving "exceptional assistance" under TARP, these payments and compensation structures for executives and the most highly compensated employees also will be subject to review by the newly appointed Special Master for TARP Executive Compensation (see below).

- ***Curtails the Payment of "Golden Parachutes."*** ARRA expanded the original EESA's limits on golden parachutes, requiring a prohibition on any golden parachute payment to a senior executive officer or any of the next 5 most highly compensated employees. While ARRA limited the definition of golden parachutes to payments for an employee's departure for any reason, the Interim Final Rule also targets another common golden-parachute practice by including as a golden parachute payment any payment made in connection with a change in control of the company.

- ***Imposes a Clawback for Any Bonus Based on Materially Inaccurate Performance Criteria***. Although the original EESA required a clawback provision applicable only to amounts paid to senior executive officers, ARRA mandates that bonuses paid to senior executive officers and the next 20 most highly compensated employees be subject to a clawback if the payment was based on materially inaccurate performance criteria. The Interim Final Rule also requires that the TARP recipient actually exercise its clawback rights in such a case unless the TARP recipient can demonstrate that it would be unreasonable to do so (for example, by showing that the expense of enforcing the clawback right exceeds the amount that could be recovered).

- ***Prohibits Tax Gross-Ups:*** As an additional standard beyond the statutory requirements, the rule prohibits the payment to senior executive officers and the next 20 most highly compensated employees of a tax "gross-up," or a payment to cover taxes due on compensation such as golden parachutes and perquisites.

ii. *Appointment of a Special Master for TARP Executive Compensation:*

- The Interim Final Rule provides for the appointment of a Special Master for TARP Executive Compensation ("Special Master"). The Special Master will be responsible for the review of proposed compensation structures arrangements for senior executive officers, executives officers, and the 100 most highly compensated employees of institutions that have received "exceptional assistance" through the TARP. Companies receiving "exceptional" financial assistance for purposes of the Interim Final Rule include those participating in the following programs: the Systemically Significant Failing Institutions Program, the Targeted Investment Program, the Asset Guarantee Program, and the Automotive Industry Financing Program. These TARP recipients currently include: AIG, Citigroup, Bank of America, Chrysler, GM, GMAC, and Chrysler Financial. The Special Master's responsibilities include:

  - ***Review and Approval of Payments:*** At firms receiving exceptional assistance, the Special Master must review and approve any compensation proposed to be paid to any employee subject to ARRA's bonus restrictions (generally for these firms, the 5 senior executive officers and 20 next most highly paid employees). If the Special Master finds that the compensation proposed for covered employees is excessive, inappropriate, or designed to encourage unsound risk-taking, the Special Master has the authority to disapprove the arrangement and require the company to resubmit its proposal, taking account of the deficiencies found by the Special Master.

  - ***Review and Approval of Compensation Structure for Executive Officers and the 100 Most Highly Paid Employees:*** At firms receiving exceptional assistance, the Special Master also must review and approve the structure of the overall compensation package for executive officers and the 100 most highly paid employees that are not subject to the bonus restrictions of the EESA (as amended by ARRA).

  - ***"Safe Harbor" Guidance on Compensation Payments and Structures***: Consistent with Treasury's February 4, 2009, guidance on executive compensation at TARP recipients, the Special Master will automatically approve proposed compensation to employees of TARP recipients receiving exceptional assistance so long as the employee's total annual compensation is not more than $500,000, with any additional compensation paid in the form of long-term restricted stock. Providing recipients with a clear "safe harbor" rule will encourage TARP recipients to use compensation structures that link compensation to long-term firm value.

- ***Negotiation of Reimbursements for Taxpayers***: The Special Master will also, consistent with the requirements of ARRA, oversee the review of bonuses, retention awards, and other compensation paid before February 17, 2009, by TARP recipients to determine whether such payments were contrary to the purposes of section 111 of EESA, the TARP, or were otherwise contrary to the public interest, and seek to negotiate appropriate reimbursements.

- ***Guidance on Long-Term Compensation Reform:*** The Interim Final Rule gives the Special Master interpretive authority over the meaning of the Interim Final Rule. Recognizing that compensation best practices will continue to evolve, the Interim Final Rule authorizes the Special Master to publish advisory opinions indicating whether particular payments or structures are consistent with ARRA, the rule, and the public interest.

- ***Principles Guiding Special Master Determinations:*** The Interim Final Rule sets out general principles for the Special Master to use in determining whether the companies receiving exceptional assistance have designed executive compensation to maximize shareholder value and protect taxpayer interests. The following briefly summarizes those principles:

  - ***Risk***: Compensation should avoid incentives that reward employees for short-term or temporary increases in value that may not ultimately result in an increase in the long-term value of the entity;

  - ***Taxpayer Return***: Compensation should reflect the need for the entity to remain a competitive enterprise and ultimately repay its TARP obligations;

  - ***Appropriate Allocation***: Compensation should be appropriately allocated among each element of pay (*e.g.* salary, short- and long-term incentive pay, and current and deferred compensation or retirement pay);

  - ***Performance-Based Compensation***: Compensation should be performance-based, and determined through tailored metrics that encompass individual performance and/or the performance of the entity or relevant business unit;

