

Section Two: Additional Views

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We concur with the issuance of the March report and offer the additional observations noted below. We appreciate the spirit with which the Panel and the staff approached this complex issue and incorporated suggestions offered during the drafting process.

As of today, the American taxpayers have involuntarily invested approximately \$17.2 billion in GMAC.⁵³⁸ Since the CBO has assigned a 59 percent subsidy rate to the various auto-related bailouts – including GMAC – as of mid-December 2009,⁵³⁹ it is not unreasonable to assume that the taxpayers will lose approximately \$10 billion⁵⁴⁰ of the \$17.2 billion of TARP funds allocated to GMAC.⁵⁴¹

In making its assessment of whether to subsidize GMAC with taxpayer-funded TARP resources, Treasury was charged with carrying the burden regarding the three fundamental issues analyzed immediately below. We question why Treasury has allocated any TARP funds to GMAC because Treasury has not demonstrated in a satisfactory manner its case with respect to any of these issues.

First, prior to committing taxpayer resources to GMAC, Treasury should have demonstrated that no other group of new or existing financial institutions could reasonably fill the void upon the liquidation of GMAC. Treasury and GMAC have attempted to justify

⁵³⁸ The taxpayers have been forced to bail out GMAC on three separate occasions over the past fifteen months. In December 2008, Treasury allocated \$5.0 billion of TARP funds to GMAC. Unfortunately, in May 2009, Treasury committed the taxpayers to pay another \$7.5 billion of TARP proceeds. In December 2009, Treasury committed the taxpayers yet again to pay another \$3.8 billion of TARP funds to GMAC.

⁵³⁹ See Congressional Budget Office, *The Budget and Economic Outlook: Fiscal Years 2010 to 2020*, at 13 (Jan. 2010) (online at www.cbo.gov/ftpdocs/108xx/doc10871/01-26-Outlook.pdf).

⁵⁴⁰ This figure is derived by using the \$17.2 billion aggregate TARP allocation to GMAC and multiplying it by the CBO subsidy rate of 59 percent for the auto related bailouts. Since the CBO subsidy rate applies to all of the auto industry bailouts, including the automakers Chrysler and GM as well as GMAC, the actual subsidy rate for GMAC may rise above or fall below 59 percent. The OMB has assigned a subsidy rate of 39 percent to the government's equity investment (\$16.3 billion) in GMAC. OMB Analytical Perspectives: FY2011 Budget, *supra* note 535, at 40.

⁵⁴¹ As a comparison, for fiscal year 2011 the National Institutes of Health (NIH) have requested \$765 million for breast cancer research. See U.S. Department of Health and Human Services, National Institutes of Health, *Estimates of Funding for Various Research, Condition and Disease Categories (RCDC)* (Feb. 1, 2010) (online at report.nih.gov/rcdc/categories/). The latest Nimitz-class aircraft carrier, the U.S.S. George H. W. Bush, cost approximately \$4.5 billion. See U.S. Navy, Official Website of USS George H.W. Bush (CVN 77), *Information about the Ship* (online at up-www01.fhc.navy.mil/cvn77/static/aboutus/aboutship.html) (accessed Mar. 10, 2010). Thus the question, is the loss of \$10 billion from the GMAC bailout worth 13 years of breast cancer research, or two Nimitz-class aircraft carriers with \$1 billion left over?

GMAC's systemic importance based upon the "special relationships" that exist between GMAC and its dealer network and the "unique IT system" employed by GMAC to monitor its extensions of credit. Many successful business enterprises rely upon these sorts of factors. It is unclear why GMAC merits more than \$17 billion of taxpayer funds based upon its "special relationships" or "unique IT systems." It appears problematic to argue that GMAC – and GMAC alone – is capable of financing a floor plan for a Chrysler or GM dealer.

