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United States Department of the Treasury Fifth Tranche Report to Congress

U. S. Department of the Treasury

UNITED STATES DEPARTMENT OF THE TREASURY
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I. INTRODUCTION

This *Fifth Tranche Report to Congress* meets the requirement for reporting at the $300 billion commitment level under section 105(b) of the Emergency Economic Stabilization Act of 2008 (EESA). Recent transactions under the Automotive Industry Financing Program (AIFP), the Targeted Investment Program (TIP), and the Asset Guarantee Program (AGP), when combined with $195.3 billion of transactions under the Capital Purchase Program (CPP) and the $40 billion transaction under the program for Systemically Significant Failing Institutions, bring the total amount of transactions to $301.1 billion. Treasury will submit the next report when transaction levels reach the $350 billion level.

The Report addresses the following six areas:

- A description of all the transactions made during the reporting period.
- A description of the pricing mechanism for the transactions.
- A justification of the price paid for, and other financial terms associated with, the transactions.
- A description of the impact of the exercise of such authority on the financial system.
- A description of the challenges that remain in the financial system, including any benchmarks yet to be achieved.
- An estimate of additional actions under the authority provided pursuant to the EESA that may be necessary to address such challenges.

II. TRANSACTION INFORMATION BY PROGRAM

This *Fifth Tranche Report* discusses transactions under four programs: the Capital Purchase Program (CPP), the Automotive Industry Financing Program (AIFP), the Targeted Investment Program (TIP), and the Asset Guarantee Program (AGP). Since Treasury's *Fourth Tranche Report to Congress*, submitted to Congress on January 7, 2009, Treasury has closed $48.3 billion in transactions under these four programs. A report listing all transactions under the Troubled Asset Relief Program is attached as the Appendix, and has been posted on our web site.

Capital Purchase Program

Treasury continues to invest funds in financial institutions across the United States through the CPP, a program created to stabilize the financial system by directly infusing capital into healthy, viable institutions increasing their capacity to lend to U.S. businesses and consumers and support the U.S. economy. Since Treasury's *Fourth Tranche Report to Congress*, Treasury has closed $17.8 billion in transactions under the CPP, bringing the total amount of funds disbursed under the CPP to $195.3 billion. Treasury has completed CPP transactions with 359 United States financial institutions and Community Development Financial Institutions in 45 states and Puerto Rico. In addition, on January 13, 2009, Treasury released a term sheet for qualified financial institutions applying to the CPP that are S corporations, with an application deadline of February 13, 2009.

Automotive Industry Financing Program

Treasury also continues to provide support to U.S. auto manufacturers and auto financing companies through the AIFP, in order to prevent a significant disruption of the American automotive industry, which would pose a systemic risk to financial market stability and have a negative effect on the economy of the United States. Guidelines for the AIFP are published on Treasury's web site at http://www.treasury.gov/initiatives/eesa/. Since Treasury's *Fourth Tranche Report to Congress*, Treasury committed an additional $1.5 billion in TARP funds through this program and funded $5.4 billion of a previously announced loan.

On January 16, 2009, Treasury announced that it will make a loan under the AIFP of up to $1.5 billion to Chrysler LB Receivables Trust (Chrysler Trust), a special purpose entity created by Chrysler Financial Services Americas LLC (Chrysler Financial), to finance the extension of new consumer auto loans. The five-year loan is secured by a senior secured interest in a pool of newly originated consumer automotive loans, and Chrysler Holding LLC will serve as a guarantor for certain covenants of Chrysler Financial. Under the agreement, Chrysler Financial must comply with the executive compensation and corporate governance requirements of section 111(b) of EESA, as well as enhanced restrictions on executive compensation including the need to reduce by 40 percent its bonus pool for Senior Executive Officers and Senior Employees. In lieu of warrants, Treasury received additional notes in an amount equal to 5 percent of the maximum loan amount. The additional notes will vest 20 percent on the closing date and 20 percent on each anniversary of the closing date and will have other terms similar to the loan.

On January 21, 2009, Treasury funded $5.4 billion of a maximum $13.4 billion loan to General Motors Corporation (GM) that was discussed in detail in Treasury's *Fourth Tranche Report to Congress*. Treasury funded $4 billion of this loan on December 31, 2008, and will provide an additional $4 billion on February 17, 2009, subject to GM meeting certain conditions.

