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WRAPPING UP THE TARP: WHAT WILL BE ITS LEGACY?

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## PROCEEDINGS

MR. GAYER: Good morning, everyone. I am Ted Gayer, vice president and director of Economic Studies here at Brookings. And I'm very pleased to introduce our speaker today, Tim Massad, who is the treasury assistant secretary for financial stability, which is an office that operates the Troubled Asset Relief Program, or as we all know it, TARP.

Assistant Secretary Massad has had various roles related to TARP. He initially came to D.C. to serve as a special legal advisor to the Congressional Oversight Panel, one of the oversight agencies for TARP. He then moved to treasury for its chief counsel for the Office of Financial Stability and later as its chief reporting officer. He was confirmed by the Senate to his current role as assistant secretary in June of 2011.

Washington Post columnist, Bob Samuelson, once wrote, "Almost everyone loves to hate TARP." It's a favored political sport of liberals, conservatives, Republicans, Democrats, and the public. My colleague, Doug Elliott, who will soon be serving as moderator today, may have described TARP best in saying, "It is the best large federal program to be despised by the public."

Treasury has, indeed, made a profit on the TARP program so far, for example, of the 205 billion that Treasury invested in banks. It has recouped 195 billion in principal and taken in more than 26 billion in

interest, dividends, warrants, and other income as of last week. But it is, as I alluded to, not without its critics. Perhaps most vocally is former Inspector General, Neil Barofsky who said that Treasury's zeal to get out of the banks could leave the financial system on shakier footing if institutions ultimately collapse.

Many also worry that TARP has exacerbated the problem of too big to fail financial institutions, something we recently held an event on right here at Brookings just a few weeks ago.

I'd also like to add that Brookings hosted the first TARP overseer, my friend and former colleague, Neil Casgary, in 2009, so it's only fitting that we now host the latest one on its five year anniversary.

So after the speech, Doug will ask Tim some questions and then open it up to all of you for audience questions. So please join me in welcoming Assistant Secretary Tim Massad.

(Applause)

MR. MASSAD: Good morning and thank you for that warm welcome. Thank you, Ted, for the very kind introduction. And thank you, Doug, for moderating this event. And most of all my thanks to the Brookings Institution for having me today. As Ted said, Neil Casgary, one of my predecessors, was here in January of 2009 to give really what was the first progress report on TARP. So my speech today could be

considered a bookend to that since we're nearing the end.

Now, when Neil spoke, TARP was being created because the financial world was falling apart. Anyone who lost their job, their home, or their savings during this recession does not need a reminder that this was a terrible crisis. But the idea that our financial system almost collapsed and what that would have meant to our modern economic way of life is I think something that's very hard to comprehend.

I want to remind you of what those times were like. These were some headlines just in case you've forgotten. It's no exaggeration to say that in September, 2008, our nation was on the verge of falling into a second Great Depression. Several major institutions had already failed, including Bear Stearns, Indymac, Washington Mutual. Fannie and Freddie had been taken over by the government.

On September 15th, Lehman Brothers filed for bankruptcy. The next day a money market fund broke the buck, essentially triggering the start of a run on money market funds generally, money market funds which many of us thought were one of the safest forms of investment.

The day after that, AIG, one of the largest and most complex financial firms in the world, was on the verge of failure. Confidence in the financial system was vanishing. Panic was spreading. The stock market dropped by more than 770 points in a single day. And every major

financial institution was vulnerable. Financial wildfire was also quickly spreading far beyond Wall Street. The credit markets that provide financing for credit cards, auto loans, student loans, small business loans and other types of financing had basically stopped functioning.

So for the first time in generations, Americans were starting to question the safety of their money in banks. For the first time in more than 80 years, a generalized run on the financial system was a real possibility.

It wasn't going to be like that scene you might remember from the Jimmy Stewart movie, you know, *It's a Wonderful Life*, they always show it around Christmas time, where all the towns people come down to the bank to line up to take their money out, you know. You wouldn't have to do that. You could move your money out with the click of a mouse, and it could have happened essentially that quickly.

The crisis was causing our economy to collapse. When President Obama took office, we were losing almost 800,000 jobs a month. In between December, 2009 and December, 2008, household wealth fell by almost 20 percent, more than 5 times the decline in 1929. It wasn't an issue of our economy growing slowly, our economy was contracting at 8 percent per year. There was great fear and uncertainty, and the government had limited options. The Federal Reserve and

Treasury were taking what actions they could under existing law, but they could not get ahead of the crisis nor contain the damage. And it was out of these extraordinary circumstances that TARP was born.

Now, as Ted noted, TARP was a program that nobody likes. Nobody in government ever wanted to do it. Americans disliked it with good reason. Who wants to use tax payer dollars to save private institutions? Indeed, I remember shortly after I joined, there was a poll that said the word TARP was less popular than the word Guantanamo. We really knew we had achieved something then.

Nobody ever wants to see TARP repeated. But the fact is, TARP is a program that did its job. It has worked faster, better, and cheaper than most people ever thought possible.

Now, this week marks the five year anniversary of the law that created TARP, so it is a good time to review the record. And even though the pain from this terrible recession is still with us, as a result of the actions taken through TARP and the other measures the government implemented, the financial panic was stopped. Our financial system did not collapse and the economy is growing again. And TARP has almost completely wound down. We have now earned positive returns for tax payers on the investments to stabilize banks and credit markets, and most remarkably, on the investment in AIG. In fact, as unlikely as it would have

sounded in the fall of 2008, we have now recovered more than we dispersed when we include those AIG profits. And tax payers will likely earn a significant positive return when one looks at all the financial interventions as a whole, what Treasury did, what the Federal Reserve did, what the FDIC did, everything together.

In short, TARP is one of the most effective, yet least understood programs in government. So as we observe this anniversary, I'm here to review exactly what TARP did, as well as where are we in the wind down, and what I hope its legacy will be.

Now, we recently published a presentation on the financial crisis, the government's response, and the progress we've made over the last five years. I've included a couple of slides from it. But because the screens are rather small, it may be hard to see. We have copies of the full presentation that we can give to you today, and it's also available on our web site.

