UNITED STATES DEPARTMENT OF THE TREASURY

The Financial Stability Plan:

Deploying our Full Arsenal to Attack the Credit Crisis on All Fronts

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Today, our nation faces the most severe financial crisis since the Great Depression. It is a crisis of confidence, of capital, of credit, and of consumer and business demand. Rather than providing the credit that allows new ideas to flourish into new jobs, or families to afford homes and autos, we have seen banks and other sources of credit freeze up – contributing to and potentially accelerating what already threatens to be a serious recession. Restarting our economy and job creation requires both jumpstarting economic demand for goods and services through our American Recovery and Reinvestment Act and simultaneously ensuring through our new Financial Stability Plan that businesses with good ideas have the credit to grow and expand, and working families can get the affordable loans they need to meet their economic needs and power an economic recovery.

To address the financial crisis, the Financial Stability Plan is designed to attack our credit crisis on all fronts with our full arsenal of financial tools and the resources commensurate to the depth of the problem. To be successful, we must address the uncertainty, troubled assets and capital constraints of our financial institutions as well as the frozen secondary markets that have been the source of around half of our lending for everything from small business loans to auto loans.

To protect taxpayers and ensure that every dollar is directed toward lending and economic revitalization, the Financial Stability Plan will institute a new era of accountability, transparency and conditions on the financial institutions receiving funds. To ensure that we are responding to this crisis as one government, Secretary Timothy Geithner -- working in collaboration and joined by Federal Reserve Chairman Ben Bernanke, FDIC Chair Sheila Bair, Office of Thrift Supervision Director John Reich and Comptroller of the Currency John Dugan – is bringing the full force and full range of financial tools available to cleaning up lingering problems in our banking system, opening up credit and beginning the process of financial recovery.

Financial Stability Plan

1. Financial Stability Trust:
   - A Comprehensive Stress Test for Major Banks
   - Increased Balance Sheet Transparency and Disclosure
   - Capital Assistance Program
2. Public-Private Investment Fund ($500 Billion - $1 Trillion)
3. Consumer and Business Lending Initiative (Up to $1 trillion)
4. Transparency and Accountability Agenda – Including Dividend Limitation
5. Affordable Housing Support and Foreclosure Prevention Plan
6. A Small Business and Community Lending Initiative

FINANCIAL STABILITY PLAN

1. **Financial Stability Trust**: A key aspect of the Financial Stability Plan is an effort to strengthen our financial institutions so that they have the ability to support recovery. This Financial Stability Trust includes:

- **A Comprehensive Stress Test: A Forward Looking Assessment of What Banks Need to Keep Lending Even Through a Severe Economic Downturn**: Today, uncertainty about the real value of distressed assets and the ability of borrowers to repay loans as well as uncertainty as to whether some financial institutions have the capital required to weather a continued decline in the economy have caused both a dramatic slowdown in lending and a decline in the confidence required for the private sector to make much needed equity investments in our major financial institutions. The Financial Stability Plan will seek to respond to these challenges with:

  - *Increased Transparency and Disclosure*: Increased transparency will facilitate a more effective use of market discipline in financial markets. The Treasury Department will work with bank supervisors and the Securities and Exchange Commission and accounting standard setters in their efforts to improve public disclosure by banks. This effort will include measures to improve the disclosure of the exposures on bank balance sheets. In conducting these exercises, supervisors recognize the need not to adopt an overly conservative posture or take steps that could inappropriately constrain lending.

  - *Coordinated, Accurate, and Realistic Assessment*: All relevant financial regulators -- the Federal Reserve, FDIC, OCC, and OTS -- will work together in a coordinated way to bring more consistent, realistic and forward looking assessment of exposures on the balance sheet of financial institutions.

  - *Forward Looking Assessment – Stress Test*: A key component of the Capital Assistance Program is a forward looking comprehensive "stress test" that requires an assessment of whether major financial institutions have the capital necessary to continue lending and to absorb the potential losses that could result from a more severe decline in the economy than projected.