Targeted Investment Program

Treasury's Targeted Investment Program (TIP) is designed to prevent a loss of confidence in financial institutions that could result in significant market disruptions, threatening the financial strength of similarly situated financial institutions, impairing broader financial markets, and undermining the overall economy. Program guidelines for the TIP are available on Treasury's web site at http://www.treasury.gov/initiatives/eesa/.

Since Treasury's *Fourth Tranche Report to Congress*, Treasury completed its second transaction under the TIP, investing $20 billion in Bank of America Corporation (Bank of America) on January 16, 2009. Under the agreement with Bank of America, Treasury purchased $20 billion of preferred stock and warrants from Bank of America, and will receive an 8 percent dividend, payable quarterly. As part of this agreement, Bank of America must implement rigorous executive compensation standards and other restrictions on corporate expenditures. As previously disclosed, Treasury has also invested in Bank of America through the CPP.

Asset Guarantee Program

The Asset Guarantee Program (AGP) provides guarantees for assets held by systemically significant financial institutions that face a risk of losing market confidence due in large part to a portfolio of distressed or illiquid assets. The AGP will be applied with extreme discretion in order to improve market confidence in the systemically significant institution and in financial markets broadly. Treasury does not anticipate that the program will be made widely available, and notes that the EESA requires that premiums under section 102 be set to ensure that taxpayers are fully protected. Details on the AGP are available on Treasury's web site.

Treasury completed its first transaction under the AGP on January 16, 2009, when it finalized the terms of a guarantee agreement with Citigroup, Inc. (Citigroup) that was previously announced on November 23, 2008. Under the agreement, Treasury, the Federal Reserve, and the Federal Deposit Insurance Corporation (FDIC) will provide protection against the possibility of large losses on an asset pool of approximately $301 billion of loans and securities backed by residential and commercial real estate and other such assets, which will remain on Citigroup's balance sheet. The following loss-sharing protocol will apply: Citigroup will absorb the first $39.5 billion in losses[1]; losses over $39.5 billion are shared by Treasury (90 percent) and Citigroup (10 percent) (the "second loss"). Treasury absorbs the second loss up to $5 billion, the FDIC absorbs the third loss up to $10 billion, and the Federal Reserve funds any residual loss through a non-recourse loan. The guarantee is in place for ten years for residential assets and five years for non-residential assets. As a fee for the guarantee, Citigroup will issue $7 billion of preferred stock with an 8 percent dividend rate; $4 billion will be issued to Treasury and $3 billion to the FDIC. As part of the agreement, Citigroup must submit an executive compensation plan to Treasury and the FDIC for approval and must comply with certain common stock dividend restrictions. As previously announced, Treasury has also invested in Citigroup through the CPP and the TIP.

In addition, Treasury and the FDIC announced that they will provide protection to Bank of America against the possibility of unusually large losses on an asset pool of approximately $118 billion of loans and securities backed by residential and commercial real estate loans, and other trading book assets that have been marked to current market value. The large majority of these assets were assumed by Bank of America as a result of its recent acquisition of Merrill Lynch & Co. The assets will remain on Bank of America's balance sheet. As a fee for this arrangement, Bank of America will issue preferred shares to Treasury and the FDIC. In addition and if necessary, the Federal Reserve is prepared to backstop residual risk in the asset pool through a non-recourse loan. As part of the agreement, Bank of America will be required to submit an executive compensation plan to Treasury and the FDIC for approval and to adhere to certain common stock dividend restrictions. The Bank of America guarantee was announced on January 16, 2009, but has not yet been finalized.

[1] This represents $29 billion as a "first loss" amount, $9.5 billion in reserves, and $1 billion related to an agreement on hedging procedures.

III. ASSESSMENT OF CURRENT MEASURES AND THE CHALLENGES AHEAD

Impact of the Transactions

In this unprecedented period of market instability, Treasury continues to develop and implement programs under the Troubled Assets Relief Program (TARP) designed to restore stability and liquidity to the U.S. financial system while safeguarding taxpayer interests. As new challenges have arisen, Treasury has responded quickly to adapt to market events and provide support to U.S. financial institutions and automotive companies in order to prevent disruption to the financial markets. Treasury's actions, in concert with the work of other regulators, have stemmed a series of financial institution and automotive industry failures.