So the first and most important measure of TARP's success is whether or not it helped to restore the financial stability of the nation. And simply put, TARP worked. Now, this slide shows a few snapshots of the economy before and during and after the crisis. There's a graph of GDP growth. Obviously red is bad, blue is good. The same for private sector job growth, as well as you can see at the bottom, and again, you'll

be able to see this better in the hard copy, how much spreads had gone up. You know, spreads are an indication of the cost of borrowing, and also the panic that had hit the markets, as well as the fall in household net worth.

And the most important fact about the government's response is that it acted with overwhelming force and speed to confront the crisis. The crisis was attacked on many fronts in order to address the many ways that American families and businesses depend on the financial system.

It was done through programs that were creatively designed, decisively launched, and carefully managed. And as a result, not only did we break the back of the panic, but we've recovered from the crisis faster than other nations.

The next chart just reminds you of the history, both the rapidity of the fall, as well as the progress we've made in recovering. And if you were to compare this, for example, to what happened in other financial crisis or in other countries, you would, again, see that the fall was very, very steep, but the recovery was much faster.

Now, all the credit for this doesn't go to TARP or to Treasury. As I said, it was only part of an overall response. And that response spanned both a Republican and a Democratic administration. It involved



programs run by the Fed, the Treasury, and other agencies. So let's talk about some of the ways that we help restore financial stability. And, you know, the notion of financial stability is sometimes kind of an obscure one. The notion of whether our financial system could collapse is, as I said, hard to understand.

Think of the financial system as the circulatory system for our nation's financial and economic health. The financial system enables people to have a checking account, get a credit card, receive their payroll deposits, buy a home, finance a car, finance a college education, save for retirement, enables businesses to grow, to make investments, to expand, and the idea that something would collapse is, of course, something that we have not experienced since the Great Depression.

And the point is that without TARP and the other measures, the pain experienced by Americans would have been far greater. So let's talk about what we did. First and foremost, we stabilized the banking system so money could start moving again throughout the economy.

There were a number of programs launched to invest in banks of all sizes. It wasn't just the biggest banks. We invested in more than 700 banks across the country, most of which were small community banks. In fact, I was down in Little Rock last week and I met with some of the smaller banks. Some of these banks have, you know, just hundreds of

millions of dollars in assets rather than the hundreds of billions that the big banks have. I was in Mississippi earlier this summer meeting with a number of small banks that do a lot of development work in the Delta region. We actually finance banks that have investment that held 98 percent of the assets of the banking system in this country at the peak, so essentially the entire system was covered.

We didn't give grants. We made investments, structured so that tax payers would receive a return as the banks recovered. Now, even after a lot of these investments had been made, you may recall there were people who said we should nationalize the major banks. Others, of course, said we shouldn't do anything, just as they had said we shouldn't do anything before, let the market cure the problem.

President Obama, after he took office, took a different course, and that path that he chose was to try to get private capital back into the system to replace the government investment. And in order to do that, Treasury and the regulatory agencies require the big banks to go through stress tests to determine which ones needed more capital. The idea was, make it transparent, restore confidence of investors, then private capital will come back in.

The government stood ready to provide additional capital. We had another TARP program ready to go for any bank that was

determined to not only not to need capital, many of them needed capital, but was then unable to raise it in the private markets. But the fact is, all of them were able to raise it in the private markets, other than Ally which we funded under the auto program, the former GMAC. So it worked.

Today banks have far more capital than they did at the time of the crisis. They rely less on short term funding which can evaporate in a crisis. And today we have almost completed our exit from these investments. We actually, at the peak of the crisis, had invested almost \$250 billion. We're now down to less than 3 billion. And as Ted mentioned, we've recovered a gain already of over 26 billion in additional income.

Moreover, I mentioned that at the peak, we had investments in banks representing 98 percent of the assets in the system. Today the investments we hold are in banks that hold less than 1 percent of the assets of the system.

So a second way that we helped restore financial stability was through three programs designed to restart what we call our secondary credit markets. Now, these are the markets that provide credit cards, financing for credit cards, mortgage loans, auto loans, student loans, and they had essentially frozen because of the crisis. And so we launched a series of programs to restart the flow of the credit. Now, you

might have heard of them. They have these funny acronyms, PPIT, NALF. I will spare you the complicated structural details here today. But essentially what we did was, in part, to partner with private fund managers in some cases or otherwise attract private investors in by providing loans. And the good news is that soon after these programs were implemented, the volume of activity in these markets increased. In fact, the mere announcement that the government was prepared to do some of these things increased confidence and helped us restart these markets.

So borrowing costs for businesses and individuals came down. And that recovery continues today. Credit is still somewhat constrained, but we are much better off than we were before. And today all those programs have been wound down. We've recovered all the investments. And tax payers have earned, again, positive returns, almost 4 billion on about 20 billion that we ultimately had to invest. It was interesting because originally we were prepared to invest a lot more, but again, the mere announcements helped restore that confidence.

Another way that we helped restore financial stability was through the TARP and Federal Reserve investments in AIG. Now, AIG and supporting AIG was one of the most difficult decisions made by the government. I was not in the government at that time, but the outrage that it caused is understandable. The Treasury and the Federal Reserve

together committed \$182 billion to a single company. I mean it's hard to fathom that amount or why it could ever have been necessary. So how did that happen?

By September of 2008, AIG had grown to become the largest insurance company in the world. At its peak, it had more than a trillion in assets, it provided conventional insurance to 75 million individual and corporate customers throughout 130 countries. But moreover, it had a substantial presence in many financial markets, whether that was corporate and municipal bonds or derivatives or otherwise.

Now, unfortunately it used its credit rating, which was very good at the time, because that came from the strength of its insurance subsidiaries, to engage in some very risky derivatives transactions. How AIG was able to do that without any federal agency essentially looking at the risk that that activity posed is the essence of the problem, but it is a larger discussion that is beyond the scope of my remarks today.

But the simple fact is that in that atmosphere of fear and panic, in the day after the money market run essentially started, which was the day after Lehman failed, which was a week after Fannie and Freddie, the sudden collapse of AIG could have dramatically accelerated the speed and intensified the severity of the financial crisis. And the people in government at the time had hours, maybe a day to make a

decision. The crisis would have likely spread to the entire insurance industry. Corporate and municipal bond markets, the derivatives markets, other financial markets would have been destabilized further. Investors would have pulled back even more from funding other institutions. And that's, simply put, why the government acted.

