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U.S. Government Responses to the Financial Crisis September 1, 2008– Present

U.S. Congress

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(last updated March 16, 2009) [1]

Congress

Emergency Economic Stabilization Act of 2008 (EESA)

Enacted October 3, 2008.

Directs the Treasury Secretary to establish the Troubled Asset Relief Program (TARP), which authorizes the purchase of up to $700 billion of “troubled assets” from “financial institutions.” Troubled assets is broadly defined to include residential and commercial mortgages, other instruments related to such mortgages, and any other financial instrument the purchase of which is determined to be necessary to promote financial stability (provided that the Secretary notifies Congress of the basis for this determination). Initial tranche of $250 billion is authorized immediately; President must then certify that additional funds are needed ($100 billion as the second tranche, and a final $350 billion tranche that is subject to disapproval by Congress).) [2] Any institution participating in the TARP must (1) provide Treasury with a warrant to receive non-voting common or preferred stock in the institution or a senior debt instrument (or, for institutions that may not issue these securities, other instruments at Treasury’s discretion), and (2) comply with applicable executive compensation and tax restrictions. See the Recovery Act entry below for information on additional executive compensation restrictions applicable to recipients of TARP funds. See the Treasury section below for details on implementation of the TARP and how the program will be reshaped under the Obama Administration’s Financial Stability Plan.

Provides tax relief to banking organizations that have suffered losses on certain holdings of Fannie Mae and Freddie Mac preferred stock by changing the character of these losses from capital to ordinary for federal income tax purposes.

Authorizes SEC to suspend mark-to-market accounting for any issuer or with respect to any class or category of transaction. Requires SEC to study mark-to-market accounting applicable to financial institutions, including depository institutions, and report its findings and recommendations to Congress. (The report was delivered to Congress on December 30, 2008 and is available at http://www.sec.gov/news/studies/2008/marktomarket123008.pdf).

Temporarily increases insurance limits on FDIC and credit union accounts to $250,000 per account through December 31, 2009.

The American Recovery and Reinvestment Act of 2009 (Recovery Act or ARRA)

Enacted February 17, 2009.

Economic stimulus package totaling $787 billion. Package includes spending initiatives in a variety of areas (e.g., education, health care, infrastructure, energy) and almost $300 billion in tax relief for both individuals and businesses.

Title VII of the Act requires the Treasury Secretary to establish standards for executive compensation and corporate governance applicable to any entity that has received or will receive assistance under the TARP. Among other things, these standards must: (1) limit the payment of incentive compensation to senior executives and other highly compensated employees; (2) provide for the entity to “claw back” any bonus or incentive compensation payment that is based on statements of earnings or similar criteria that are later found to be materially inaccurate; (3) require the entity’s CEO and CFO to certify compliance with the standards; (4) require the entity’s board to adopt a policy on “excessive or luxury expenditures”; and (5) for public entities, give shareholders an annual, non-binding “say-on-pay” vote. TARP recipients are generally permitted to withdraw from the program at any time by repaying the government assistance.

Federal Reserve

AIG—Federal Assistance Package

September 2008: AIG is permitted to draw up to $85 billion under loan facility with a two-year term. Interest to accrue on the outstanding balance at a rate of three-month Libor plus 850 basis points.

November 10, 2008: Federal Reserve and Treasury announce a restructuring of the federal assistance to AIG:

- Treasury to purchase $40 billion of newly issued AIG preferred shares under the TARP.
- AIG loan facility to be modified as follows: (1) amount available reduced from $85 billion to $60 billion; (2) length of facility extended from two to five years; and (3) interest rate reduced to three-month Libor plus 300 basis points.
- Residential Mortgage-Backed Securities Facility to be established: Newly formed limited liability company will borrow up to $22.5 billion to purchase residential mortgage-backed securities from AIG's U.S. securities lending collateral portfolio. Proceeds from the facility, together with other AIG resources, will be used to return all cash collateral posted for loans outstanding under AIG's U.S. securities lending program. Prior $37.8 billion lending facility established on October 8, 2008, by the New York Federal Reserve Bank will be repaid and terminated.
- Collateralized Debt Obligations Facility to be established: Newly formed limited liability company will borrow up to $30 billion to purchase multi-sector collateralized debt obligations on which AIG has written credit default swap (CDS) contracts. CDS counterparties will concurrently unwind the related CDS transactions.

March 2, 2009: Federal Reserve and Treasury announce a further restructuring of the federal assistance to AIG:

- Treasury to exchange its existing $40 billion in cumulative perpetual preferred shares for new preferred shares with revised terms more closely resembling common equity.
- Treasury to create a new equity capital facility that will allow AIG to draw down up to $30 billion in exchange for non-cumulative preferred stock issued to Treasury.