  - ***Comparable Payments***: Compensation should be consistent with, and not excessive in comparison to, pay for those in similar roles at similar entities; and

- ***Employee Contribution***: Compensation should reflect the current or prospective contributions of the employee to the value of the TARP recipient.

iii. *Standards for Corporate Governance and Disclosure:*

- The Interim Final Rule also implements the corporate governance provisions in ARRA and expands upon those provisions by setting forth additional governance standards required by Treasury. The rule addresses the need for shareholders and directors to work together to ensure that compensation practices at TARP recipients are reformed over the long term. These rules include the following:

  - ***"Say on Pay":*** Consistent with Treasury's February 4, 2009, proposals, ARRA requires that TARP recipients provide an annual shareholder vote on a non-binding resolution to approve executive compensation packages. The Interim Final Rule requires each TARP recipient to permit such a vote in accordance with any applicable regulations or guidance promulgated by the SEC.

  - ***Compensation Risk Assessments:*** The original EESA included a requirement that compensation arrangements for senior executive officers be limited to avoid incentives for unnecessary risk-taking, and ARRA expanded that provision to require that no employee compensation arrangement encourage the manipulation of earnings. The new rule expands upon those important provisions by requiring that the compensation committee of each TARP recipient provide a narrative explanation for its analysis of these matters, allowing shareholders to understand and evaluate directors' reasoning with respect to the risks presented by compensation arrangements.

  - ***Luxury Expenditure Policies:*** The rule implements ARRA's requirement that the board of directors of each financial institution establish a company-wide policy on luxury or excessive expenditures. To help ensure that the top executives of each company monitor these types of expenditures, the rule also requires that the Chief Executive Officer and the Chief Financial Officer of each TARP recipient certify that any expenditure requiring the approval of the board of directors, or a senior executive officer, or any executive officer of a substantially similar level of responsibility was properly approved, and requires that the policy mandate prompt internal reporting of any violations of the policy.

  - ***Additional Disclosure of Perks:*** The Interim Final Rule expands upon the SEC's disclosure requirements by requiring each TARP recipient to disclose any perquisites provided to any employee subject to ARRA's bonus limitations with total value exceeding $25,000. These firms will

also be required to provide a narrative description of, and justification for, the benefit. (Existing SEC rules only require disclosure of perquisites to the top five named executive officers of the company.) The expanded disclosure and narrative requirements of the Interim Final Rule are intended to enable the owners of each TARP recipient to better understand why directors have provided perquisites to employees — and whether these perquisites are likely to maximize shareholder value.

- ***Disclosure of Compensation Consultants:*** In light of the extensive involvement of compensation consultants in setting pay for top executives, the rule requires TARP recipients to disclose whether the company or its compensation committee engaged a compensation consultant. In order to give shareholders a clearer sense of the consultant's influence over pay and any possible conflict of interest, the rule requires TARP recipients to provide a narrative description of the services provided by any such consultant, including any non-compensation-related services provided by the consultant or any of its affiliates, as well as a description of any use of "benchmarking" procedures in the consultant's analysis.

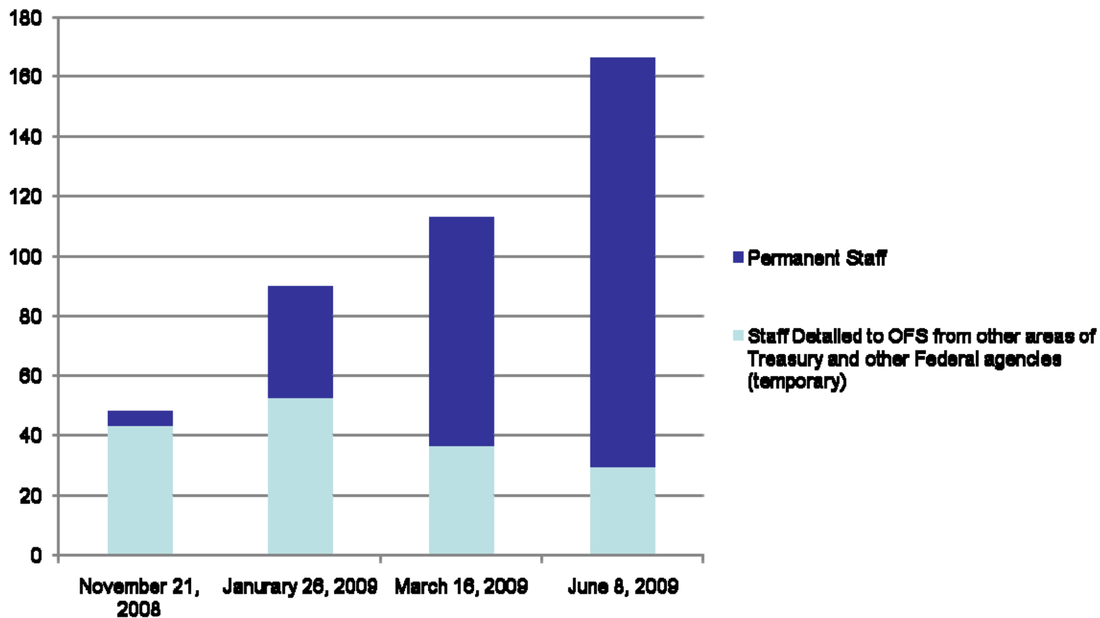
### g. Administrative Activities of the Office of Financial Stability

The Oversight Board has continued to review and monitor the progress made by Treasury's Office of Financial Stability in ensuring that the necessary infrastructure is in place to design and implement all programs established under EESA. This includes hiring staff and establishing the necessary infrastructure, internal controls, and compliance and monitoring programs for the TARP. The following outlines the progress that OFS has made in the areas of staffing, procurement, reporting, and internal controls during the quarterly period.