It did not act simply to save AIG. It did not act simply to help particular financial institutions that dealt with AIG. It was because AIG's sudden collapse at that time and in those circumstances would have had catastrophic consequences. Some of the support for AIG came from TARP. The rest came from the Federal Reserve. As I mentioned, total commitments of 182 billion. We have as of today recovered all of that plus a profit of 23 billion. We have no further interest in AIG.

Moreover, today the government has powers to not only regulate large non-bank institutions, financial institutions, but also unwind them if they pose those kinds of risks.

Now, many have still questioned whether TARP and the response to the crisis generally did enough to help Main Street. The evidence of its impact on Main Street is not always obvious to many Americans and that's for I think a few reasons. One is, the programs themselves invested in institutions and markets. That was the design of the law. The design of the law was that Treasury would purchase financial

instruments from financial institutions. The programs had complex details, odd acronyms, so, you know, they were remote from everyday lives. And after all, most Americans who've known economic hardship these past few years don't think about the collapse of Lehman Brothers when they think about the recession. In fact, when you ask most people when did the financial crisis start, at least outside of maybe here and New York, you know, a lot of people probably wouldn't date it to Lehman weekend, they'd say, well, you know, it's when I got a pink slip or when I received a notice of foreclosure on my home.

And another reason, therefore, why I think people don't maybe understand the impact of these programs is, we are still struggling with the damage from the crisis. Growth is too small and unemployment is too high. And median family income, as was indicated by a recent report, has not increased in many years. So we still have work to do to get where we need to be. But I don't think that diminishes what TARP did.

Now, you may be aware there have been some studies of this. Of course, it's very hard, you know, to do the counterfactual analysis, what would have happened had we not taken these actions, but economists do make estimates. And there was one I think that was particularly good that you may have seen by two economists, one who advised John McCain, Mark Zandy, another who worked in the Clinton

Administration, Alan Blinder, who's also at the Fed. And they said that without TARP and all the other things that the government did, unemployment would have likely topped 16 percent. We would have lost 8.5 million more jobs on top of what we lost. We would have had much higher deficits. And the nation would have likely entered what they called "a 1930's like Depression." So while the damage from the recession was deep and recovery has been slower than we would like, we fortunately did not experience anything on the scale of what we saw in the 1930's.

I also want to highlight a couple ways that TARP's impact on everyday life is perhaps more apparent. One is our actions to protect the broader economy by stabilizing the American auto industry.

Now, the auto industry was in decline before the crisis. But the decline became a potential free fall as we moved into the crisis. In 2008, the auto industry shed more than 400,000 jobs. By December, the situation was dire. With a deepening recession, credit markets frozen, Americans couldn't get auto loans, car sales were plummeting. GM and Chrysler were quickly running out of cash. Ford had basically wisely stockpiled cash.

So there were no options for private financing. And, therefore, the government, under TARP, stepped in as a lender of last resort, to prevent GM and Chrysler from collapsing. And the devastating



impact that would have had on our economy, which was already on the ropes, again, because of the circumstances of the time, government determined that we could not afford this. And again, the decision was initially made under the Bush Administration. The same conclusion was then reached under the Obama Administration.

The actions not only saved GM and Chrysler, they saved businesses up and down the auto industry supply chain. And they even helped Ford. Ford CEO, Alan Mulally, has many times acknowledged the importance of the government's action to Ford's own fortunes and whether Ford could have survived this crisis.

Some experts have estimated that as many as one million American jobs were saved as a result of the government's actions. And today the industry has come roaring back. GM, Chrysler, and Ford are all profitable. They are adding thousands of jobs and they are selling more cars. And Treasury is exiting the remaining investments we made.

Another way that TARP directly touched middle class Americans is by helping people keep their homes. Now, not since the 1930's have we seen a housing crisis on this scale. Crisis has many causes. Buying a home has always required responsibility on everyone's part. But in the years before the crisis, responsibility too often gave way to recklessness by many lenders who sold loans to people who couldn't

afford them, and also by buyers who knew they couldn't afford them. So we tried to help responsible homeowners. But that has been a far more complex challenge than we imagined.

Nevertheless, as a result of the actions we took, millions more families have avoided foreclosure than otherwise would have. And many families, through both the mortgage assistance programs, as well as the refinancing efforts, are spending less each month on their mortgage payments. And the good news is, the housing market is recovering with home prices rising at their fastest pace in seven years.

Let me now turn to cost. The true cost of the financial crisis, of course, is not the fiscal cost of these programs. The true cost is measured in the human suffering and the economic damage it caused. Again, there are estimates of this. The Dallas Fed recently put the number I think at 14 trillion in terms of the cost of the crisis.

The cost is the jobs lost, foreclosed homes, the college educations that cannot be financed, the retirements that must be postponed. And the most important measure of success of programs like TARP is, again, not a profit and loss statement, but whether the programs were successful in stopping the crisis and containing the damage.

Nevertheless, the fiscal cost of TARP is something that people are interested in. And the answer I think surprises many people.

Congress authorized up to \$700 billion for TARP. That's the number that most people still associate with it. A lot of people, of course, think that number went up in smoke, you know, you gave it out to a bunch of big banks, they paid it out in bonuses, we will never see it again.

And there were predictions that the TARP funds wouldn't be recovered and the cost of all of the interventions, when people looked at everything the Fed was doing, FDIC, the other actions of Treasury, those interventions would run into the trillions of dollars. I remember seeing one estimate that it would be \$23 trillion.

So perhaps we should remember the advice of Yogi Bear who famously said, "it's difficult to make predictions, especially about the future."

So in reality, and this chart will show you, for TARP, we dispersed about \$420 billion. We are still making some disbursements on the housing programs, but nothing else. Now, 420, that's a big number, but it's not 700. And the chart shows what we dispersed over time and what we've recovered.

