Written Testimony of Herbert M. Allison, Jr.,
Assistant Secretary for Financial Stability
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Chairman Serrano, Ranking Member Emerson, and Members of the Subcommittee, thank you for the opportunity to testify today regarding the Emergency Economic Stabilization Act of 2008 (EESA) and the Troubled Asset Relief Program (TARP).

Country Faced Economic Crisis

In October of 2008, the country faced economic difficulties not encountered since the Great Depression: credit markets were frozen; the global economy and the nation's economy were declining at an accelerating rate; and Americans had already lost trillions of dollars of wealth, in the value of their homes and in their savings. Interest rate spreads on credit cards and auto loans peaked at roughly 600 basis points, or six times their normal rates. This stagnation in the credit markets had a direct impact on Americans' daily lives: credit card limits were drastically reduced, obtaining a home loan became very difficult, and cars became more expensive due to the increased cost of credit.

Purpose of TARP

TARP is part of a broad effort by the Administration to promote financial stability and to stimulate the economy. The purpose of TARP was to restore liquidity and stability to the financial system, and the beneficiaries of TARP are the American people. Financial stability is a necessary precondition for economic recovery and growth. Investment of taxpayer funds in financial institutions was necessary in order for this stabilization to occur. These investments directly and indirectly continue to benefit taxpayers by re-establishing the willingness of banks to lend to consumers, by keeping interest rates low, and by helping homeowners stay in their homes. The TARP programs were created in order to benefit the American taxpayer.

Financial System Showing Signs of Stability

Our financial system has experienced a partial but significant recovery over the past year. The condition of most securities markets and large financial institutions has improved substantially. Borrowing costs for large banks, nonfinancial businesses, and state and local governments have returned to near normal levels. Securities markets that were essentially frozen a year ago have reopened, allowing businesses to issue over $1 trillion in debt without government guarantees. Prices for many "legacy" securities most exposed to losses that were held by banks have improved, and trading in these assets has resumed. Large banks are better capitalized than they were before the crisis, and restructuring in the financial industry is well underway. Housing markets are also showing signs of stabilizing. All of these indicators ultimately benefit the taxpayer. Stabilization of the financial system was a necessary precondition to many of the specific efforts we have undertaken to assist our citizens.

Government policies are responsible for many of the improvements to date. A combination of federal loans, capital injections, and guarantees has helped restore investor confidence in U.S. financial markets and institutions, which has translated into lower borrowing costs. The "stress test" of our largest financial institutions provided the transparency necessary for them to raise substantial capital from private sources to absorb losses from the crisis and repay government investments. Securitization markets important for consumer and small business loans have also improved, in large part because of a joint Treasury-Federal Reserve program, the Term Asset-Backed Securities Loan Facility (TALF) supported by TARP. The recovery of the securitization markets has helped increase the availability of credit for consumers and small businesses and has helped lower the cost of that credit. Availability of credit is critical for small businesses to grow and for consumers to make home improvements, buy a new car, or send their children to college. Additionally, the health of the securitization markets, and the companies that issue asset-backed securities, has had a positive impact on employment throughout the country. It is not just financial firms that rely upon the securitization markets for funding. Car companies, student loan companies and many small businesses are examples of non-bank institutions that need functioning capital markets in order to succeed. TALF helped accomplish this.

Home sales are improving due to a combination of housing policies. Mortgage rates are near historical lows, thereby stimulating home sales and refinancing. The American Recovery and Reinvestment Act of 2009 (Recovery Act) continues to improve the employment outlook, provide important support for state and local governments, and lay a stronger foundation for long-term economic growth. The improved health of the banking system is enabling some institutions to repay TARP funds.

TARP Funds Generated A Positive Return For Taxpayers

Treasury now expects to *make* – not lose – money on the $245 billion of investments in banks made through TARP programs. This is in sharp contrast to the original 2010 President's Budget estimate that Treasury's investments in the banks would cost taxpayers $79 billion. In fact, Treasury is being repaid at a very substantial rate. As of April 16th, banks have returned $176 billion in taxpayer investments – nearly 75% of all TARP funds invested in the banking system—and TARP has received $19 billion in dividend and warrant proceeds from banks.

