

The Alphabet Soup of the Financial System Bailout

By Carol Hempfling Pratt

A glossary of programs administered by the Treasury, the FDIC and the Federal Reserve.

TARP, TALF, TGLP ... Help!!! Ever since Congress passed the Emergency Economic Stabilization Act on October 3, 2008, the Secretary of the Treasury, the Federal Deposit Insurance Corporation (FDIC) and the Federal Reserve have been working at a feverish pace to come up with solutions to the unprecedented crisis in the financial markets. These efforts have resulted in an overwhelming number of new plans and programs—each with its own acronym. As a result, professionals in the banking and financial services industry have a whole new language to learn. This article aims to provide a glossary for this new language, to help make sense of the most commonly used terms and show how they relate to each other.

Rather than list all terms alphabetically, this glossary first defines the statutes and statutory terms, then groups alphabetically the programs sponsored by the U.S. Treasury (“the Treasury”), by the FDIC and by the Federal Reserve (through the Federal Reserve Bank of New York, or FRBNY).

Statutes and Statutory Terms

Congress has passed two statutes—EESA and ARRA—targeted at the crisis in our financial system. Within the statutory language of the EESA, the ubiquitous acronym TARP was born.

ARRA—*American Recovery and Reinvestment Act*—signed by President Barack Obama on February 17, 2009, is a \$789 billion stimulus bill that includes tax cuts as well as spending on health care, education, infrastructure, low-income aid, energy, housing, scientific research and more. ARRA amended the

executive compensation rules included in EESA, with retroactive application to existing participants in the CPP.

EESA—*Emergency Economic Stabilization Act of 2008*—is the \$700 billion bailout bill enacted on October 3, 2008, under which the term TARP (Troubled Assets Relief Program) was coined. EESA granted authority to the Secretary of the Treasury to purchase troubled assets from financial institutions and to insure or guarantee troubled assets, with “troubled assets” defined as residential or commercial mortgages and mortgage-backed securities. EESA also included a catchall grant of authority to purchase “any other financial instrument” that the Secretary of the Treasury, in consultation with the Federal Reserve chairman, deems necessary to promote financial market stability. The Secretary of the Treasury has established multiple market stabilization programs under the TARP umbrella, including investing in equity securities of financial institutions (through the CPP/CAP) under his authority to “purchase any other financial instrument”

TARP—*Troubled Assets Relief Program*—is the term coined by Congress to refer to the authority granted to the Secretary of the Treasury under the EESA. TARP is the umbrella spanning all of the programs sponsored by the Treasury under EESA authority, including the CPP, CAP, credit protection under TALF, PPIP, the SSFI Program, the TIP, the AGP and the “Making Home Affordable” program. The Secretary of the Treasury also used his TARP authority to bail out GM and Chrysler under the Automotive Industry Financing Program.

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Programs Primarily Sponsored by U.S. Treasury and Related Terms

The TARP authority granted to the Secretary of the Treasury under the EESA has spawned a confusing number of programs and related terms in a short period of time. The Treasury is also collaborating with the FDIC and the Federal Reserve with respect to programs primarily sponsored by those agencies (TALF, LLP), which are described below.

AGP—*Asset Guarantee Program*—enables the Treasury to guarantee certain assets of systemically significant institutions, with eligibility and participation determined on a case-by-case basis. An AGP asset guarantee was included as part of the Citigroup bailout.

CAP—*Capital Assistance Program*—the successor to the CPP, is the second vehicle under which the Treasury will provide capital to qualifying financial institutions (QFIs, see below). Under the CAP, the Treasury will purchase preferred stock of QFIs through a separate entity—the Financial Stability Trust (FST)—set up to manage the government’s investments in financial institutions. The securities issued under the CAP will be convertible preferred stock with a nine-percent dividend, compounding quarterly, together with warrants to purchase a number of shares of the QFI’s common stock equal to 20 percent of the preferred stock investment amount divided by the market price. The securities convert into common stock: at any time at the option of the QFI (with approval of the QFI’s primary federal regulator); upon certain events (such as merger of the QFI) at the option of the Treasury; and mandatorily after seven years. The program is open to all QFIs, but the 19 institutions with more than \$100 billion in assets were required to participate in a stress test conducted by the banking regulators; if the regulators determine that an additional capital buffer is needed, these institutions will be required to commit to participate in the CAP but will have six months to raise private capital instead. CAP funds may be used to repay CPP funds, but the same executive compensation restrictions apply to both programs.