#### *i. Staffing*

The OFS continues to make significant progress in hiring staff to design and execute TARP programs. As of June 8, 2009, Treasury has increased the number of permanent OFS staff to 137; this is a 78 percent increase in the number of permanent staff reported in the last quarterly report. The number of staff detailed to OFS from other areas of Treasury and other Federal agencies continues to fall. Specifically, the number of staff detailed to OFS fell from 36 to 29, as of June 8, 2009; this is a 19 percent drop in the number of staff detailed to OFS. These figures are illustrated in the chart below (figure 23).

Figure 23




Treasury anticipates that the OFS will need 225 full-time employees to operate at full capacity in fiscal year 2010. Treasury will continue to utilize a combination of permanent staff and detailees to best support the implementation of TARP and FSP.

*ii. Procurement*

Treasury continues to utilize private sector expertise to support the execution of TARP and FSP programs. For example, during the quarterly period, Treasury continued to engage private sector firms to assist with the significant volume of work associated with the TARP in the areas of accounting and internal controls, administrative support, facilities, legal advisory, financial advisory, and information technology.

Treasury awarded five new contracts during the quarterly period. Treasury retained the firms of Simpson Thacher & Bartlett, LLP and Anderson, McCoy, & Orta, LLP for legal services relating to the PPIP program. Treasury retained the services of The Boston Consulting Group for management consulting in relation to the AIFP. Treasury also awarded contracts to Herman Miller and American Furniture Rental for office furniture. In June, Treasury increased the ceiling value maximum order amount allowable under the Auto-Industry Participant Investment Legal Services contract for the Chrysler and GM bankruptcy litigations; the three contractors impacted by the change are Sonneschein, Nath & Rosenthal; Cadwalader, Wickersham & Taft LLP; and Haynes and Boone. In addition to contracts, during the quarterly period, Treasury awarded three new financial agency agreements for asset management services with the firms AllianceBernstein, L.P., FSI Group, LLC, and Piedmont Investment Advisors, LLC.

On January 21, 2009, Treasury published an interim final regulation designed to address actual or potential conflicts of interest among contractors and financial agents

performing services in conjunction with 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 contracts' terms. The comment period for the interim final Conflict of Interest Regulation ended on March 23, 2009, and OFS's Risk and Compliance Office is currently analyzing the public comments received and will amend the rule, as appropriate, after the review is complete.

Conflict issues that arise with new and existing contracts and financial agent agreements are principally handled through the OFS's Risk and Compliance Office. When a potential conflict does arise in an existing contract or financial agent agreement, OFS's Risk and Compliance Office takes a standard approach to evaluating the potential conflicts of interest and feasibility of mitigation measures.

The OFS is actively renegotiating the contracts that were in place before the new Interim Final Conflict of Interest regulation became effective on January 21, 2009, and that remained active after April 30, 2009. As of June 25, 2009, Treasury has renegotiated the conflicts of interest provisions and approved the conflicts mitigation plans for four of the eight contracts that required these modifications. Treasury is conducting regular meetings with the remaining four contractors to incorporate the appropriate modifications and expects to complete this process by July 31, 2009.

The OFS has discussed the process for formal conflict of interest inquiries with most of its contractors and financial agents. The OFS's Risk and Compliance Office documents and tracks all formal decisions on conflict of interest inquiries. As of June 25, 2009, OFS's Risk and Compliance Office has held a training session on the conflicts of interest inquiry processes and will issue written guidance on the conflicts of interest inquiry processes, and communicate this process to contractors and financial agents.

*iii. Reporting*

Treasury is committed to transparency in all of the TARP programs and improving its external communications about those programs. In this regard, Treasury has met all of its EESA-mandated reporting requirements on time since the establishment of TARP. Treasury makes all of its reports, which detail the objectives, structure, and terms of each TARP program and investment, available on its web site (*www.financialstability.gov*) and shares these reports with Congress and other oversight bodies.

As of June 25, 2009, Treasury had filed:

- 55 transactions reports, in accordance with section 114 of the EESA, which include key details of the acquisition and, beginning March 31, 2009, the disposition of TARP investments;

- 7 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

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

In addition to transactions, tranche, and monthly reports, Treasury also reports the lending activities of banks that have received a Treasury investment through the CPP. As of June 25, 2009, Treasury had released:

- 5 monthly bank Lending and Intermediation Surveys and Snapshots, which detail lending activities of the top 21 recipients of CPP investment. The survey includes data on consumer and commercial lending, including loans to small businesses; and

- 2 monthly Lending Reports, which detail the consumer and commercial lending activities of all CPP investment recipients.