The purpose of the Capital Purchase Program (CPP) is to stabilize the financial system by building the capital base of healthy, viable U.S. financial institutions, which in turn will increase the capacity of those institutions to lend to U.S. businesses and consumers and support the U.S. economy. Since the inception of the CPP in October 2008, Treasury has strengthened small and large, regional and national, financial institutions as well as Community Development Financial Institutions through total CPP investments of $195.3 billion in 359 institutions in 45 states and Puerto Rico. In January, Treasury collaborated with bank regulators and CPP participants to develop a survey of the 20 largest participating institutions that will collect and disseminate monthly data on lending and other activities. In addition, the Office of Financial Stability will analyze quarterly monitoring data (call reports) and report on the results. The deadline for participants to respond to the initial survey was January 31, 2009. The input received from CPP participants through these surveys will help Treasury monitor and report the effects our strategy is having on lending and other bank activities. As of January 31, 2009, Treasury has received over $271 million in dividends related to its investments through the CPP.

Treasury's loan to Chrysler Financial was necessary in order to provide stability and prevent disruption to the U.S. automotive sector. This loan is part of a larger effort to assist the domestic automotive industry in becoming financially viable. An inability to finance automobile loans by Chrysler Financial would pose a systemic risk to financial market stability, have a negative effect on the economy of the United States, and threaten the company's prospects for long-term viability. Treasury's loan to Chrysler Financial provided liquidity necessary to finance consumer purchases of Chrysler vehicles while Chrysler restructures its business operations.

Treasury's investment in Bank of America was necessary to restore confidence in that institution, a significant market participant in several critical financial markets and payments systems. Failure to act could have had severe repercussions on global financial markets and the economy. Bank of America is the largest domestic banking institution by asset size, providing commercial and retail banking services and other financial services in the United States and internationally. The company is a dominant provider of deposit and credit products to the U.S. consumer sector with particular emphasis on the residential mortgage market, and is a key participant in the U.S. payments and securities settlement systems. The inability of a major financial institution to fulfill its role and obligations in these sectors could shake consumer confidence in U.S. financial institutions in general, cause significant market disruptions, and threaten the overall economy. Treasury's investment in Bank of America provided additional liquidity and has helped restore confidence in that institution.

The agreement of Treasury and the FDIC to provide protection to Citigroup against the possibility of unusually large losses is part of a broader effort to support Citigroup as the company executes its restructuring plans. This effort includes an investment in Citigroup through the TIP, which was discussed in detail in Treasury's *Fourth Tranche Report to Congress*. Citigroup is one of the nation's largest financial institutions, providing commercial and retail banking services and other financial services in the United States and internationally. The company has some 200 million customer accounts and does business in more than 100 countries. At the end of the third quarter of 2008, Citigroup had assets of $2.05 trillion, making it the second largest banking organization in the United States in terms of assets. In an environment of high volatility and severe financial market strains, the loss of confidence in a major financial institution could result in significant market disruptions and threaten the financial strength of similarly situated financial institutions and thus broader financial markets and pose a threat to the overall economy. The protections afforded to Citigroup by Treasury and the FDIC through the asset guarantee have helped restore confidence in that institution.

Treasury is committed to implementing the TARP with the highest degree of accountability and transparency possible. On January 28, 2009, we announced that we will begin posting redacted investment contracts for future transactions on Treasury's web site within ten business days of a transaction's closing. For transactions that have already closed, Treasury will publicly post contracts on a rolling basis until all investment agreements are available on the web site. In January 2009, Treasury also announced additional voluntary actions to bolster transparency and ensure that TARP investment decisions are protected from lobbyist influence. For example, under one measure, Treasury will begin certifying to Congress that each TARP investment decision is based solely on objective investment criteria.

Challenges That Lie Ahead

The current financial crisis is one of the most challenging in recent history. In response, Treasury has implemented a number of programs under the TARP to quickly stabilize the financial system and restore confidence in our financial institutions, thus increasing credit availability, promoting jobs and economic recovery, and safeguarding taxpayer interests. While there is no single action the Federal Government can take to end the financial market turmoil and the economic downturn, the authorities Congress provided last fall dramatically expanded the tools available to address the needs of our system. Treasury will continue to develop the most effective combination of tools to further stabilize the financial system and speed the process of economic recovery. While many challenges lie ahead, we are confident that these efforts will lay a strong foundation for economic recovery and market stability.