CBLI—*Consumer and Business Lending Initiative*—represents the Treasury’s announced intention to expand its TALF commitment from \$20 billion to

up to \$100 billion in TARP funds (with a possible increase in the FRBNY’s TALF leverage from \$200 billion to up to \$1 trillion). Under the CBLI, the Treasury and the Federal Reserve also announced the intention to expand the types of loan pools eligible for financing under the TALF to include commercial mortgage-backed securities (CMBS) and others that the Treasury and the Federal Reserve determine to be appropriate. The CBLI is also the program under which the Treasury announced the intention (under the title “Unlocking Credit for Small Businesses”) to directly purchase securities backed by Small Business Administration (SBA) loans and to make other changes in the SBA program (including higher loan guarantees and reduced fees) intended to induce lenders to make more SBA loans available.

CPP—*Capital Purchase Program*—announced by Treasury Secretary Henry Paulson less than two weeks after EESA was enacted, is a program under which \$250 billion of the EESA funding was earmarked by the Treasury to purchase equity stakes in U.S. financial institutions. At the time that the CPP was announced, nine large financial institutions had already agreed to participate, including Bank of America, Bank of New York Mellon, Citigroup, Goldman Sachs, JPMorgan Chase, Merrill Lynch, Morgan Stanley, State Street Corporation and Wells Fargo. Subsequently, healthy banks across the country were encouraged to apply for (and received) CPP funds. In exchange for the CPP funds, the Treasury invested in shares of senior preferred stock of the QFI, with a guaranteed dividend of five percent until the fifth anniversary and nine percent thereafter, as well as warrants to purchase a number of shares of common stock equal to 15 percent of the preferred stock investment divided by the market price of the QFI’s stock on the date the investment is made. Different terms apply for privately traded institutions, S corporations and mutual institutions. CPP funds are conditioned upon the participant limiting executive compensation as required by EESA; these executive compensation rules were retroactively expanded as part of the ARRA.

The stated purpose of the CPP program was to provide additional capital to healthy financial institutions so that they would be in a position to make more credit available. However, the media has characterized the CPP funds as “bailout” money, which was undoubtedly accurate in the case of at

least some of the nine original recipients but is not true for many of the subsequent participants. The stigma caused by this public characterization (as well as Congress's retroactive changing of the rules, particularly with respect to executive compensation) has resulted in some CPP participants redeeming the preferred stock and returning the CPP funds to the Treasury, with others planning to follow (see *Capital Purchase Program Funds: Thanks, but Maybe No Thanks* in this issue).

FSP—*Financial Stability Plan*—is the term coined by Secretary Timothy Geithner in his announcement on February 10, 2009, of the Obama administration's plan to address the credit crisis. The announced components of the FSP include the CAP, the PPIP and the CBLI, as well as increased reporting of and oversight over the use of TARP funds.

LSP—*Legacy Securities Program*—a joint Treasury/Federal Reserve program (which is part of the Treasury's PPIP), has two parts. First, the Treasury and the FRBNY are expanding the TALF beyond newly originated asset-backed securities (ABS) to include certain legacy securities, including residential mortgage-backed securities (RMBS) that were originally rated AAA and outstanding AAA-rated ABS and CMBS. Second, the Treasury will partner with private capital providers to support the market for legacy securities. The Treasury plans to approve approximately five private asset managers with a proven track record of purchasing and managing legacy assets and that meet certain eligibility requirements. Approved managers would be given time to privately raise a public-private investment fund (PPIF) in which the Treasury would invest in a one-for-one match with the private equity investors. The Treasury would also loan to the PPIF an amount equal to its equity investment and may consider requests to double the amount of its loan subject to certain conditions. The PPIF would also be eligible to obtain financing from the FRBNY through the expanded TALF program for legacy securities when it is launched, and the Treasury's senior debt would be subordinated to any TALF financing. The private manager of the PPIF would have full discretion to make investment decisions, but the Treasury expects the PPIFs to predominately follow a long-term buy-and-hold strategy and to initially target nonagency RMBS and CMBS originated before 2009 with a AAA rating at origination.