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, speeches, and briefings to Congressional staff. Treasury, working with its partners, will also hold informational events for homeowners throughout the country on the Making Home Affordable Program.

*iv. Governance and Internal Controls*

During the quarterly period, OFS continued to build-out the system of internal controls across all program areas. This expansion includes the development of a broad set of draft policies and procedures by management with support from PricewaterhouseCoopers and Ernst & Young. The draft policies include the control objectives as determined by management, and the draft procedures include the control techniques used to achieve the control objectives.

The OFS continues to execute an integrated plan to meet the requirements of the Federal Managers' Financial Integrity Act ("FMFIA"), OMB Circular A-123, Appendix A, Internal Control Over Financial Reporting, the Federal Financial Management Improvement Act ("FFMIA"), and other federal statutes and directives. This integrated plan includes the following four phases: (1) planning and scoping; (2) documenting and testing significant business processes and IT internal controls; (3) transforming testing and assessment results into actionable risk mitigation strategies; and (4) monitoring those

risk-mitigation strategies and validating their effectiveness. The OFS internal control program is built to address the complex environment inherent in TARP business activities. OFS will continue to identify and correct weaknesses in a timely manner.

The OFS coordinates internally across offices to provide advice to the OFS business programs, as well as to TARP-related Financial Agents on the appropriate design of risk-mitigation techniques, including appropriate internal control design throughout the business lifecycle (program design, execution, and closing). Additionally, the ICPO is rolling out a near real-time evidence collection capability utilizing a document repository to further enhance the oversight and effectiveness of control execution. Such steps reflect Treasury's commitment to creating and maintaining a robust and effective internal control program with regard to the design and implementation of TARP programs.

# APPENDIX A

Minutes of Financial Stability Oversight Board Meetings
During the Quarterly Period

# Minutes of the Financial Stability Oversight Board Meeting
# April 6, 2009

A meeting of the Financial Stability Oversight Board ("Board") was held at 4:00 p.m. (EDT) on Monday, April 6, 2009, at the offices of the Federal Housing Finance Agency ("FHFA").

MEMBERS PRESENT:

Mr. Bernanke, Chairperson
Mr. Geithner
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 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. Morse, Chief Counsel, Office of Financial Stability, Department of the Treasury

Ms. Aveil, Special Assistant to the Secretary, Department of the Treasury

Ms. Liang, Associate Director, Division of Research & Statistics, Board of Governors of the Federal Reserve System

Mr. Oliner, Senior Advisor, Division of Research & Statistics, Board of Governors of the Federal Reserve System

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

Mr. Herold, Deputy General Counsel, Department of Housing and Urban Development

Mr. Daly, Assistant General Counsel, Department of Housing and Urban Development

Ms. Nisanci, Chief of Staff, Securities and Exchange Commission

Mr. Becker, General Counsel and Senior Policy Director, Securities and Exchange Commission

Mr. Sirri, Director, Division of Trading and Markets, 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 4:05 p.m. (EDT).

The Board first considered draft minutes for the meetings of the Board held on February 25, March 1, and March 19, 2009, which had been circulated in advance of the meeting. Upon a motion duly made and seconded, the Members unanimously voted to approve the minutes of such meetings, subject to such technical revisions as may be received from the Members.

Using prepared materials, officials from the Department of the Treasury ("Treasury") then provided the Board with a briefing on recent initiatives and actions taken by Treasury under the Troubled Asset Relief Program ("TARP"), the current level of funding of TARP programs, and the administrative activities of the Office of Financial Stability.

Using prepared materials, Treasury officials first reviewed and discussed with the Members the terms, conditions and timing of the key components of the Public-Private Investment Partnership ("PPIP") program announced by Treasury on March 23, 2009. The PPIP program is designed to draw new private capital into the market for legacy assets through the provision of government equity co-investment and public-supported financing and thereby help repair the balance sheets of financial institutions that hold legacy assets and restore liquidity to the market for such assets. This discussion initially focused on the legacy securities component of the PPIP program, through which public-private investment funds ("PPIFs") may acquire legacy securities, such as residential or commercial mortgage-backed securities, from U.S. financial institutions. Such PPIFs would be capitalized through equal equity investments by private investors and Treasury, and would have the ability to obtain debt financing from Treasury or potentially the Term Asset-Backed Securities Loan Facility ("TALF"). Members and officials discussed, among other things, the applications process and selection criteria for prospective PPIF managers, the types of legacy securities that may be acquired by PPIFs, the anticipated timeline for implementation of the legacy securities program, and the terms and conditions (including warrant requirements) that may be applied to fund managers and PPIFs.

The briefing and discussion then turned to the terms, conditions and timing of the legacy loans component of the PPIP program, which will be operated by the Treasury and the Federal Deposit Insurance Corporation ("FDIC"). Under this component of the PPIP program, individual PPIFs will be formed to acquire legacy loans from banking organizations. Such PPIFs would be capitalized by private investors and potentially Treasury, and would have the ability to issue debt backed by FDIC-provided guarantees. Members and officials discussed, among other things, the nature and scope of involvement of Treasury and the FDIC in the legacy loan

program, the process for identifying pools of loans for purchase, the potential timing of implementation of the program, and the status of the FDIC's notice and comment rulemaking with respect to the legacy loan program. Members also discussed the potential impact of recently implemented changes to accounting standards on the PPIP program.