The recoveries include all of Treasury's gains on AIG. There is a technical issue with some of that. Technically it's not put on the TARP balance sheet, but it's already come in, it's already in the door, it's already paid down the debt. So if we include all that as of a couple of weeks ago,

we had dispersed 420 billion, we've recovered 422. And our estimates are, when you look at all the government programs combined, tax payers are likely to realize a significant gain. Most of the programs are wound up, not all are, so some of those estimates have some – there's a variation in those, but still it looks like a significant profit.

I think another important fact about the record is, I think we operated TARP with the highest standards of transparency and accountability. And I say this about the standards that Neel Kashkari set when he first started implementing it, and then my predecessor, Herb Allison, who I worked with very closely and then continuing today.

We produce a wealth of reports on a yearly, monthly, and even daily basis. I venture to say if you go to our web site, you can find just about anything you want to know. It may take a little digging, clicking, but it's there.

We actually post on our web site a daily balance sheet, quite detailed. It lists all the programs, it lists what we dispersed, it lists how much has come back in repayments, it lists any write-offs or losses, how much is still outstanding, other income, it's all there, updated every day. Recently we launched a new tool on our web site to enable people to not only track the flow of funds, but then go quickly to the various events associated with the programs, find the program documents and so forth.

All the contracts are there, all the program guidelines. We've also been subject to oversight from four separate oversight agencies and their reports are available.

So TARP is by no means perfect. People sometimes ask me, you know, looking back now, what would you have done differently? I don't have the distance or objectivity to answer that today. But I think it's a very important discussion to have over time. I am sure there are things that could have been done better. But I do believe the government got the big things right.

So I've talked about what TARP did, where we are in the wind down. So what should be its legacy? Now, Ted mentioned at the outset, well, you know, some people would say, all right, these things may have helped contain the damage, but they worsened the moral hazard problem, the too big to fail problem. It really made it worse, you know.

And I think, you know, that really confuses the issue of what we had to do to respond to the crisis from what we must do to address the problems revealed by the crisis. I like to think of it this way, if your neighbor's home is burning down in the middle of the night because he fell asleep smoking in bed, and the fire is threatening your house and the whole neighborhood, do you want the fire department to come and put it out or do you say, no, let's let it burn down because that will teach all

those smokers a lesson? Well, I think TARP was like the fire department. It was called to put out the fire. But there is no question that any time the government provides assistance to private companies with tax payer dollars, we create a risk of moral hazard. Moral hazard is the risk that other institutions will think the government will come in to save them. That is a real problem. But you've got to contain the panic first and deal with that issue next, because if you don't, the costs are even greater.

So the crisis made clear that our regulatory system was out of date. We did not identify risks building up in the system, nor did we have the tools to deal with the crisis. And that's why the Obama Administration took up the mantle of financial reform and fought to pass the Dodd-Frank Act and other measures. And those reforms now being implemented will give us better tools to monitor risk and wind down large financial firms whose failure could threaten the system.

Those reforms will now require the largest financial institutions to hold more capital and undergo regular stress tests to see if they can determine, see if they can weather severe economic conditions. The reforms will bring more transparency to the derivatives market and they will create stronger safeguards for consumers. Now, there is still more work to do. The job is by no means finished. But the system is safer and stronger today. And the crisis also reminds us that the financial

system is dynamic and constantly changing. And so as sources of risk change, our regulation and oversight must keep pace.

So like the fire department that should not be blamed for the fact that people smoke in bed, I hope the legacy of TARP is thought of separately from the issue of, well, how do we regulate the financial system going forward.

So in that regard, let me conclude on this note. I've read a number of books about the financial crisis. One that I enjoyed the most was actually written by John Kenneth Galbraith. Now, for those of you who know something about John Kenneth Galbraith, you might be thinking, well, wait a minute, you know, he died in 2006, the financial crisis was 2008.

So he wrote a book about the Great Depression called The Great Crash, a small book. But, you know, there's a lot of wisdom in that little book that's relevant to our times. And one of the things he said that really stuck with me was that memory is far better than law as protection against financial allusion or insanity.

Now, the reason that stuck with me is, you know, I don't know if this is true for some of you, but, you know, I grew up with parents who were little kids during the Great Depression. They were living in Oklahoma and Kansas. Their parents were poor immigrants. And so, you

know, I heard stories about what was life like during the Great Depression. Many of you might have had the same experience. Maybe, you know, some of it were even closer to it personally, I don't know. And the experience for them of growing up in the Depression I think shaped their lives and their attitudes and the values they communicated to their children forever.

And, you know, today when we think of the Great Depression, we may have images of bread lines or tent cities for the homeless or maybe something out of Grapes of Wrath or whatever. But we are fortunate that as bad as the crisis was, the worse did not happen, of course. But that is, to me, all the more reason to remember how close we came and to think about what will be our memories of this crisis and what will we do with those memories.

We live in a time when the public's confidence in government's ability to solve big challenges has never been lower. Many of us rightly detest the partisanship and gridlock that has come to define this city and that is being carried out today.

But the great paradox of TARP is that while it was so unpopular, it was perhaps the best recent example of effective bipartisan government. A law was passed with bipartisan majorities in both Houses. The program was carried out quickly, and boldly, and wisely, I think, by



both a Republican and Democratic administration. There is actually quite a bit of continuity on what was done. So as TARP moves into the history books, my hope is that its greatest legacy will be this, that when the nation was confronted with an extraordinary challenge, in this case the potential collapse of our entire financial system, the government rose to the occasion. And if we remember that lesson, maybe we'll be better able to confront the challenges ahead. Thank you very much.

(Applause)

MR. ELLIOTT: Thank you very much for that clear exposition of TARP and of your views on it. Let me just ask you a few questions before we turn it over to the audience for their participation. And as Ted already mentioned in his remarks, I am personally a big fan of the TARP program. I think it was a very low cost way of achieving objectives that I personally would have been willing for us to pay much more for.

The large majority of economists feel the same way. There have been surveys on this and it's quite clear people in both parties from the economics profession largely share your views on the effectiveness of it.

I do a lot with the Europeans and when they talk about their banking systems, I run into a kind of TARP envy that they wish they had

been able to do. There were reasons why they couldn't, but they wish they had been able to do something early so they wouldn't still have the banking crisis they have. With all that said, that leaves – one major question is, why does everyone hate TARP so much? And as we look for lessons for the future, some of them will clearly be about communications. And I can identify at least three major communications decisions that I suspect were mistakes, though I believe there were arguments why they may have been inevitable mistakes.