Making Home Affordable—originally called the *Homeowner Affordability and Stability Plan*—has three components: a program to help borrowers with little or no equity refinance at the lower rates currently available; a loan modification program to reduce monthly mortgage payments; and additional capital for Fannie Mae and Freddie Mac to help lower mortgage rates and increase lending.

PPIF—*Public-Private Investment Fund*—is an investment fund established with private and Treasury equity for the purpose of participating in the LLP or the LSP.

PPIP—*Public-Private Investment Program*—announced on March 23, 2009, finally tackled the primary purpose of EESA: the purchase of troubled assets from banks ("troubled assets" have been renamed "legacy assets"). Under this program, the Treasury will collaborate with private investors and with the FDIC to purchase "legacy loans" from banks (see "LLP," below) and will be collaborating with private investors and with the Federal Reserve to purchase "legacy securities" from banks (see "LSP," above). The Treasury intends to make \$75 million to \$100 million of TARP funds available for this program, the FDIC plans to make up to \$600 million in debt guarantees available for the LLP, and the Federal Reserve plans to make TALF financing available for the LSP.

QFI—*Qualifying Financial Institution*—is a financial institution that qualifies for participation in the CPP/CAP. The definitions differ for publicly traded, private, S corps and mutual institutions, but aside from the differences arising from form of ownership, a QFI is a U.S. bank, savings institution, top-tier bank holding company or top-tier savings and loan holding company that is predominantly engaged in activities that a financial holding company could conduct.

SSFI Program—*Systemically Significant Failing Institution Program*—enables the Treasury to provide financial assistance on a case-by-case basis to a financial institution that the Treasury has determined to be "systemically significant" and at "substantial risk of failure." A systemically significant determination depends upon the extent to which a disorderly failure of the institution would directly affect creditors and counterparties; would indirectly affect other institutions that are considered by investors and counterparties as similarly situated; or would, with

a high probability, cause major disruptions to credit markets or payments and settlement systems, seriously destabilize key asset prices or significantly increase uncertainty or loss of confidence thereby materially weakening the overall economy. To date, AIG is the only institution that has received SSFI Program funds.

TIP—*Targeted Investment Program*—enables the Treasury to provide financial assistance on a case-by-case basis to a financial institution if the Treasury determines that a loss of confidence in that institution could result in significant market disruptions that threaten the financial strength of similarly situated financial institutions and thus impair broader financial markets and pose a threat to the overall economy, even if the institution is not at a substantial risk of failure. In determining eligibility, the Treasury will consider factors similar to those considered under the SSFI Program, including the threat that destabilization of the institution would have to creditors and counterparties and to other similarly situated institutions; the extent to which the institution is at a risk of a loss of confidence (and whether it is caused by distressed or illiquid assets); whether the institution is so important to the economy that loss of confidence would disrupt credit markets, settlement and payment systems, etc. The Citigroup bailout included both TIP funds and an AGP asset guarantee.

Programs Sponsored by the FDIC

The FDIC has established the following programs for the purpose of strengthening confidence and encouraging liquidity in the banking system.

LLP—*Legacy Loans Program*—is a joint FDIC/Treasury program (which is part of the PPIP) under which private investors would create individual public-private investment funds (PPIFs, see above) to bid on the purchase of loan pools from banks. The Treasury and private investors would each provide 50 percent of the equity capital in each PPIF, but private managers would manage each PPIF, subject to FDIC oversight. The FDIC would analyze each loan pool proposed to be sold and determine whether it would be willing to guarantee debt in connection with the purchase of the pool (at a debt-to-equity ratio of up to six to one). The FDIC would then

conduct an auction to sell each loan pool to the highest-bidding PPIF. If the selling bank is willing to accept the price, the FDIC would (for a fee) guarantee the debt issued by the PPIF to the selling bank to finance the purchase of the pool, up to the debt-to-equity ratio previously determined.