Members and officials then discussed the status of, and recent developments concerning, the TALF. For example, officials noted that the first subscription under the TALF was funded on March 25, 2009, with approximately $4.7 billion in loans being provided in support of the issuance of approximately $8.3 billion in consumer-related asset-backed securities ("ABS"), and that the second monthly subscription period was scheduled for April 7, 2009. Members also reviewed and discussed, among other things, the expansion of ABS asset classes eligible for financing under the TALF announced on March 19, 2009, and the potential for the TALF to be expanded both in terms of maximum dollar volume and eligible asset classes, such as recently issued or legacy residential and commercial mortgage-backed securities.

Using written materials, Treasury officials and Members also reviewed and discussed the Automotive Industry Financing Program ("AIFP") and the recent actions taken under the program to assist the domestic automotive industry in becoming financially viable. For example, Members and officials discussed the findings of the Presidential Task Force on the Auto Industry ("Auto Task Force") with respect to the restructuring plans submitted by General Motors Corp. ("GM") and Chrysler Holding LLC ("Chrysler") on February 19, 2009, and the potential for additional financing to be provided to these companies under the existing loan agreements while they pursue restructuring plans consistent with the goals and conditions set by the Auto Task Force.

Treasury officials then briefed the Members regarding the Auto Supplier Support Program ("ASSP") announced on March 19, 2009, which is designed to provide qualified automotive supply companies with financial protection on the receivables owed to these companies by domestic auto manufactures, and to provide auto supply companies with immediate access to liquidity. Treasury officials reviewed with the Members the key terms under which Treasury would make up to $5 billion in loans to special purpose vehicles ("SPVs") established by GM and Chrysler. The SPVs would then use the proceeds of these loans to purchase receivables from participating auto suppliers identified by GM and Chrysler. As part of this discussion, Members discussed ways that Treasury might be able to monitor which auto suppliers are selected by GM and Chrysler to participate in the program.

Treasury officials also briefed the Members concerning the Warranty Commitment Program announced by Treasury on March 30, 2009, which is designed to give consumers who are considering new car purchases from GM and Chrysler confidence that the warranties offered by these manufacturers will be honored during the finite period during which GM and Chrysler are pursuing restructurings that are consistent with the goals and conditions set by the Auto Task Force.

Treasury officials then provided the Members with an update concerning the Unlocking Credit for Small Businesses program announced by Treasury on March 16, 2009. Members and officials discussed, among other things, the terms under which Treasury may purchase securities backed by guaranteed portions of loans made under the 7(a) loan program established by the Small Business Administration ("SBA"), and first-lien mortgage securities made by private-sector lenders in connection with SBA's 504 community development loan program. As part of this discussion, Members also discussed the potential for using the TALF to help support the markets for these types of loans.

Treasury officials then provided the Members with an update regarding the Home Affordable Modification Program ("HAMP") announced by Treasury in February 2009. As part of this discussion, Treasury officials noted the progress being made by Treasury, in conjunction with HUD, FHFA and the Federal banking agencies, among others, in developing the HAMP and related guidelines, protocols and procedures.

Using prepared materials, Treasury officials then provided the Members with an update on the capital purchase program ("CPP"). Members and officials discussed, among other things, the number of applications received and approved by Treasury under the CPP, as well as the amount of funds requested, disbursed, and received or expected to be received by Treasury under the program. Members and officials also discussed the steps taken by Treasury to monitor the lending and intermediation activities of recipients of TARP funds; the results of Treasury's monthly lending and financial intermediation snapshots; and the work being conducted by Treasury, 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 and bank holding companies.

Members and officials then reviewed and discussed Treasury's progress in hiring staff, establishing a system of internal controls, and monitoring contractors and agents for the Office of Financial Stability. In addition, Members discussed the recent legislative changes to executive compensation restrictions applicable to TARP recipients, which resulted from the passage of the American Recovery and Reinvestment Act of 2009 ("ARRA"), and the steps being taken by Treasury to develop new guidelines that would implement these restrictions and harmonize these restrictions to the extent possible with the executive compensation guidance previously proposed by Treasury.

Treasury officials then provided the Members with a briefing and update regarding the financial commitments entered into by the Treasury under the TARP, including the aggregate amount of commitments and disbursements under the each TARP program and the resources that remain available under the TARP.

Using written materials prepared by various agencies represented on the Board, the Members then engaged in a roundtable discussion regarding the current state of the U.S. housing and financial markets. Members and officials discussed, among other things, the

difficulty of isolating the beneficial effects of Treasury's actions under the TARP 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. As part of this discussion, Members and officials reviewed and discussed a variety of financial market data, including data related to short-term borrowing costs, conditions in the commercial paper and ABS markets, credit default swap spreads for selected financial institutions, as well as data related to credit demand and standards drawn from the Federal Reserve's Senior Loan Officer Opinion Survey. In considering the state of the housing and housing finance markets, Members and officials reviewed, among other things, data related to mortgage rates, housing prices, home starts and sales, housing inventory, and delinquency rates. During this discussion, Members also considered and discussed liquidity issues in the market for mortgage lending.