The first was, and there is a question here, I do want your views on it, but the first was that the TARP was actually sold to Congress and the public as being a program to buy up toxic assets. It turned out to be used almost immediately in a very different way to inject capital.

MR. MASSAD: Right.

MR. ELLIOTT: Again, I personally think that was the right ultimate decision, but the communication message was very different. Second, and I'd have to go back to the wording of public statements, but certainly the public and Congress came away thinking TARP would lead to higher loan volumes, whereas, in fact, what it was only ever going to be able to do was to cut back on the massive decline in lending and eventually help lead to an increase.

So proponents of TARP ended up from the beginning having

to say that they weren't meeting the objectives the public thought they were trying to meet.

MR. MASSAD: Right.

MR. ELLIOTT: And third was almost more of a technical thing. But nothing was set up to show how the money was being used. And there are reasons why that actually wasn't a sensible question as it was generally posed. But it would have been easy to eliminate the question by doing various things.

MR. MASSAD: Right.

MR. ELLIOTT: First of all, would you largely agree with that synopsis? Do you think there are ways that could have been handled?

MR. MASSAD: You know, I think there clearly were communication things that could have been done differently and you've highlighted a couple that I would agree with. I'm not sure that would have really changed the public's view of a program that was taking huge amounts of tax payer dollars to subsidize private institutions, particularly when, as was inevitable, a lot of it went to very big banks, where people make large salaries, and particularly as Americans were starting to feel the brunt of the recession. That's simply a reality that I don't know that even had those communication issues been handled better, I'm not sure that would have changed things.

But, you know, I agree with you. And I think Secretary Paulson has said that the issue you mentioned on how it was rolled out was obviously a communications problem. And what happened was, the original idea was to focus on buying these toxic assets, these mortgage related assets. They quickly realized that they could not set up a way to do that where you could determine the value of those assets and administer it quickly enough. The crisis was just moving too fast.

So they had to move to investing, you know, equitably, essentially buying preferred stock. Now, interestingly, of course, that's what we did in the Great Depression, right. I mean initially the government tried to do loans, tried to do other things, and they moved to preferred stock. So there had been a path there.

On the issue of the lending, yeah, you know, in a recession, lending falls. And lending is both a supply and a demand issue. It's a question of whether the banks have the capital, as well as whether there is a demand. Plus, you had regulators who wanted to make sure banks weren't making imprudent loans. So lending was never going to go up. It was always a question of could you at least prevent the complete free fall.

On the last issue of kind of where did the money go, you know, it's an interesting issue. And I remember internal discussions. You know, there were those who said, well, you should track what the banks

are doing with the money. And there were, you know, many who thought, and I think in both the Republican and Democratic administrations, who thought, well, you know, capital is fungible. You know, if you invest – if you go buy IBM stock, you don't say what did they do with my \$1,000? I want to see what they did with my \$1,000. Well, you know, they get investments from lots of places and you can't track money that way. So there was a view that that was dishonest, to try to say that the TARP money was used for X, and then instead, we would report, you know, aggregate lending and other statistics.

Now, of course, the problem with that is, that doesn't quite resonate with Americans either, right, you know. If, you know, you make the median income of \$51,000 a year, and, you know, you get another, you know, you get a raise and you get \$2,000, and you come home and you tell your wife, I got a raise, \$2,000, and she says what are we going to do with this money, you know, should we, you know, buy a new car, you don't say, well, you know, money is fungible, and I can't really say whether it's this \$2,000 or our other \$51,000 that we're going to spend on that car, and people don't think that way. So people wanted to know, what did they do with the money. It's a perfectly reasonable question.

But the reality is that, you know, it's only through kind of aggregate measures that you can really say what's happening. But those aggregate

measures are not things that, you know, connect to people's lives. So my short answer is, I agree with your comments on communication failures, but I think at bottom the essence of this program is something that no one is ever going to like very much.

MR. ELLIOTT: It certainly seems to be the case. Another related set of criticisms effectively come down to, okay, maybe you really had to do something, maybe even it was largely like the TARP, but couldn't you have gotten a better deal?

MR. MASSAD: Right.

MR. ELLIOTT: Couldn't you have made the banks pay more for this? Couldn't you have insisted they cut back on bonuses because that would have helped restore the strength of the banking system and the bonuses were seen as repugnant to the public? Couldn't you have just gotten a better deal? It seems like you just sort of threw money out.

MR. MASSAD: Right. My short answer to this one is, boy, am I glad we can ask that question, you know. Isn't it wonderful that we can – and I mean this with all due respect, isn't it wonderful that we can sit here and discuss shouldn't we have made more profit on this thing? You know, the program – and the Republican administration set the initial terms, you know. In terms of the bank investments, for example, they basically set the economics. And they asked for, you know, a 5 percent

dividend rate. So was that below market? Yeah, absolutely it was below market. The market was – I mean there wasn't a market, right. No one would provide private capital. But could you have set it at 8 percent, 12 percent? Yeah, maybe. You might not have gotten as much participation because even though you say, well, you're helping the banks, why wouldn't they take the money? Well, you know, in a crisis, people don't necessarily, particularly financial institutions, don't necessarily act the way you would want them to in terms of what you feel is needed to save the system.

So, you know, I worked with Elizabeth Warren on the Congressional Oversight Panel initially when they looked at this, and they said, well, gee, you know, this is a subsidy, they should have charged more. But again, the fact was, it was deliberately done that way to get the money out quickly and to stabilize the system and then bring in private capital after that. And, you know, the government is not an investment fund. That's not why we did this. We did it to prevent a collapse of the financial system and it worked.

MR. ELLIOTT: Okay. And then my third question before we go to the audience is, what are the lessons for the future? Now, you've already talked about what's effectively the big lesson, is don't ever get in this situation again. We have had and will have many other events here in

which we talk about how to avoid that. But if in the future, and hopefully this will be many years hence if it were to happen, there needs to be a government intervention in a financial crisis, do you think any of the lessons that we can draw here are generalizable?