Additional changes to the AIG loan facility noted above (for details, see http://www.federalreserve.gov/newsevents/press/other/20090302a.htm).

Asset-Backed Commercial Paper Money Market Mutual Fund Liquidity Facility (AMLF)

Non-recourse loans at the primary credit rate to U.S. depository institutions and bank holding companies to finance purchases of high-quality asset-backed commercial paper from money market mutual funds. AMLF was initiated on September 19, 2008, and subsequently extended twice; it is now authorized until October 30, 2009. Responses to frequently asked questions are available at http://www.frbdiscountwindow.org/mmmf.cfm?hdrID=14#f4.

Commercial Paper Funding Facility (CPFF)

A liquidity backstop to U.S. issuers of commercial paper through a special purpose vehicle that will purchase three-month unsecured and asset-backed commercial paper directly from eligible issuers. CPFF became operational on October 27, 2008, and was extended once; it is now authorized until October 30, 2009. Responses to frequently asked questions are available at http://www.newyorkfed.org/markets/cpff_faq.html.

Interest on Required Reserve Balances and Excess Reserves

Under an interim final rule effective October 9, 2008, the Federal Reserve Banks will pay interest on depository institutions' required and excess reserve balances. The payment of interest on required reserve balances effectively eliminates the implicit tax that reserve requirements imposed on depository institutions. The payment of interest on excess balances reduces the incentive for institutions to lend federal funds at rates much below the targeted federal funds rate. Responses to frequently asked questions are available at http://reportingandreserves.org/IOR_FAQ.pdf.

Money Market Investor Funding Facility (MMIFF)

October 21, 2008: Federal Reserve creates a funding facility to support a private-sector initiative intended to provide liquidity to U.S. money markets. Under the MMIFF, the Federal Reserve Bank of New York will provide senior secured funding to a series of special purpose vehicles (SPVs) that will purchase high-quality money market instruments maturing in 90 days or less from U.S. money market funds. The SPVs became operational in late November 2008 and were initially authorized to purchase assets until April 30, 2009; this date was later extended until October 30, 2009. Information about the MMIFF and responses to frequently asked questions are available at http://www.newyorkfed.org/markets/mmiff_faq.html.

January 7, 2009: Participation in MMIFF expanded to include other money market investors, such as U.S.-based securities lending cash-collateral reinvestment funds, portfolios, and accounts, as well as U.S.-based investment funds that operate in a manner similar to money market funds (e.g., certain local government investment pools, common trust funds, collective investment funds).

Primary Dealer Credit Facility (PDCF)

Overnight loan facility that provides discount window loans to primary dealers. Program was initiated in March 2008 and expanded in September to broaden allowable collateral to match closely the types of collateral that can be pledged in the tri-party repo systems of the two major clearing banks. The PDCF, which has been extended twice, is now set to expire on October 30, 2009. Responses to frequently asked questions are available at http://www.newyorkfed.org/markets/pdcf_faq.html.

Purchases of GSE Direct Obligations and Mortgage-Backed Securities

November 25, 2008: Federal Reserve announces that it will initiate a program to purchase direct obligations of housing-related government-sponsored enterprises (GSEs) and mortgage-backed securities (MBS) backed by Fannie Mae, Freddie Mac, and Ginnie Mae. The intent of the program is to reduce the cost and increase the availability of credit for the purchase of houses. Purchases of up to $100 billion in GSE direct obligations will be conducted with the Federal Reserve primary dealers through a series of competitive auctions, and purchases of $500 billion in MBS will be conducted by asset managers selected via a competitive process. Both types of purchases are expected to take place over several quarters.

December 30, 2008: Federal Reserve announces that the MBS purchase program is expected to begin operation in early January 2009. Responses to frequently asked questions about the MBS purchase program are available at http://www.newyorkfed.org/markets/mbs_faq.html.

Reciprocal Currency Arrangements

Temporary reciprocal currency arrangements (swap lines) between the Federal Reserve and central banks in other jurisdictions. A currency swap is a transaction where two parties exchange an agreed amount of two currencies, while at the same time agreeing to unwind the currency exchange at a future date. An underlying aspect of a currency swap is that banks (and businesses) around the world have assets and liabilities not only in their home currency, but also in dollars. Reluctance to lend in the interbank market has pushed up the premium for short-term U.S. dollar funding. The purpose of these swap lines is to inject liquidity, which can help bring interbank lending rates down.