Members and officials then engaged in a discussion regarding the Board's quarterly report to Congress for the quarter ending March 31, 2009, that will be issued by the Board pursuant to section 104(g) of the EESA. Members and officials discussed, among other things, the timing and potential contents of the report.

The meeting was adjourned at approximately 5:25 p.m. (EST).

[Signed Electronically]

Jason A. Gonzalez
Secretary

# Minutes of the Financial Stability Oversight Board Meeting
# May 28, 2009

A meeting of the Financial Stability Oversight Board ("Board") was held at 4:00 p.m. (EDT) on Thursday, May 28, 2009, at the offices of the Board of Governors of the Federal Reserve System ("Federal Reserve").

MEMBERS PRESENT:

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

STAFF PRESENT:

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

AGENCY OFFICIALS PRESENT:

Mr. Allison, Counselor to the Secretary and Nominee for Assistant Secretary of the Treasury for Financial Stability, Department of the Treasury

Ms. Abdelrazek, Senior Advisor to the Counselor to the Secretary and Nominee for Assistant Secretary of the Treasury for Financial Stability, Department of the Treasury

Mr. Wheeler, Deputy Assistant Secretary for Federal Finance, Department of the Treasury

Mr. Madison, Nominee for General Counsel, Department of the Treasury

Ms. Schaffer, Assistant General Counsel for Banking and Finance, Department of the Treasury

Mr. Lambright, Chief Investment Officer, Office of Financial Stability, Department of the Treasury

Mr. Rattner, Lead Advisor to the Secretary on the Automotive Industry and Member of the Presidential Task Force on the Automotive Industry, Department of the Treasury

Ms. Aveil, Special Assistant to the Secretary, Department of the Treasury

Mr. Wilcox, Deputy Director, Division of Research & Statistics, Board of Governors of the Federal Reserve System

Mr. Foley, Senior Advisor, Division of Banking Supervision and Regulation, Board of Governors of the Federal Reserve System

Mr. Clark, Senior Advisor, Division of Banking Supervision and Regulation, 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. Apgar, Senior Advisor to the Secretary, Department of Housing and Urban Development

Mr. Herold, Deputy General Counsel, Department of Housing and Urban Development

Mr. Daly, Assistant General Counsel, Department of Housing and Urban Development

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

Mr. Lawler, Chief Economist, Federal Housing Finance Agency

Chairperson Bernanke called the meeting to order at approximately 4:05 p.m. (EDT).

The Board first considered draft minutes for the meeting of the Board held on April 6, 2009, which had been circulated in advance of the meeting. Upon a motion duly made and seconded, the Members unanimously voted to approve the minutes of the meeting, subject to such technical revisions as may be received from the Members.

Using prepared materials, officials from the Department of the Treasury ("Treasury") then provided an update on the programs established by Treasury under the Troubled Asset Relief Program ("TARP"). Discussion during the meeting focused on the Supervisory Capital Assessment Program ("SCAP"), the Capital Assistance Program ("CAP"), the Term Asset-Backed Securities Loan Facility ("TALF"), the Home Affordable Modification Program ("HAMP"), and the Automotive Industry Financing Program ("AIFP") in light of recent developments with respect to each of these programs. Throughout the discussion, Members raised and discussed various matters with respect to these and other programs established by Treasury to implement and achieve the objectives of the TARP.

Treasury and Federal Reserve officials first reviewed and discussed with Members the results of the SCAP, a supervisory exercise conducted by the Federal Reserve and the other Federal banking agencies ("FBAs") in consultation with Treasury. The SCAP was designed to assess how much of an additional capital buffer, if any, each of the 19 largest U.S. bank holding companies ("BHCs") would need to establish now to ensure that the institutions could withstand losses and sustain lending even in a significantly more adverse economic environment than currently anticipated. According to the SCAP results, under the more adverse economic scenario, losses at the 19 largest BHCs could total approximately $600 billion during 2009 and 2010. After taking account of potential resources to absorb those losses and other factors, the SCAP results indicated that: (i) 9 of the 19 firms already had capital buffers sufficient to withstand the adverse scenario, and (ii) 10 of the 19 institutions needed to collectively raise additional common equity of approximately $75 billion.

Members and officials also discussed the process, timing and requirements of the capital plans each of the 10 institutions must submit to their primary FBA describing how the institution will increase or enhance the

quality of their capital to meet the required capital buffer. Members also reviewed the status of the efforts of all institutions subject to the SCAP in raising capital from private sources, issuing non-governmental guaranteed debt, and taking other steps to improve their capital position. Federal Reserve officials noted that the 10 firms determined to be in need of additional capital as a result of the SCAP had already raised more than $36 billion of new common equity, with a number of these offerings of common shares being over-subscribed. In addition, it was noted that these firms had announced actions that would generate up to an additional $12 billon of common equity. Members noted that the substantial progress of firms in raising private capital suggested that investors were gaining greater confidence in the banking system and discussed the reactions of the market to the SCAP announcements and the robustness of the assessments undertaken as part of the SCAP.