MR. MASSAD: Well, you know, again, I think the generalizable lesson to me, and I don't mean to sound Pollyannaish, but I think it is of some comfort in these times, is, you know, the government did step up in a time of crisis. I mean we did overcome our partisan differences and we were able to do the right thing.

Beyond that, you know, I think, again, we're trying today to attack the gaps in our regulatory system and the underlying causes of this crisis in ways that will ensure we don't have to do a program like this.

Now, of course, there will be more financial crisis and we don't know the sources of those. So whether the steps we're taking today will be enough, you know, only time will tell. I think one of the most important things, though, that we're doing today is trying to get beyond what has been essentially a regulatory system that was compartmentalized.

You know, we had the bank regulators, we had, you know, several of them. And then we had the SEC regulating securities. And then we had the CFTC regulating futures. And then we had, you know, so



we had various people doing various things. And there was not a vehicle for kind of looking at risk across the system. And what has been done through Dodd-Frank is to create that and create means to sort of look at risk as it might be building up across the system. That, to me, is one of the most important things we've done.

We've created the Financial Stability Oversight Counsel, where all the various regulators come together, as well as the Office of Financial Research, to try to look at, okay, where are the new risks coming from in our financial system. Time will tell if all that works. But I think that's, you know, one of the most important and underrated steps that we've taken.

MR. ELLIOTT: Okay. Thank you. Let me turn to the audience. And let me just give you a few ground rules. First of all, please make sure there is an actual question here. And if you do need to add a premise in order for the question to be understandable, please try to keep that condensed. Let's do just one question per person at a time. We may have time for additional questions from people later. And I think I should start with my boss, Ted Gayer. Oh, I should also say, please wait for the microphone and let us know who you are, except we know Ted already, so you can skip that one.

MR. GAYER: First of all, thanks again for coming. This is a clarifying question. The title is Wrapping Up the TARP. So my question

is, is it wrapped up, meaning there will be no more disbursements, or is it essentially a line of credit that will continue to exist –

MR. MASSAD: Yeah.

MR. GAYER: -- such that if a crisis or something comes up in the future, that we can just tap into – the government can tap into it again?

MR. MASSAD: A very good question. Our authority to make investments ended over three years ago, in basically October of 2010, in fact, actually when Dodd-Frank was passed. From that point in the summer, we couldn't implement any new programs. We were able after that point to make disbursements under the existing program.

But the only disbursements we will make going forward are for our housing assistance programs, where we're helping people modify mortgages. Recently we're working with states under what we call the Hardest Hit Fund Program, where we allocated money to the hardest hit fund states. We're working with Michigan and Ohio to use some of that money for demolition. But that's capped. Essentially all of those housing programs, the budget was 38 million, we've spent about 10. We won't even spend that remaining 28, maybe half of that or something. So it's not a line of credit.

In terms of wrapping it up then, those housing programs

continue for a number of years. I mean the reason those disbursements are made over time is, the mortgage assistance is structured on what we call a kind of pay for success basis. As long as the homeowner continues to meet his or her obligations, the government provides a little assistance. So those programs run for another five or so years. The payouts continue over that time.

On the investment side, we basically recovered everything other than, as I said, about 3 billion in investments in small banks and then about 20 or so in the auto industry, but we're getting that back pretty quickly. And hopefully in a fairly short time we'll be finished getting the auto investments back.

MR. GAYER: Okay. Next question in the red shirt there.

MR. CHECCO: Thank you. Larry Checco, Checco Communications and a very concerned citizen about this. Just a quick answer to why people – I think most of the people do not like TARP, and I'll use Mr. Massad's own analogy. I think the fire department went in and saved the smokers, as well as the house, and the smokers have not quit. They built bigger houses. Okay. But aside from that, I would just like to say that – or ask. My question is, you keep saying that the tax payers have profited on TARP. Where is that money going? Is it just going to the general funds or is it being allocated to get people back into the houses?

Because the banks did well.

MR. MASSAD: Right.

MR. CHECCO: Main Street is still suffering. Thank you.

MR. MASSAD: It goes into the general fund. It pays down the debt. It's not recycled.

MR. CHECCO: Not –

MR. MASSAD: It's like your income tax check. I mean it goes to the same place.

MR. GAYER: Okay. Actually right back there.

MR. BARON: Hi. Richard Baron. Was TARP originally set up to be a five year program, or why now, and what forces in the market or the government have basically let it come to such a quick end?

MR. MASSAD: Yeah, I think the original expectation was that it would take a lot longer to get the investments back. And I think the reason that we've been able to get out fairly quickly is the same reason as the recovery was actually, you know, faster than a lot of people expected given the severity of the crisis. And, to me, that is because of the overwhelming force of the response to the crisis, the fact that the government really, you know, threw the kitchen sink at the problem.

That enabled us to climb back faster. And therefore, you know, the investments – we were able to get private capital back into

these industries and get the government out.

MR. GAYER: Okay. On the aisle over here.

MR. TRACY: Hi, Mr. Secretary. Ryan Tracy with the Wall Street Journal.

MR. MASSAD: Yeah.

MR. TRACY: One of the ways that Treasury has been getting private capital out, as you say, is auctioning off the stakes and banks, and the public doesn't know in the individual transactions who is buying the stake, and that's raised, you know, some criticism that there may be private sector entities, hedge funds, or private equity or whoever that's buying these on the cheap end, you know, maybe getting enriched by the fact that the government is sort of unwinding. So I wanted to ask first, why haven't you disclosed who you're selling those stakes to? And second, what do you think of that criticism that there's some unjust enrichment there?

MR. MASSAD: Well, what we've done is, we've set up an auction platform that's open, you know, so it's competitive. So I don't think there's any unjust enrichment in the sense that, you know, any institution can participate in the auctions. And by institution, you know, anyone who qualifies under the securities laws. We were advised by the Security and Exchange Commission I guess that we shouldn't have it be individuals,

but, you know, it's any company essentially.