In addition, Chrysler Financial has fully repaid (with interest) the $1.5 billion loan that it received. Just this month, General Motors made another repayment to the government in the amount of $1 billion. Repayments from all TARP recipients now total $181 billion, well ahead of last fall's projections for 2010 and represent repayment of nearly forty-six percent of all TARP disbursements to date. These early repayments are testaments to the success of the government's efforts to stabilize and rehabilitate our financial system.

TARP Costs Significantly Less Than Expected

Before President Obama took office, nearly $240 billion of taxpayer money had been invested into banks, accounting for about three quarters of the assets of the entire banking system. In addition, the Federal Reserve, Treasury and FDIC put in place guarantees and special liquidity facilities that amounted to trillions of dollars.

Since President Obama has taken office, Treasury has taken steps to dramatically bring down the cost of TARP and to shift its focus to small business and housing. As of the midsession review of the 2010 Budget, the projected cost of TARP was $341 billion. At that time, the Administration removed a $250 billion reserve included in the 2010 Budget, originally earmarked should additional stabilization efforts be necessary. After improved financial conditions and careful stewardship, the 2011 Budget projects the total costs of TARP to be less than $127 billion[1]. If Congress joins the President in enacting the financial recovery fee, American taxpayers will not have had to pay a penny for TARP.

TARP Exit Strategy

Because the various TARP investments have helped to stabilize the financial system and many have earned a positive return for taxpayers, the Administration is winding down many of its programs. As the President has previously said, Treasury will seek to exit its TARP investments as soon as practicable, in a manner protecting the taxpayers' interests. This will mean different timetables for different programs and institutions. For example, some institutions are thriving and have the ability to repay Treasury now or in the very near future. Other institutions will need more time to recover and repay Treasury, which is to be expected given the nature and impact of this financial crisis.

Treasury has already wound down many of its largest investment programs. The Capital Purchase and Capital Assistance Programs have closed. The Asset Guarantee Program, which generated positive returns for taxpayers, has been terminated. The previously discussed TALF has ceased making loans against collateral other than newly issued commercial mortgage-backed securities, and the final subscription for new issue commercial mortgage-backed securities is expected in June. We currently anticipate that TALF, as well, will generate positive returns for taxpayers.

Most of the TARP programs have ended or are ending, and our focus has shifted to continuing our careful management of those investments, protecting homeowners and stimulating small business lending.

Focus on Helping Homeowners

As the Obama Administration came into office last year, the country faced extraordinary economic and housing market conditions that required the rapid introduction of unprecedented policies designed to stabilize the housing and mortgage markets. On February 18, 2009, President Obama announced a comprehensive Homeowner Affordability and Stability Plan (HASP), which sought to address the issue of mortgage affordability for millions of struggling homeowners in America.

The Administration's goal is to promote stability for both the housing market and homeowners. To meet these objectives, the Administration has developed a comprehensive approach using mortgage modifications and refinancing, support for Fannie Mae and Freddie Mac, tax credits for homebuyers, state and local housing agency initiatives, and neighborhood stabilization and community development

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[1] The 2011 Budget estimated the deficit impact of TARP to be $117 billion, including programmatic costs and downward interest on reestimates of approximately $10 billion.

programs. With the record-low mortgage rates seen this past year and, thanks in large part to these programs, more than four million homeowners have refinanced their mortgages to more affordable levels helping to save more than $7 billion in the past year; more than one million homeowners have had a reduction in mortgage payments averaging $500 per month through trial-period and permanent loan modifications under the Administration's mortgage modification program; home equity (wealth for homeowners) increased by more than $13,000 for the average homeowner in the last three quarters of 2009; and the economy is growing.