Current status: Size and number of these swap lines have been increased on several occasions since December 2007. On October 13, 2008, swap lines with the Bank of England, the European Central Bank, and the Swiss National Bank were increased to accommodate whatever quantity of U.S. dollar funding is demanded. Program is currently in effect until October 30, 2009.

Regulatory Capital Calculations for Banks Holding Fannie Mae and Freddie Mac Preferred Stock

October 17, 2008: Federal Reserve and other regulators announce that banking organizations, in their third quarter 2008 regulatory capital calculations, may recognize the effect of the tax change in the EESA for certain holdings of Fannie Mae and Freddie Mac preferred stock (notwithstanding that EESA was not enacted until October 3).

Term Asset-Backed Securities Loan Facility (TALF)

November 25, 2008: Federal Reserve announces a loan facility designed to increase credit availability and support economic activity by facilitating renewed issuance of consumer and small business asset-backed securities. Federal Reserve Bank of New York (FRBNY) will lend up to $200 billion on a non-recourse basis to holders of certain AAA-rated asset-backed securities (ABS) that are backed by newly and recently originated auto loans, credit card loans, student loans, and small business loans guaranteed by the Small Business Administration. Treasury, through the TARP, will provide $20 billion of credit protection to the FRBNY in connection with this facility.

February 10, 2009: Federal Reserve announces that it “is prepared to undertake a substantial expansion” of the TALF, which could increase in size to as much as $1 trillion; the classes of ABS eligible for financing also could be broadened. Expansion of the TALF would be supported by additional funds from Treasury under the TARP.

March 3, 2009: Federal Reserve and Treasury announce the launch of the TALF, which will hold monthly fundings beginning March 25 and ending in December 2009. Responses to frequently asked questions about the TALF are available at http://www.newyorkfed.org/markets/talf_faq.html.

Term Auction Facility (TAF)

Biweekly auctions of term funds to depository institutions against collateral that can be used to secure loans at the discount window. Program initiated in December 2007.

Current status: Size of program has been expanded many times since its inception. Biweekly alternating auctions of 28-day and 84-day term paper now at $150 billion each. Program to continue until the Fed deems it is no longer necessary. Information about the TAF is available at http://www.federalreserve.gov/monetarypolicy/taffaq.htm.

Term Securities Lending Facility (TSLF)

Weekly loan facility that promotes liquidity in Treasury securities and other collateral markets, and thus fosters the functioning of financial markets more generally. The program offers Treasury securities for loan over a one-month term against other program-eligible general collateral. Securities loans are awarded to primary dealers based on a competitive single-price auction. Program was initiated in March 2008.

Current status: The amount of Treasury securities offered for auction and the types of eligible collateral have been increased several times since the program’s inception. Program is currently in effect until October 30, 2009. Responses to frequently asked questions about the TSLF are available at http://www.newyorkfed.org/markets/tslf_faq.html.

Treasury Department

Bank of America—Federal Assistance Package

January 16, 2009: Treasury, Federal Reserve, and FDIC announce an agreement with Bank of America to provide a package of guarantees, liquidity access, and capital. Composition of the assistance package is similar to that granted to Citigroup (described below), except that protected asset pool in this case totals approximately $118 billion.

Citigroup—Federal Assistance Package

November 23, 2008: Treasury, Federal Reserve, and FDIC announce an agreement with Citigroup to provide a package of guarantees, liquidity access, and capital:

> Treasury (pursuant to the Asset Guarantee Program under the TARP, which is described below) and FDIC to provide protection against “possibility of unusually large losses” on approximately $306 billion of loans and asset-backed securities that will remain on Citigroup’s balance sheet. Citigroup to issue preferred shares to each agency.
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> If necessary, Federal Reserve will backstop residual risk in the asset pool through a non-recourse loan.
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> Treasury (pursuant to the Targeted Investment Program under the TARP, which is described below) to invest $20 billion in Citigroup, in exchange for preferred stock paying an 8 percent dividend.

February 27, 2009: Treasury agrees to restructure its interest in Citigroup, the details of which are described at http://treas.gov/press/releases/tg41.htm.

Fannie Mae/Freddie Mac Guarantee

Treasury guarantees outstanding debt of Fannie Mae and Freddie Mac on September 7, 2008, when both agencies were placed in conservatorship by the Federal Housing Finance Agency.