- Requirement for $100 Billion-Plus Banks: All banking institutions with assets in excess of $100 billion will be required to participate in the coordinated supervisory review process and comprehensive stress test.

- **Capital Assistance Program**: While banks will be encouraged to access private markets to raise any additional capital needed to establish this buffer, a financial institution that has undergone a comprehensive "stress test" will have access to a Treasury provided "capital buffer" to help absorb losses and serve as a bridge to receiving increased private capital. While most banks have strong capital positions, the Financial Stability Trust will provide a capital buffer that will: Operate as a form of "contingent equity" to ensure firms the capital strength to preserve or increase lending in a worse than expected economic downturn. Firms will receive a preferred security investment from Treasury in convertible securities that they can convert into common equity if needed to preserve lending in a worse-than-expected economic environment. This convertible preferred security will carry a dividend to be specified later and a conversion price set at a modest discount from the prevailing level of the institution's stock price as of February 9, 2009. Banking institutions with consolidated assets below $100 billion will also be eligible to obtain capital from the CAP after a supervisory review.
- **Financial Stability Trust**: Any capital investments made by Treasury under the CAP will be placed in a separate entity – the Financial Stability Trust – set up to manage the government's investments in US financial institutions.

2. **Public-Private Investment Fund**: One aspect of a full arsenal approach is the need to provide greater means for financial institutions to cleanse their balance sheets of what are often referred to as "legacy" assets. Many proposals designed to achieve this are complicated both by their sole reliance on public purchasing and the difficulties in pricing assets. Working together in partnership with the FDIC and the Federal Reserve, the Treasury Department will initiate a Public-Private Investment Fund that takes a new approach.

- **Public-Private Capital**: This new program will be designed with a public-private financing component, which could involve putting public or private capital side-by-side and using public financing to leverage private capital on an initial scale of up to $500 billion, with the potential to expand up to $1 trillion.
- **Private Sector Pricing of Assets**: Because the new program is designed to bring private sector equity contributions to make large-scale asset purchases, it not only minimizes public capital and maximizes private capital: it allows private sector buyers to determine the price for current troubled and previously illiquid assets

3. **Consumer & Business Lending Initiative – Up to $1 Trillion**: Addressing our credit crisis on all fronts means going beyond simply dealing with banks. While the intricacies of secondary markets and securitization – the bundling together and selling of loans – may be

complex, they account for almost half of the credit going to Main Street as well as Wall Street. When banks making loans for small businesses, commercial real estate or autos are able to bundle and sell those loans into a vibrant and liquid secondary market, it instantly recycles money back to financial institutions to make additional loans to other worthy borrowers. When those markets freeze up, the impact on lending for consumers and businesses – small and large – can be devastating. Unable to sell loans into secondary markets, lenders freeze up, leading those seeking credit like car loans to face exorbitant rates. Between 2006 and 2008, there was a net $1.2 trillion decline in securitized lending (outside of the GSEs) in these markets. That is why a core component of the Financial Stability Plan is:

- **A Bold Expansion Up to $1 Trillion**: This joint initiative with the Federal Reserve builds off, broadens and expands the resources of the previously announced but not yet implemented Term Asset-Backed Securities Loan Facility (TALF). The Consumer & Business Lending Initiative will support the purchase of loans by providing the financing to private investors to help unfreeze and lower interest rates for auto, small business, credit card and other consumer and business credit. Previously, Treasury was to use $20 billion to leverage $200 billion of lending from the Federal Reserve. The Financial Stability Plan will dramatically increase the size by using $100 billion to leverage up to $1 trillion and kick start lending by focusing on new loans.
- **Protecting Taxpayer Resources by Limiting Purchases to Newly Packaged AAA Loans**: Because these are the highest quality portion of any security -- the first ones to be paid -- we will be able to best protect against taxpayer losses and efficiently leverage taxpayer money to support a large flow of credit to these sectors.
- **Expand Reach – Including Commercial Real Estate**: The Consumer & Business Lending Initiative will expand the initial reach of the Term Asset-Backed Securities Loan Facility to now include commercial mortgage-backed securities (CMBS). In addition, the Treasury will continue to consult with the Federal Reserve regarding possible further expansion of the TALF program to include other asset classes, such as non-Agency residential mortgage-backed securities (RMBS) and assets collateralized by corporate debt.