As part of this discussion, Members also considered and discussed the potential for additional capital to be made available through the CAP, if needed, as well as the potential for institutions to repay the capital previously received under the TARP and the process and conditions for institutions to receive approval to do so.

Using written materials, Members and officials then discussed the status of, and recent developments concerning, the TALF. During this discussion, Federal Reserve officials explained that the amount of loans requested in May under the program increased to $10.6 billion and noted the potential for this trend to continue in the future. Members and officials also discussed the recent expansion of the TALF to include both recently issued and legacy commercial mortgage-backed securities as eligible collateral, as well as the potential for additional eligible asset classes to be included in the TALF, such as recently issued collateralized loan obligations and newly issued and legacy residential mortgage-backed securities. Members and officials also discussed the steps taken by Treasury and the Federal Reserve, working in conjunction with the Special Inspector General for the TARP, to establish internal controls for the TALF that would help prevent fraud and protect taxpayers. Members also discussed efforts to promote participation in the program by small, minority and women-owned businesses.

Treasury officials then provided the Members with an update regarding the HAMP announced by Treasury in February 2009, which is intended to bring relief to responsible homeowners struggling to make their mortgage payments. Members and officials discussed, among other things, the number of first-lien mortgage loans that had been or are expected to be modified under the program; recent improvements to the program to address second-lien mortgages and to encourage short sales or deeds-in-lieu in cases where borrowers are not eligible for, or default on, a HAMP-modified loan; and the amount of funds requested and disbursed from TARP in support of the program. Members and officials also discussed ways that Treasury, working in conjunction with HUD, FHFA and the FBAs could monitor and review lender participation in the program. As part of this discussion, officials from FHFA provided Members with an update on the

separate refinancing initiative introduced by Fannie Mae and Freddie Mac for borrowers with high loan-to-value ratios.

Using written materials, Mr. Rattner and other Treasury officials then provided the Members with an update regarding the AIFP and the steps taken by Treasury and the Presidential Task Force on the Auto Industry ("Auto Task Force") to help General Motors Corp. ("GM") and Chrysler LLP ("Chrysler") restructure in order to become financially viable.

During this discussion, Members and officials discussed key aspects of the restructuring plans and processes for GM and Chrysler, as well as the potential impact of these restructurings on bondholders, pension funds and other stakeholders. For example, Members discussed the approximately $3.3 billion in debtor-in-possession financing Treasury will provide to support Chrysler through an expedited chapter 11 proceeding; the exit financing Treasury will provide to facilitate Chrysler's re-launch and alliance with Fiat S.p.A. ("Fiat"); and the 8 percent equity position Treasury will obtain in the new Chrysler. Members also discussed the status and progress of the restructuring process for GM and the potential for Treasury to provide GM with debtor-in-possession financing should GM file for bankruptcy protection.

Members and officials then reviewed and discussed the key terms and timing of Treasury's purchase of mandatory convertible preferred stock of GMAC LLC ("GMAC") following release of the SCAP results, including the $7.5 billion investment made on May 21, 2009, to help address the company's capital needs, stabilize the auto financing market, and contribute to the overall economic recovery of the automotive industry. Members also discussed the exchange of Treasury's pre-existing $884 million loan to GM for common shares of GMAC, as contemplated by the initial loan agreement, and Treasury's ownership position in GMAC following this exchange.

The meeting was adjourned at approximately 5:25 p.m. (EDT).

[Electronically Signed]

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Jason A. Gonzalez
Secretary

# Minutes of the Financial Stability Oversight Board Meeting
# June 25, 2009

A meeting of the Financial Stability Oversight Board ("Board") was held at 5:00 p.m. (EDT) on Thursday, June 25, 2009, at the offices of the Department of the Treasury ("Treasury").

MEMBERS PRESENT:

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

STAFF PRESENT:

Mr. Fallon, General Counsel
Mr. Gonzalez, Secretary

AGENCY OFFICIALS PRESENT:

Mr. Allison, Counselor to the Secretary and Assistant Secretary of the Treasury for Financial Stability, Department of the Treasury

Mr. Wheeler, Deputy Assistant Secretary for Federal Finance, Department of the Treasury

Mr. Madison, Nominee for General Counsel, Department of the Treasury

Mr. Albrecht, Counselor to the General Counsel, Department of the Treasury

Mr. Feinberg, Special Master for Executive Compensation under the Troubled Asset Relief Program, Department of the Treasury

Mr. Miller, Director of Investments, Office of Financial Stability, Department of the Treasury

Ms. Abdelrazek, Senior Advisor to the Counselor to the Secretary and Assistant Secretary of the Treasury for Financial Stability, Department of the Treasury

Ms. Aveil, Special Assistant to the Secretary, Department of the Treasury

Ms. Liang, Associate Director, Division of Research & Statistics, Board of Governors of the Federal Reserve System

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

Mr. Delfin, Special Counsel 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 5:05 p.m. (EDT).

The Board first considered draft minutes for the meeting of the Board held on May 28, 2009, which had been circulated in advance of the meeting. Upon a motion duly made and seconded, the Members unanimously voted to approve the minutes of the meeting,

subject to such technical revisions as may be received from the Members.