Reserve Fund—Assistance with Liquidation of its U.S. Government Money Market Fund

November 20, 2008: Treasury announces that it will serve as a buyer of last resort for the fund’s securities to ensure that the fund is liquidated in an orderly and timely fashion. The agreement requires the fund to use best efforts to sell its assets within a 45-day period, after which Treasury’s Exchange Stabilization Fund will purchase any remaining securities at amortized cost, up to an amount required to ensure that each shareholder receives $1 per share. Information about the agreement is available at http://www.treas.gov/press/releases/hp1286.htm.

Temporary Guarantee Program for Money Market Funds

September 19, 2008: Treasury announces temporary guarantee program for publicly offered Rule 2a-7 money market funds that elect to participate in the program. Guarantee applies only to shares held by any shareholder of record on September 19 and would be triggered if a fund’s NAV falls below a certain level. Upon the fund’s liquidation, program would make up the difference between the value per share and $1. Information about the program and responses to frequently asked questions are available at http://www.treasury.gov/offices/domestic-finance/key-initiatives/money-market-fund.shtml. Program originally set to expire on December 18, 2008.

November 24, 2008: Treasury extends the program until April 30, 2009, for money market funds that are current participants and meet certain requirements. Funds must make an extension payment and submit an extension notice by December 5, 2008. Information about the extension is available at http://www.treas.gov/press/releases/hp1290.htm.

TARP

Capital Purchase Program

> October 14, 2008: Treasury announces that it will purchase up to $250 billion of senior preferred shares from certain U.S. controlled banks and thrifts, as well as certain bank and savings and loan holding companies. In addition to the non-voting preferred shares, Treasury will receive warrants to purchase common stock from each participating institution. Intent of the program is to encourage financial institutions to build capital so as to increase the flow of financing to U.S. businesses and consumers.
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> Application documents and responses to frequently asked questions for three categories of applicants—public institutions, privately-held institutions, and S corporations—are available at http://www.treas.gov/initiatives/eesa/application-documents.shtml.

Systemically Significant Failing Institutions

> Program objective is to provide stability and prevent disruption to financial markets in order to limit the impact from the failure of a systemically significant institution. Program guidelines are available at http://www.treas.gov/initiatives/eesa/program-descriptions/ssfip.shtml.
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> November 10, 2008: Treasury announces that it will purchase $40 billion of newly issued AIG preferred shares as part of a restructuring of federal aid to the company (see Federal Reserve section above for details).

Targeted Investment Program

> Program objective is to strengthen financial market stability through targeted investments. Treasury will determine the form, terms, and conditions of any such investment on a case-by-case basis in accordance with the considerations mandated in EESA. Program guidelines are available at http://www.treas.gov/press/releases/hp1338.htm.
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> Investments in Bank of America and Citigroup made pursuant to this program (see entries for each at the beginning of this section).

Asset Guarantee Program

Established as required by section 102(a) of EESA, the program provides guarantees for certain assets held by systemically significant financial institutions that face a high risk of losing market confidence due in large part to a portfolio of distressed or illiquid assets. Treasury intends that the program will be applied with extreme discretion and not be made widely available. The program is discussed more fully in Treasury's report to Congress dated December 31, 2008, which is available at http://www.treas.gov/initiatives/eesa/congressionalreports102.shtml.

Asset guarantees for Bank of America and Citigroup made pursuant to this program (see entries for each at the beginning of this section).

Financial Stability Plan—Obama Administration's Reshaping of the TARP

February 10, 2009: Treasury—together with the Federal Reserve, FDIC, Office of the Comptroller of the Currency, and Office of Thrift Supervision—announce a comprehensive set of measures intended to restore confidence in the strength of U.S. financial institutions and restart the critical flow of credit to households and businesses. Announcement (available at http://www.treasury.gov/press/releases/tg21.htm) notes that "Congress has already allocated substantial resources and authority for this program through [EESA]," but leaves open the possibility of requesting additional resources and further adapting the program in the future.

Core elements of the Financial Stability Plan include:

Capital Assistance Plan: (1) bank regulators to conduct a forward-looking, comprehensive "stress test" of the largest bank holding companies (those with assets exceeding $100 billion) in order to assess the risks on their balance sheets and their capital needs; (2) banks requiring additional capital may raise it privately or access it through a new Capital Assistance Program (CAP), under which Treasury will provide capital in exchange for convertible preferred stock [note: banks not going through the stress test also may access the CAP]; and (3) all capital investments made by Treasury through the CAP will be managed through a new Financial Stability Trust. Application guidelines, responses to frequently asked questions, and other information about the CAP are available at http://www.treas.gov/initiatives/eesa.

