United States Senate
Committee on Finance

Sen. Chuck Grassley · Iowa
Ranking Member

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Grassley Questions Changing Direction of Financial Stabilization Spending, Seeks Answers

WASHINGTON – Sen. Chuck Grassley, ranking member of the Committee on Finance, today questioned why the Treasury Department and Federal Reserve repeatedly have changed direction in the use of taxpayer funds authorized in the *Emergency Economic Stabilization Act of 2008*.

"When you see so many changes, you wonder if they really know what they're doing," Grassley said. "The administration and congressional leadership were so confident when they brought this to the members. Changing direction like this may be completely legal, but it certainly raises some questions as to if they have a handle on how bad the situation really is. Just as important is Congress' need to conduct vigorous oversight, despite Treasury changing the plan for stabilization."

The Committee on Finance has general jurisdiction over and oversight responsibility for the Treasury Department. Grassley outlined a series of questions in a letter to Treasury Secretary Henry Paulson and Federal Reserve Board Chairman Ben Bernanke. The text of his letter follows here.

November 12, 2008

The Honorable Henry M. Paulson, Jr.
Secretary
U.S. Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, DC 20220

The Honorable Ben S. Bernanke
Chairman

Board of Governors of the Federal Reserve System
Twentieth and Constitution Avenue, NW
Washington, DC 20551

Dear Secretary Paulson and Chairman Bernanke:

I am writing to express my concerns and receive answers to questions I have regarding the Treasury Department's implementation of the Emergency Economic Stabilization Act of 2008 (the "Act") which was signed into law on October 3, 2008. As you know, pursuant to the Act and the President's written certification of need dated October 14, 2008, Treasury received the authority to purchase, or commit to purchase, troubled assets up to the limit of $350 billion outstanding at any one time. Of the first $350 billion, I understand that Treasury has already sent out $125 billion to 9 large banks, is in the process of sending out up to $125 billion to other financial institutions, including smaller banks, and will be sending another $40 billion to AIG.

Under the Act, the President can submit a request to authorize Treasury to obtain an additional $350 billion. Secretary Paulson in his statement today indicated that these additional funds should be used to reinvigorate the markets for credit cards, student loans and auto loans. In addition, he stated that the funds would not be used to purchase the "toxic assets" that Treasury intended to purchase when it sought passage of the Act.

In light of the President's imminent request for up to an additional $350 billion, I ask that you respond to my questions and concerns. I noted that in my statement entered into the Congressional record on October 1, 2008, the day the Senate passed the Act, that Congress would be monitoring Treasury's actions and asking questions about its implementation of the Act. In that speech, I stated that "[t]axpayers are protected because the final bill doesn't provide $700 billion upfront. The Administration originally wanted the authority to have it all at once, but this bill provides for the program to be implemented in stages. Only $250 billion will be provided immediately, and another $100 billion will be provided upon a written certification of need by the President. Finally, the remaining $350 billion will be provided unless Congress acts. Let's be clear. Congress can act anytime to revoke the Treasury's authority. They will be watched, and they will be questioned. And, if Congress doesn't like what it sees, we can repeal this economic stabilization plan."

<u>Executive Compensation</u>
The Act only restricts the deductibility of compensation and the payment of golden parachute payments to the top five executives of financial institutions that: (1) sell an equity interest or debt position to Treasury in a "direct purchase" or (2) sell at least $300 million in troubled assets to Treasury in an "auction sale." The Act does not restrict, for example, the payment of bonuses and other perks paid to executives and top managers outside of the top five executives. The Act also does not restrict the payment of severance benefits to executives who voluntarily terminate from employment. Recent reports indicate that financial institutions that have received taxpayer funds under the Act are using these funds to pay bonuses to executives inside and outside of the top five

executives of the institution. Top executives are walking away from their troubled institutions with tens of millions of dollars.

As I stated in my October 10, 2008, letter to you, I am concerned that these provisions are mere window dressing. My concerns have only increased given Secretary Paulson's announcement this morning that Treasury will not be using funds authorized by the Act to purchase "toxic assets." It would appear that no penalties will apply to institutions that receive taxpayer funds and violate the Act's restrictions on executive compensation.

Treasury is not constrained by the Act and should be exercising its broad authority to issue regulations that further limit executive compensation and other expenses paid by institutions that are receiving funds under the Act. Treasury should also take steps to ensure that taxpayer dollars are not being used to pay bonuses or other rewards to those executives responsible for their institutions' poor performance that, in turn, led to an institution's demise and destruction of shareholder value. On November 10, 2008, the same day on which AIG received an additional $40 billion of federal funds, there were new reports of AIG spending money on another lavish retreat in Arizona. This is unconscionable.