TLGP—*Temporary Liquidity Guaranty Program*—is a program under which the FDIC is providing (for a fee) a guarantee of newly issued senior unsecured debt of FDIC-insured institutions and bank holding companies (debt guarantee program, or DGP) and full deposit insurance coverage for non-interest-bearing deposit transaction accounts through December 31, 2009, regardless of dollar amount (transaction account guarantee program, or TAG). Eligible institutions were automatically *in* both the DGP and the TAG when it was announced and had until December 5, 2008, to opt out of one or the other or both parts of the program. Originally, the DGP only extended to debt issued on or before June 30, 2009; this has been extended to October 31, 2009.

Programs Sponsored by the Federal Reserve

In addition to the LSP program described above (jointly sponsored by the Treasury and the Federal Reserve), the Federal Reserve has established a number of credit and funding facilities (through the FRBNY) intended to help restore liquidity to various markets.

AMLF—*Asset-Backed Commercial Paper Money Market Mutual Fund Liquidity Facility*—like the MMLFF, is a credit facility provided by the FRBNY to help restore liquidity to the money market funds.

CPFF—*Commercial Paper Funding Facility*—is a funding facility established by the FRBNY to provide a liquidity backstop for commercial paper issuers by purchasing three-month commercial paper through a special-purpose vehicle established by the FRBNY. The program is designed to eliminate much of the risk that issuers will not be able to roll over their maturing commercial paper obligations, thereby encouraging investors to engage in term lending in the commercial paper market.

MMIFF—*Money Market Investor Funding Facility*—like the AMLF, is a credit facility provided by the FRBNY to help restore liquidity to the money market funds.

PDCF—*Primary Dealer Credit Facility*—is an overnight loan facility of the FRBNY to provide funding to primary dealers in exchange for a specified range of eligible collateral and is intended to foster the functioning of financial markets.

TALF—*Temporary Asset-Backed Security Loan Facility*—is a joint Federal Reserve/Treasury initiative to reopen the market for ABS. Under this program, the FRBNY is making loans (\$200 billion, but may be increased to \$1 trillion as part of the CBLI) on a nonrecourse basis to eligible borrowers who purchase eligible ABS. The ABS are pledged to secure the loans, and the Treasury has allocated \$20 billion of TARP funds to provide credit protection to the FRBNY (which may be increased to \$100 billion). Initially, the program was limited to AAA-rated ABS backed by newly and recently originated auto loans, credit card loans, student loans and SBA-guaranteed small business loans. It was expanded to include newly issued AAA-rated ABS backed by business equipment loans, floor plan loans to finance dealer inventories and receivables related to residential mortgage servicing advances. Further expansion is expected to include CMBS, “private label” RMBS, agricultural equipment and other classes of ABS.

In addition, the Treasury and the Federal Reserve have announced the intention to expand the TALF so that certain legacy securities may be used as collateral for TALF financing, including RMBS that were originally rated AAA and outstanding AAA-rated ABS and CMBS.

TSLF—*Term Securities Lending Facility*—established in March 2008, is a 28-day facility pursuant to which the FRBNY loans the Treasury general collateral to its primary dealers (on a competitive bid basis) against other eligible collateral. It is intended to promote liquidity in the financing markets for the Treasury and other collateral and, thus, to foster the functioning of financial markets more generally.

The foregoing definitions are necessarily brief overviews without all the details of the programs. Even so, by the time this article is published, some of this information will likely need updating, because new programs (and acronyms) are being created and existing programs are being modified, expanded or explained on almost a daily basis. To find current (and more detailed) information on these programs and how they work, see www.financialstability.gov/roadtostability/programs.htm; www.newyorkfed.org/markets/ and <http://www.fdic.gov/> (box in upper right).

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