We haven't disclosed who buys the securities for the same reasons, you know, that Treasury doesn't disclose, you know, the particular buyers in a government, you know, in a Treasury bills auction. I mean there's lots of auctions the government runs where they don't disclose the buyers. I think if you did, you know, you might dampen participation. And I don't think most people, you know, most people care to the extent they follow this. They care about, you know, are we getting out of this or are we getting our money back and that's what we're doing.

MR. GAYER: Okay. Next question. Keep going.

MS. GARCIA: Jillian Garcia. This is an un-American question. If this was such a profitable deal for the government, why don't you continue doing it?

MR. MASSAD: Oh no. You know, again, the profit is not the main measure of success. And, you know, it was terrible that we had to do this. It was awful that we had to take tax payer dollars and do this at a time when we're cutting so many other programs that, you know, people need. So, you know, the fact that we've recovered the money is good, but I don't want to have to do it again.

MR. ELLIOTT: I might add, I've written a book on the federal credit program. It's an area of interest to me. The government, because it

can borrow so cheaply, could essentially make money out of almost any lending program it wants. So there are always a lot of public reasons why we don't go and do that. And certainly I know that the intent was never to come out with a profit on this. It's fantastic that there's a very small profit on this. Perhaps not even – I don't know if you've done the numbers. Is it enough to pay for what Treasury had to pay on the borrowings to support this?

MR. GAYER: We haven't done those –

MR. ELLIOTT: They haven't done the numbers because it was just never of the essence of what the program was about. Chala all the way in the back there.

CHALA: Thank you. Chala (inaudible) IMF. TARP, a lot of lessons for many, especially Europeans, as Doug mentioned. One question, though. You didn't mention Fannie and Freddie and the contingent claims in the GSE's. How does that tie with the fiscal (inaudible)

MR. MASSAD: Sure. So I didn't mention Fannie and Freddie because technically that was outside of the TARP program. There was a separate law that addressed that. You know, the numbers as of today on Fannie and Freddie are that the government invested about 188 billion. It's recovered almost 150 billion. Companies are profitable, so

they will continue to pay dividends.

Now, what happens in the future, though, is really now being focused on in the context of what do we do about the housing finance system, and that's really where the focus should be. What should we do with these entities? And the President has made very clear that the entities should not continue to exist, you know, in their current form. We need to, you know, shrink the government's footprint in the market.

So, you know, the ultimate recovery on the GSC's kind of depends on the timing of that reform effort, what happens in that reform effort and so forth. But, you know, as of today, we're getting pretty close to getting all the money back.

The made a statement that the overall programs, if you look at everything combined, there will likely to be a profit, of course, because that's, you know, the Federal Reserve did a number of programs and the estimates on those are pretty significant profits.

MR. GAYER: Okay. Next question.

MR. WALLACH: Hi. I'm Phil Wallach from Brookings. You said rightly that we did not nationalize AIG or any of these other companies, but we became a nearly 80 percent shareholder in AIG. Now, there's still outstanding lawsuits by the remaining 20 percent of the shareholders saying that their interests were not properly looked after



once the Treasury became the 80 percent stakeholder. So I was just wondering if you could talk about how Treasury thought of what it means to be an 80 percent shareholder in terms of its relationship to the management of the companies?

MR. MASSAD: Yeah, sure. So we actually articulated some principals that would govern all of our investments. And what we said was that Treasury is a shareholder because of the fact that we had to act to, you know, break the back of the panic, deal with the crisis. But we're not like a normal commercial shareholder, and therefore, we're not going to get involved in day to day management of any of these companies. And it would be a bad thing for the government to get involved in day to day management of these companies.

And we said we would basically limit our exercise of voting rights to kind of core things that would affect our investment and the ability to exit our investment. Election of directors, amendments to the charter of a company, mergers and acquisitions and things like that, and kind of, you know, changes in the capital structure basically, and that's pretty much, you know, what we've done throughout.

Now, in some cases we've, you know, all the cases we worked very closely with the companies on how we exit. We worked very closely with AIG on that. We're now working with Ally on that. We're

almost out of GM and so forth. But that's kind of been our philosophy.

You know, in the case of AIG in particular, you know, we actually at one point held 92 percent of the common stock. And the other thing we did in a lot of these companies, you know, we did demand changes in management up front. So, for example, in the case of AIG, you know, the Federal Reserve made the initial investments. You know, the CEO was changed, the Board was changed. The same was true in some of these other companies. And obviously in the case of GM and Chrysler, where we conditioned the assistance on pretty dramatic structural changes up front that required sacrifices of all the constituencies, that was the condition that President Obama set for continuing to provide assistance. But once that was done, you know, we didn't tell them what cars to make, what color to paint the cars, you know, any of that.

MR. GAYER: Okay. Over there.

MR. BRODSKY: I'm Mark Brodsky, retired physicist and CEO. You gave an example of a contra factual analysis about TARP. Is there any such analysis about Glass-Steagall, and had that not been repealed, would that have alleviated in any way the crisis? And what's your view on reinstating the separations that were in Glass-Steagall about banking?

MR. MASSAD: Yeah. You know, I think, as many people have noted, it's hard to directly connect repeal of Glass-Steagall to institutions that failed just given that, you know, a lot of the banks – it was really separate investment banks initially that failed, not those that were combined. You know, my portfolio is not the financial reform portfolio, so I'm not going to go too far down this path with you. But, you know, I think the view of Treasury is that let's focus on implementing the reforms that we've adopted through Dodd-Frank as the tool to address these issues and these risks because we've got a lot on our plate through that.

Obviously, the Bocca Rule, which is part of these reforms, does say we do want to limit the ability of these large institutions to engage in proprietary trading. But let me kind of leave it at that if I may.

MR. GAYER: Okay. Next question. All the way in the back there.

MR. WAPLE: Hello. My name is Bared Waple. I'm with the Congressional Research Service. You mentioned Ally, which is the largest amount outstanding at this point and has been sitting there –

MR. MASSAD: Yeah.

MR. WAPLE: -- I think because of the Res Cap situation. And I just wonder if you might want to comment on if there's any time table or when –

MR. MASSAD: Sure, I'd be happy to. So Ally financial used to be called GMAC. It was the auto lending arm of GM, but GM spun it off, separated it from GM. The government initially, again, under the Bush Administration, and then continued under Obama, provided funds to Ally, as well as to the Chrysler financing arm, because had it not done so, the effort to save the auto companies themselves would not have worked. If people can get loans to buy cars, and if dealers can't get loans to get cars on their lots, then whatever you're doing for the auto companies is for not. So the government provided assistance to the auto financing companies.