4. **New Era of Transparency, Accountability, Monitoring and Conditions**: A major and legitimate source of public frustration and even anger with the initial deployment of the first $350 billion of EESA funds was a lack of accountability or transparency as to whether assistance was being provided solely for the public interest and a stronger economy, rather than the private gain of shareholders, bondholders or executives. Going forward, the Financial Stability Plan will call for greater transparency, accountability and conditionality with tougher standards for firms receiving exceptional assistance. These will be the new standards going forward and are not retroactive. These stronger monitoring conditions were informed by recommendations made by formal oversight groups – the Congressional Oversight Panel, the Special Inspector General, and the Government Accountability Office -- as well as Congressional committees charged with oversight of the banking system.

- ***Requiring Firms to Show How Assistance from Financial Stability Plan Will Expand Lending***: The core of the new monitoring requirement is to require recipients of exceptional assistance or capital buffer assistance to show how every dollar of capital they receive is enabling them to preserve or generate new lending compared to what would have been possible without government capital assistance.

- *Intended Use of Government Funds*: All recipients of assistance must submit a plan for how they intend to use that capital to preserve and strengthen their lending capacity. This plan will be submitted during the application process, and the Treasury Department will make these reports public upon completion of the capital investment in the firm.
- *The Impact on Lending Requirement*: Firms must detail in monthly reports submitted to the Treasury Department their lending broken out by category, showing how many new loans they provided to businesses and consumers and how many asset-backed and mortgage-backed securities they purchased, accompanied by a description of the lending environment in the communities and markets they serve. This report will also include a comparison to their most rigorous estimate of what their lending would have been in the absence of government support. For public companies, similar reports will be filed on an 8K simultaneous with the filing of their 10-Q or 10-K reports. Additionally, the Treasury Department will – in collaboration with banking agencies – publish and regularly update key metrics showing the impact of the Financial Stability Plan on credit markets. These reports will be put on the Treasury FinancialStability.gov website so that they can be subject to scrutiny by outside and independent experts.
- *Taxpayers' Right to Know*: All information disclosed or reported to Treasury by recipients of capital assistance will be posted on FinancialStability.gov because taxpayers have the right to know whether these programs are succeeding in creating and preserving lending and financial stability.

- **Committing Recipients to Mortgage Foreclosure Mitigation**: All recipients of capital investments under the new initiatives announced today will be required to commit to participate in mortgage foreclosure mitigation programs consistent with guidelines Treasury will release on industry standard best practices.
- **Restricting Dividends, Stock Repurchases and Acquisitions**: Limiting common dividends, stock repurchases and acquisitions provides assurance to taxpayers that all of the capital invested by the government under the Financial Stability Trust will go to improving banks' capital bases and promoting lending. All banks that receive new capital assistance will be:
  - *Restricted from Paying Quarterly Common Dividend Payments in Excess Of $0.01 Until the Government Investment Is Repaid*: Banks that receive exceptional assistance can only pay $0.01 quarterly. That presumption will be the same for firms that receive generally available capital unless the Treasury Department and their primary regulator approve more based on their assessment that it is consistent with reaching their capital planning objectives.
  - *Restricted from Repurchasing Shares*: All banks that receive funding from the new Capital Assistance Program are restricted from repurchasing any privately-held shares,

subject to approval by the Treasury Department and their primary regulator, until the government's investment is repaid.

  - *Restricted from Pursuing Acquisitions*: All banks that receive capital assistance are restricted from pursuing cash acquisitions of healthy firms until the government investment is repaid. Exceptions will be made for explicit supervisor-approved restructuring plans.