Using prepared materials, officials from the Department of the Treasury ("Treasury") then provided an update on the programs established by Treasury under the Troubled Asset Relief Program ("TARP"). Discussion during the meeting focused on the executive compensation and corporate governance regulations recently issued by Treasury under the TARP; the Capital Purchase Program ("CPP"); the Public-Private Investment Partnership ("PPIP") program; and developments in the financial and housing markets. Materials and updates concerning the other programs established by Treasury under the TARP, including the aggregate level and distribution of commitments and disbursements under the TARP, repayments of TARP funds, and the level of resources that remain available under the TARP, was included in the materials prepared for the meeting. During this discussion, Members also raised and discussed various matters with respect to the development and ongoing implementation of other policies and programs under the TARP.

Using prepared materials, Mr. Feinberg and other Treasury officials briefed the Members on the role and functions of the Office of the Special Master for Executive Compensation and the key aspects of the interim final rule on executive compensation and corporate governance (the "interim final rule"), which Treasury had announced on June 10, 2009, to help ensure that public funds provided to TARP recipients are directed towards the public interest and not toward inappropriate private gain. As part of this discussion, Members and officials reviewed and discussed the standards for executive compensation set forth in the interim final rule, including the provisions: designed to prevent senior executive officers ("SEOs") from taking unnecessary and excessive risks that threaten the value of the recipient of TARP funds; requiring the recovery of any bonus, retention award, or incentive compensation paid to a SEO or any of the next twenty most highly-compensated employees based on materially inaccurate statements of earnings, revenues, gains, or other criteria; and prohibiting golden parachute payments to SEOs and other highly compensated employees. As part of this discussion, Treasury officials reviewed and discussed with the Members the process established by the Office of the Special Master to review payments and compensation plans for the SEOs and other highly compensated employees of TARP recipients that have received exceptional assistance. Members also discussed key aspects of the accompanying rules on corporate governance and disclosure set forth in Treasury's interim final rule, which provide for: the establishment of a compensation committee of independent directors to meet semi-annually to review employee compensation plans and the risks posed by these plans to the TARP recipient; the adoption of an excessive or luxury expenditures policy; the disclosure of perquisites offered to SEOs and certain highly compensated employees; the disclosures related to compensation consultant engagements; and the applicability of the federal securities rules and regulations regarding the submission of a non-binding resolution on SEO compensation to shareholders.

Using prepared materials, Treasury officials then provided the Members with an update on the CPP.

Officials and Members reviewed and discussed, among other things, the number of applications received and approved by Treasury under the program; the amount of funds requested, disbursed and repaid to Treasury; and the key terms and timing of the re-opening and expansion of the CPP, which Treasury had announced on May 13, 2009, to support small and community banks.

As part of this discussion, Members and officials also discussed the manner in which warrants acquired by Treasury under the CPP would be valued and sold, as well as the treatment of redemptions and dividend proceeds received by Treasury for TARP and federal budgeting purposes.

Using prepared materials, Treasury officials then provided the Members with an update on the legacy securities component of the PPIP program, under which Treasury will partner with approved asset managers who will raise private capital for public-private investment funds ("PPIFs") to invest in legacy commercial mortgage-backed securities and residential mortgage-backed securities. As part of this discussion, Members and officials reviewed the progress Treasury has made in reviewing the 104 fund manager applications that were submitted to Treasury prior to the applications deadline for the program, which Treasury had extended to April 24, 2009, to better accommodate increased interest in the program, and the potential timing of commencement of the program.

Members and officials then engaged in a roundtable discussion regarding the current state of the U.S. housing and financial markets, during which officials from the Federal Reserve and the Federal Housing Finance Agency presented certain data to the Members, including data related to corporate bond spreads, stock prices, credit default swap spreads for selected financial institutions, debt growth among household and nonfinancial businesses, conditions in the commercial paper and asset-backed securities markets, issues financed under the Term Asset-backed Securities Loan Facility ("TALF"), and data related to credit demand and standards drawn from the Federal Reserve's Senior Loan Officer Opinion Survey. As part of this discussion, Members and officials also discussed current financial market developments and the potential for loan losses on small and medium sized banking organizations. In considering the state of the housing and housing finance markets, Members and officials reviewed, among other things, data related to mortgage rates, delinquencies and housing prices. During this discussion, Members also discussed potential modifications to the refinancing initiative introduced by Fannie Mae and Freddie Mac for borrowers with high loan-to-value ratios, as well as liquidity issues in the market for mortgage lending.

Following this discussion, Treasury officials provided an update regarding the Home Affordable Modification Program ("HAMP"). As part of this discussion, Members and officials reviewed and discussed the number of first-lien mortgage loans that had been or are expected to be modified under the program and the amount of funds requested and disbursed from TARP in support of the program.

Members and officials then engaged in a discussion regarding the

Board's quarterly report to Congress for the quarter ending June 30, 2009, that will be issued by the Board pursuant to section 104(g) of the EESA. Members and officials discussed, among other things, the timing and potential contents of the report.

The meeting was adjourned at approximately 6:05 p.m. (EDT).

[Electronically Signed]

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Jason A. Gonzalez
Secretary