On Ally, we provided a total of 17. We've gotten back roughly 6 already. We've recently announced transactions that, assuming we get approval from the Federal Reserve, because they're subject to Federal Reserve approval, we will get another six billion back. They've largely worked through the Res Cap problem now. There's not a final order. They had a mortgage subsidiary which had a lot of problems, as many mortgage companies did, and they put it into Chapter 11, and they've just about completed that process.

That was one of the strategic initiatives that we agreed they should undertake. And so we're hoping that fairly soon we'll get another six billion back and we'll be left with about five. And we're very confident that we can exit that remaining five in the near future. But we won't announce

the precise plan to do that until we're actually ready to pull the trigger on it.

MR. GAYER: Okay. How about over there?

MR. ROLE: Ron Role with The Deal. A lot of the community banks that are part of the TARP program have their dividends, they're about to increase from 5 to 9 percent shortly. And I'm just wondering what your response will be if something starts balking at this issue and some of them can't afford it and –

MR. MASSAD: Right.

MR. ROLE: -- that kind of issue. And a lot of, you know, I guess there's over 100 banks (inaudible) Thank you.

MR. MASSAD: Yeah, there's about 100 banks left. So first of all, dividends are not like, you know, your payments on your car loan or your mortgage loan, right. Dividends have to be declared by the Board. If a bank can't pay the dividends, there's no default. You don't go into bankruptcy because you failed to pay the dividends, you just don't pay the dividends.

In many of our investments, the dividends accumulate, meaning if they didn't declare it and pay it to us in that corner, it's still there. They're supposed to pay it before they can pay their common shareholders. But it can never cause them to go under. And they always must have regulatory approval to pay those dividends.

So, as you know, the dividend rate does go up. That was done because the thinking was, well, after five years, we want to incentivize all the banks to repay. In fact, the initial terms of the program prohibited repayments for three years. So again, going back to the question earlier, how we got out so quickly, you know, you can see people's thinking originally was, this was going to take much longer. The fact that the rate goes up from 5 to 9 percent, we took that into account when we came up with our exit plan. And our exit plan was, let's look at the portfolio. We did this about a year and a half ago when there were 350 banks. And we said, some of the banks we know, or we think, are going to be able to repay us sometime in the near future, you know, because we do an analysis of all of them, we have advisors that help us analyze those. We said we will wait for them to repay.

Then we looked at others and we said, it's very unlikely they can repay. And even the banks in most cases would say to us, yeah, we're not sure how we're ever going to repay. And those are the ones that we decided to auction off basically. In some cases where the bank wanted to restructure and was trying to bring in private capital to restructure, we're working with them on that.

But basically for the banks that can repay, when 5 percent goes to 9 percent, they're saying to themselves, well, yeah, that will

incentivize our repayment. For those that can't repay and aren't paying dividends, when 5 percent goes to 9 percent, you know, they weren't paying us 5 percent, they're not going to pay us 9 percent. But, you know, we are auctioning those off and we're finding, you know, we're getting pretty good prices on those because there are many investors who are willing to say to themselves, well, I'll take this risk, I'll hold it for a longer period of time, and maybe, you know, down the road, it'll turn around.

MR. GAYER: Okay. How about there?

MR. PRICE: This is Lee Price at the FDIC. I want to raise a question about moral hazard, but it relates to a problem I have with one of the arguments you make about this being the best recent example of effective bipartisan government. You don't mention the fact that it failed in the House the first time it came along. And the Congress was not happy with it. And then the financial markets went wild and they finally did pass it because of that, and let's hope that that isn't required this time, this fall when we face some difficult efforts in trying to find bipartisan support for these.

But what Doug had referred to as a communication issue, well, it may be related to the political issue of whether this was going to be troubled assets or this was going to be investment in the banks. And what the public I think sees is, we invested in the banks. We didn't take

troubled assets and deal with the system problem, we dealt with the individual banks.

And then we didn't really – there were a few cases, but not the big, prominent ones where we left the management in place and we let them pay enormous bonuses a year later, bonuses that could never have been paid but for the fact that we rescued them. The government stepped in, rescued them, and then they were paying big bonuses a year later. And so don't you think there's a problem? I know you're reluctant to look at the legacy, but if we're going to look at the legacy, shouldn't the legacy be that we haven't really dealt with the moral hazard of leaving people in place and letting them pay themselves big bonuses a year later after the government bailed them out?

MR. MASSAD: Well, yeah, I'd say a couple things.

MR. PRICE: And a program that was sold on one basis and then delivered on another.

MR. MASSAD: Okay. So on the issue of bonuses and executive compensation, actually, you know, I think you know, there were put in place executive compensation restrictions. And we then did have a special master for executive compensation who reviewed the compensation of the top 25 individuals in the top institutions and forced massive changes in their compensation, basically cut compensation by



about 95 percent, forced most of it into stock as opposed to cash.

In the case of AIG even, most of those bonuses weren't paid. A lot of them were recovered. But, you know, I don't disagree that the fact that people at a lot of these big banks make far, far, far more than most Americans make left people with a bad taste for all of this. As to, you know, we didn't force enough changes, you know, had you purchased troubled assets, you wouldn't have forced changes in the banks either. In fact, you probably would have forced fewer changes, right, because you just would have taken the bad assets off their balance sheets.

I think the issue of forcing the banks to change is, again, one that is an issue for the reform of the system, as well as for the regulators, for the FDIC, and for the Fed and so forth. It wasn't Treasury's job to regulate the banks. Our job was to provide the assistance and, you know, purchase the financial instruments and then get out.

But it seems to me that the issues of how should these banks operate, are they taking on too much risk, what changes should we require is one that we are addressing through Dodd-Frank and all those reforms, as well as one that is clearly on the regulator's plate.

MR. GAYER: Okay. And we've actually run out of time. But thank you all. And thank you very much, Secretary Massad.

MR. MASSAD: Thank you.

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