Public-Private Investment Fund: Treasury, Federal Reserve, and FDIC to design program intended to assist financial institutions in removing real estate–related "legacy" assets from their balance sheets. Expected to use public financing to leverage public and private capital on an initial scale of up to $500 billion, with possible expansion up to $1 trillion.

Consumer and Business Lending Initiative: Expansion of the TALF program, as discussed in the Federal Reserve section above.

Extension of the Temporary Liquidity Guarantee Program (see FDIC section below).

New framework for governance and oversight to help ensure that banks are held responsible for appropriate use of government assistance through stronger conditions on lending, dividends, and executive compensation, along with enhanced public reporting.

Securities and Exchange Commission

Ban on Short Selling of Financial Stocks

September 18, 2008: SEC issues an order temporarily banning the short sale of 799 financial stocks. Ban later modified to (1) include additional financial stocks and (2) exclude bona fide market making activity.

Current status: Short sale ban expired on October 8, 2008, following EESA enactment.

Disclosure of Short Sale Activity

September 18, 2008: SEC issues an order temporarily requiring institutional investment managers to make weekly disclosures of daily short sale activity. Order later extended and modified to provide that disclosure is made only to SEC and not publicly.

Current status: Disclosure requirement extended, with certain modifications, as interim final temporary Rule 10a-3T under the Securities Exchange Act until August 1, 2009.

Prohibition Against "Naked" Short Sales

September 17, 2008: SEC issues temporary Rule 204T under the Securities Exchange Act to address "naked" short selling. Rule requires that short sellers and their broker-dealers deliver securities by the close of business on the settlement date (three days after the sale transaction date, or T+3). Broker-dealers in violation of this requirement are prohibited from further short sales in the same security unless the shares are located and pre-borrowed.

Current status: Close-out requirement and pre-borrow penalty in temporary Rule 204T extended as interim final rule until July 31, 2009. Interim final rule specifies that securities lending will not be treated as a short sale under the temporary rule if a bona fide recall of the security is initiated within two business days after trade date.

Shadow Pricing Relief for Money Market Funds

No-action letter to the Institute dated October 10, 2008: Temporarily allowed money market funds to value certain securities at amortized cost for shadow pricing under Rule 2a-7. Relief limited to First Tier Securities with maturities of 60 days or less that the fund reasonably expects to hold to maturity. Relief expired on January 12, 2009.

Temporary Exemption for Certain Money Market Fund Liquidations

November 20, 2008: SEC issues Rule 22e-3T under the Investment Company Act of 1940 as an interim final temporary rule. Rule applies to certain money market funds that have elected to participate in the Treasury Department's Temporary Guarantee Program for Money Market Funds (see Treasury section above for program summary). Rule is intended to facilitate orderly liquidations and help prevent the sale of fund assets at "fire sale" prices. The rule will expire on October 18, 2009, unless the SEC announces an earlier expiration date.

Easing Restrictions on Issuer Repurchases

September 18, 2008: SEC issues order to temporarily alter the timing and volume restrictions that typically apply when issuers repurchase their shares. Intent was to provide additional flexibility and certainty to issuers that could be executing repurchases during the current market conditions.

Current status: Order extended once and then allowed to expire on October 17, 2008.

Federal Deposit Insurance Corporation

Temporary Liquidity Guarantee Program (TLGP)

October 14, 2008: FDIC announces that it will guarantee all newly issued senior unsecured debt of banks, thrifts, and certain holding companies issued on or before June 30, 2009. FDIC also will provide unlimited insurance for non-interest-bearing deposit transaction accounts through the end of 2009 in order to help stabilize the payroll and working capital accounts of small- and medium-sized businesses. All FDIC-insured institutions are covered under both aspects of the program for the first 30 days without charge; after that, institutions must opt out of the coverage or be assessed charges for their continued participation.

October 23, 2008: FDIC issues interim rule to govern the program (which provides the coverage described above as of October 14). Rule becomes effective immediately, but agency to accept public comments. FDIC also extends the opt-out deadline for participation in the TLGP to December 5, 2008.

November 21, 2008: FDIC approves final rule, which includes significant changes to the TLGP in response to public comments. Information about the program and responses to frequently asked questions are available at http://www.fdic.gov/regulations/resources/TLGP/index.html.

February 10, 2009: FDIC announces that it will extend the TLGP for an additional four months, to October 31, 2009.

ENDNOTES

[1] This document focuses primarily on government programs and initiatives that relate to the financial services sector and are most likely to be of interest to Institute members. It does not cover, for example, many of the initiatives to support the U.S. housing market or federal assistance to the auto industry.

[2] In January 2009, both the House and Senate voted to reject resolutions that would have disapproved the final $350 billion.