- **Limiting Executive Compensation**: Firms will be required to comply with the senior executive compensation restrictions announced February 4th, including those pertaining to a $500,000 in total annual compensation cap plus restricted stock payable when the government is getting paid back, "say on pay" shareholder votes, and new disclosure and accountability requirements applicable to luxury purchases.
- **Prohibiting Political Interference in Investment Decisions**: The Treasury Department has announced measures to ensure that lobbyists do not influence applications for, or disbursements of, Financial Stability Plan funds, and will certify that each investment decision is based only on investment criteria and the facts of the case.
- **Posting Contracts and Investment Information on the Web**: The Treasury Department will post all contracts under the Financial Stability Plan on FinancialStability.gov within five to 10 business days of their completion. Whenever Treasury makes a capital investment under these new initiatives, it will make public the value of the investment, the quantity and strike price of warrants received, the schedule of required payments to the government and when government is being paid back. The terms of pricing of these investments will be compared to terms and pricing of recent market transactions during the period the investment was made, if available.

5. **Housing Support and Foreclosure Prevention**: There is bipartisan agreement today that stemming foreclosures and restructuring troubled mortgages will help slow the downward spiral harming financial institutions and the real American economy. Many Congressional leaders, housing advocates, and ordinary citizens have been disappointed that the Troubled Asset Relief Program was not aimed at ending the foreclosure crisis. We will soon be announcing a comprehensive plan that builds on the work of Congressional leaders and the FDIC. Among other things, our plan will:
   - **Drive Down Overall Mortgage Rates**: The Treasury Department and the Federal Reserve remain committed to expand as necessary the current effort by the Federal Reserve to help drive down mortgage rates – freeing up funds for working families – through continuation of its efforts to spend as much as $600 billion for purchasing of GSE mortgage-backed securities and GSE debt.
   - **Commit $50 Billion to Prevent Avoidable Foreclosures** of owner-occupied middle class homes by helping to reduce monthly payments in line with prudent underwriting and long-term loan performance.
   - **Help Bring Order and Consistency** to the various efforts to address the foreclosure crisis by establishing loan modification guidelines and standards for government and private programs.

- **Require All Financial Stability Plan Recipients to Participate in Foreclosure Mitigation Plans** consistent with Treasury guidance.
- **Build Flexibility into Hope for Homeowners and the FHA** to enable loan modifications for a greater number of distressed borrowers.

6. **<u>Small Business and Community Lending Initiative</u>**: Few aspects of our current financial crisis have created more justifiable resentment than the specter of hard-working entrepreneurs and small business owners seeing their companies hurt and even bankrupt because of a squeeze on credit they played no role in creating. Currently, the increased capital constraints of banks, the inability to sell SBA loans on the secondary market and a weakening economy have combined to dramatically reduce SBA lending at the very time our economy cannot afford to deny credit to any entrepreneur with the potential to create jobs and expand markets. Further adding to this frustration is the sense that community banks – which still engage in relationship lending that serves their local communities -- have been overlooked not just during this crisis, but over the last several years.

Over the next several days, President Obama, the Treasury Department and the SBA will announce the launch of a Small Business and Community Bank Lending Initiative: This effort will seek to arrest the precipitous decline in SBA lending – down 57 percent last quarter from the same quarter a year earlier for the flagship 7(a) loans through:

- **Use of the Consumer &Business Lending Initiative** to finance the purchase of AAA-rated SBA loans to unfreeze secondary markets for small business loans.
- **Increasing the Guarantee for SBA Loans to 90%:** The Administration is seeking to pass in the American Recovery and Reinvestment Act an increase in the guarantee of SBA loans from as low as 75% to as high as 90%.
- **Reducing Fees for SBA 7(a) and 504 Lending and Provide Funds for Both Oversight and Speedier and Less Burdensome Processing of Loan Applications**.