Our housing initiatives must balance the need to help responsible homeowners struggling to stay in their homes, with the recognition that we cannot and should not help everyone. The President has said: "We can't stop every foreclosure." And in fact, we can't maintain this balance if we try to assist every borrower. For example, investors and speculators should not be protected under our efforts, nor should Americans living in million-dollar homes or defaulters on vacation homes. Some people simply will not be able to afford to stay in their homes because they bought more than they could afford. Instead, the Administration must focus on providing responsible homeowners opportunities to obtain a modification or to refinance and prevent avoidable foreclosures and, when necessary, facilitate the transition to a more sustainable housing situation. The newly announced adjustments to the FHA and Home Affordable Modification Programs are tailored to accomplish these goals by helping a targeted group of borrowers.

Treasury has set aside $50 billion in TARP funds to address the housing problem. Programs targeting this problem include first-lien modifications, second-lien modifications, Home Affordable Foreclosure Alternatives Program (HAFA) and the newly announced adjustments to the FHA Refinance Program designed to address borrowers with significant negative equity situations.

On February 19, 2010, we announced the $1.5 billion HFA Hardest-Hit Fund for five state HFAs in the nation's hardest-hit housing markets to design innovative, locally targeted foreclosure prevention programs. On March 29, 2010, we announced a $600 million expansion of that program for an additional five states. Overall, we anticipate that all of the housing programs together will utilize the $50 billion allocation in full.

Focus on Small Businesses

The other area in which Treasury anticipates an ongoing commitment is helping small businesses. Recently, Treasury announced final terms for the Community Development Capital Initiative (CDCI) program that will provide TARP funds to Community Development Financial Institutions (CDFIs) to lend to small businesses. The CDFIs play a vital role in providing financial services to some of the hardest-hit and poorest communities. This program will help deploy funds to the communities that most need the funds by leveraging the valuable experience of CDFIs.

Additionally, we launched a program for Treasury to purchase, using TARP funds, securities that have been guaranteed by the Small Business Administration (SBA) under its section 7(a) program, and we conducted our first purchases on March 18th. This program is designed to provide additional liquidity through the secondary market so that banks using SBA programs will have increased capital to lend to

small businesses. This program – combined with Recovery Act provisions that temporarily increased SBA loan guarantees and reduced fees –has helped significantly increase SBA loan volumes and secondary market activity.

Finally, the Administration has called for the creation, through legislation, of a new $30 billion Small Business Lending Fund outside of TARP to invest capital in community and smaller banks with incentives to support additional small business lending. The Administration is also working with Congress to consider additional ideas that might be included in the Small Business Lending Fund proposal.

Promoting Long Term Economic Stability- The Need for Regulatory Reform

The financial crisis was in large part the result of failures in government policy and oversight, failures in the design and enforcement of rules and regulation. But we are still living with the same financial system that brought us to the edge of collapse, and the success of the crisis response, without financial reform, will make future crises more likely. Even with improving credit markets and reduced borrowing costs, when we speak with businesses across the country, they tell us that banks are lending less, in part because they are not certain what new rules are coming. Delaying reform forces them to live with that continued uncertainty. Financial reform is necessary to help prevent future crises and bring certainty to the families and businesses that depend on the financial system to protect their savings and finance their home purchases, college educations, or business growth.

Today, the financial system is operating under the same rules that led to its near-collapse and to the recession. These rules must be changed to address the moral hazard posed by large, interconnected financial institutions considered "too big to fail." The Administration has proposed comprehensive financial reforms that seek to address this moral hazard by forcing these institutions to internalize the risks they impose on our financial system and to remove expectations of government support.

As we look ahead, we must not forget the lessons we have learned from this period. We need to reform our nation's laws to provide stronger, more effective regulation of our financial system and to protect consumers. Reforming our regulatory system in a way that is stronger and better suited to manage risk and ensure safety and soundness must be our highest priority.

Conclusion

The Congress has played a critical role in pulling our financial system back from the brink of collapse. We have made great progress to date, but it is important that we continue this progress by focusing on small businesses, the housing issue and comprehensive regulatory reform.