U.S. Announces New Programs and Extension of Existing Programs to Restore Confidence in U.S. Financial Institutions and Restart Lending

March 12, 2009

The U.S. Department of the Treasury, the Federal Reserve Board, the Federal Deposit Insurance Corporation ("FDIC"), the Office of the Comptroller of the Currency, and the Office of Thrift Supervision have announced a comprehensive set of measures to restore confidence in the strength of U.S. financial institutions and restart the flow of credit to households and businesses. These measures introduce new programs as well as expand or extend existing programs established under the Emergency Economic Stabilization Act of 2008.

The core program elements announced to date include:

- a Capital Assistance Program ("CAP") (similar to the previously announced Capital Purchase Program discussed in our prior Alert) to ensure that banking institutions are adequately capitalized as well as establishing a supervisory process to produce forward-looking assessments of the risks on banks' balance sheets and their potential capital needs;
- a new Public-Private Investment Fund to expedite the removal of "toxic assets" from the balance sheets of financial institutions using public and private capital;
- an expansion of the existing Term Asset-Backed Securities Loan Facility ("TALF") (discussed in our prior Alert) designed to reduce credit spreads and restart the securitized credit markets;
- an extension of the FDIC's Temporary Liquidity Guarantee Program (discussed in our prior Alert) through October 31, 2009;
- a new framework of governance and oversight to help ensure that banks receiving funds are held responsible for appropriate use of those funds through stronger conditions on lending, dividends and executive compensation, along with enhanced reporting to the public;
- a new Homeowner Affordability and Stability Plan to assist eligible homeowners by modifying existing mortgages and preventing foreclosures; and
- a new Small Business and Community Bank Lending Initiative to encourage Small Business Administration lending.

Capital Assistance Program

The purpose of the CAP is to ensure the continued ability of U.S. financial institutions to lend to creditworthy borrowers in the face of a weaker-than-expected economic environment and larger-than-expected potential losses. The CAP consists of two core elements: (1) forward-looking capital assessments (commonly referred to as "stress tests") to determine whether any of the major U.S. banking organizations need to establish an additional capital buffer during this period of uncertainty; and (2) access for qualifying financial institutions to capital provided by the U.S. government, in exchange for securities convertible to common stock, as a bridge to private capital in the future.

Stress Tests

As part of the CAP, federal banking and thrift regulators will undertake a coordinated supervisory capital planning exercise with each of the 19 banking organizations with assets in excess of $100 billion. This exercise involves evaluating expected losses and the resources to absorb those losses over the next two years based upon the most recent forecasts from professional forecasters as well as a scenario reflecting a deeper and longer recession than was indicated in the consensus forecast. As a result, regulators can determine whether an additional capital buffer is needed for the banking organization to comfortably absorb losses and continue lending even in a more adverse environment. If the exercise indicates that such a buffer is needed, the banking organization will have a six-month window to raise capital privately or to access the capital made available by the Department of the Treasury.

Securities Convertible to Common Stock

In exchange for the capital provided to qualifying banking organizations by the Department of the Treasury, these organizations will issue preferred securities that are convertible into common stock at a conversion price set at a 10 percent discount from the prevailing level of the qualifying banking organization's stock price as of February 9, 2009. Each CAP instrument will be designed to incentivize the redemption or replacement of the government-provided capital with private capital. Additionally, banking organizations that previously issued preferred stock under the Troubled Assets Relief Program's Capital Purchase Program are eligible to exchange their new preferred securities for the previously issued preferred stock.

Term Asset-Backed Securities Loan Facility

On March 3, 2009, the Department of the Treasury and the Federal Reserve Board provided further details regarding the expansion of the TALF. This expansion is designed to expedite the securitization markets by providing financing to investors to support their purchases of certain AAA-rated asset-backed securities ("ABS"). Under this plan, the Federal Reserve Bank of New York will lend up to $200 billion to eligible owners of certain AAA-rated ABS backed by newly and recently originated auto loans, credit card loans, student loans and SBA-guaranteed small business loans. Issuers and investors in the private sector are expected to begin arranging and marketing new securitizations of recently generated loans, and subscriptions for funding in March 2009 will be accepted on March 17, 2009. Beginning March 25, 2009, the program will fund monthly securitizations, creating new lending capacity for additional future loans through December 2009 (or longer if the Federal Reserve Board chooses to extend the facility).

The Department of the Treasury and the Federal Reserve Board continue to analyze the terms and conditions for accepting commercial mortgage-backed securities and are evaluating a number of other types of AAA-rated newly issued ABS for possible acceptance under the expanded program. The Department of the Treasury and the Federal Reserve Board anticipate that ABS backed by rental, commercial and government vehicle fleet leases, and ABS backed by "small ticket" equipment, heavy equipment, and agricultural equipment loans and leases will be eligible for the April 2009 funding of the TALF. Other types of securities under consideration include private-label residential mortgage-backed securities, collateralized loan and debt obligations, and other ABS not included in the initial rollout, such as ABS backed by non-auto floorplan loans and ABS backed by mortgage-servicer advances.

Homeowner Affordability and Stability Plan

On March 4, 2009, the Department of the Treasury announced the Making Home Affordable Program of the Homeowner Affordability and Stability Plan, including details on programs for eligible homeowners to refinance their existing mortgages, to encourage mortgage modification for certain homeowners and to strengthen confidence in Fannie Mae and Freddie Mac.

Other Programs

Details regarding the other elements of the expanded financial stability plan have not yet been made available. Duane Morris will continue to monitor the development of these programs and issue additional Alerts, as necessary.

For Further Information

If you have any questions regarding any of the programs described in this Alert, including how they may affect your company or its executives, please contact anymember of the Corporate Practice Group, any member of the Business Reorganization and Financial Restructuring Practice Group or the attorney in the firm with whom you are most regularly in contact.