I raised a number of questions in my October 10, 2008, letter to you. To date, I have not received a response. Please provide responses to these questions that I am repeating here.

1. Why would the Troubled Asset Relief Program ("TARP"), Capital Purchase Program, and the program for Systematically Significant Failing Institutions fail if the Act contained tighter provisions for executive compensation?
2. What is being done to monitor the expenses of companies rescued with taxpayer dollars?
3. Given that Treasury has broad authority to write regulations governing executive compensation, why is Treasury not utilizing this authority to restrict compensation and other expenses paid by rescued companies?

Purchase of Mortgage-Backed Securities

When Treasury pitched the need for a financial rescue bill to Congress, Congress was told that $700 billion was needed to purchase mortgage-backed securities in order to reestablish a market in these securities that had frozen up. Congress was told that this was essential to unfreezing the credit markets, and that if Congress did not act, Americans on Main Street would soon begin to suffer as a result of an inability to get credit to fund small businesses and purchase items such as houses and cars. However, shortly after the Act was signed into law, Treasury announced that it would partially nationalize certain banks. Next, Treasury announced that it was considering guaranteeing up to 3 million mortgages totaling up to $600 billion in principal amount according to press reports. In addition, on November 10, 2008, the Treasury Department announced that it would be providing an additional $40 billion to AIG under the Act in exchange for preferred stock and warrants of AIG. When added together with aid provided by Treasury outside of the Act, AIG will have received approximately $150 billion of taxpayer money. Then, in his news conference today, Secretary Paulson announced that

Treasury is no longer considering purchasing mortgage-backed securities and indicated there were other priorities for TARP funds.

In light of the above, I would appreciate detailed responses to the following questions.

1. Why did Treasury decide to use the money to partially nationalize certain banks rather than follow through with the stated purpose of purchasing mortgage-backed securities?
2. Was Treasury considering using the money that it expected to receive under the Act to partially nationalize certain banks and guarantee mortgages prior to October 3, 2008, the date the Act was passed in the House of Representatives and signed into law by the President?
    a. If yes, did you inform any members of Congress of the fact that Treasury was considering using the money that it expected to receive under the Act for these purposes?
    b. If yes, which members of Congress did you inform and when?
3. Explain in detail the Department's rationale for providing $40 billion in additional aid to AIG under the Act and provide all relevant materials to support this decision.
4. Explain in detail the rationale prioritizing the markets for credit cards, student loans and auto loans.

<u>Extension of Credit</u>
According to a number of published reports, the banks that have received large sums of money from the Act are not using the majority of that money to extend credit. Instead, it has been reported that these banks are using the money received under the Act to acquire other banks, pay large bonuses to their executives, and pay dividends to their shareholders.

Because these reports raise additional concerns, please respond to the following questions.

1. Is Treasury tracking how these banks are using the taxpayers' money? If yes, describe in detail the methodology for tracking these funds, including how Treasury is managing any databases that it may be using.
2. Describe in detail how taxpayer money is being used?

<u>Contracts with Third Parties</u>
Treasury has already executed a number of contracts with companies to assist Treasury in implementing the Act. I am strong believer that sunlight is the best disinfectant and think it is important that the process of implementing the Act be as transparent as possible, especially when taxpayer money is being used. As a result, please provide responses to the following questions.

1. Provide original copies of all contracts.
2. Explain why only redacted copies of these contracts are available on your website and explain the rationale for redactions in each contract.

3. Explain how the Treasury plans to abide by the Act to ensure that there are no conflicts of interest that may arise in connection with the administration and execution of the authorities provided.

Selection of Participants

As you know, on October 24, 2008, Treasury approved $7.7 billion in aid to PNC Financial Services Group Incorporated, which just hours later announced that it was acquiring National City Corporation for $5.58 billion. Although Treasury approved aid to PNC, it had denied aid to National City Corporation.

1. Describe in detail, and provide copies, of the standards, policies and procedures the Department is using to decide which banks will receive aid.
2. Who makes the decision as to whether or not a bank will receive aid from Treasury?
3. How did Treasury decide that National City was ineligible to receive funds?

Resolution of Disapproval

Since it appears that Treasury has already identified uses for the additional $350 billion, it seems very likely that the President will be requesting the use of these funds soon. As you aware, should Congress decide to deny the President's request, Congress would only have 15 days from the transmission of the President's request to pass a resolution of disapproval. I am concerned that the President may transmit this request when Congress is not in session and unable to come back in session within the 15 days in which Congress must act to deny the President's request.

As a result, I would like to know when the President intends to submit to Congress the request for the additional funds.

If you have any questions, please do not hesitate to contact Ellen McCarthy of my staff at (202) 224-4515.

Sincerely,

Chuck Grassley
Ranking Member