It is not unreasonable to anticipate that other financial institutions and private equity firms would welcome the opportunity to extend credit to the retail customers and dealers of Chrysler and GM and to securitize the instruments received in such transactions.⁵⁴² During the dark days of late 2008 and early 2009, Treasury could have encouraged other market participants to enter GMAC's auto finance business by providing short-term guarantees of their financings as well as other credit support. The government could also have encouraged one or more of these market participants to purchase GMAC's auto finance business and retain the services of its employees. The government may have needed to provide short-term financing to fund the acquisition, but it seems reasonable to conclude that the cost of such financing to the taxpayers would have equaled much less than the \$17 billion ultimately advanced to GMAC under TARP. Since GMAC's auto finance business is profitable, the taxpayers would have been subject to far less risk than they currently carry under the bailout as actually implemented.

Even if GMAC – and GMAC alone – possessed the expertise necessary to conduct an auto finance business, why does the United States government continue to sanction and subsidize such concentration instead of encouraging healthy competition from other private sector financial institutions and firms seeking to enter the market?⁵⁴³ Although the bailout of GMAC was in part premised upon the overwhelming market dominance of GMAC's floorplan business, it does not appear that Treasury has taken any action to break up this concentration and foster competition from other market participants with established expertise in the floorplan business. Instead, Treasury has perpetuated GMAC's floorplan market share by providing the company with access to unlimited TARP funds in the name of not reneging on an informal Treasury commitment. By funneling the floorplan business of Chrysler and GM through the narrow – yet virtually exclusive – financing conduit of GMAC, Treasury has left Chrysler and GM susceptible to any future mismanagement of GMAC and raised the possibility that the taxpayers will yet again be called upon to rescue GMAC.

⁵⁴² This analysis is based upon the assumption that GMAC's business model is not premised upon charging retail customers above-market rates of interest so as to subsidize the below-market rates it charges the dealers.

⁵⁴³ By contrast, in early February the Administration announced that it plans to end the Ares I program and outsource low earth orbit rocket launches to a group of private sector aerospace companies. See Kenneth Chang, *Obama Calls for End of NASA's Moon Program*, New York Times (Feb. 1, 2010) (online at www.nytimes.com/2010/02/02/science/02nasa.html?scp=1&sq=constellation%20nasa&st=cse). If private sector participants are lined up to bid for the right to design and launch rockets, there must be at least a few financial institutions that are prepared to finance retail customers and dealers of Chrysler and GM.

Of course, both Chrysler and GM might ultimately benefit from controlling its own well-managed financing subsidiary, as other vehicle manufacturers do. While such subsidiaries often control a substantial share of their parent's financing needs, they infrequently venture into other high-risk and non-complementary business operations that they are incapable of properly managing – such as ResCap or, perhaps, Ally Bank – the failure of which could undermine the viability of their vehicle financing operations, as ResCap did for GMAC. For these reasons, it is possible that Chrysler and GM may undertake to form a limited liability special purpose entity to acquire the auto finance business of GMAC (without, most likely, any of the operations of the failed ResCap). It is also possible that Chrysler and GM may seek to form their own independent financing subsidiaries to compete with the auto finance business of GMAC.⁵⁴⁴ The occurrence of either event may materially influence how and when the taxpayers are repaid their TARP advances to GMAC.

Second, if Treasury carries the burden on the first issue, Treasury must next demonstrate that it had no viable choice but to bail-out ResCap – the entity through which GMAC made ill-conceived bets in the residential mortgage and subprime housing markets – in hopes of saving GMAC's auto finance business.⁵⁴⁵ In satisfying this burden, Treasury should show that no viable approach existed under the U.S. bankruptcy code or otherwise to extricate GMAC's auto finance business from the taint of its insolvent mortgage finance business other than through the expenditure of over \$17 billion of hard-earned taxpayer-funded resources.

GMAC could have, for example, sold its auto finance business for fair market value to a third party outside of bankruptcy (and avoided a fraudulent conveyance/transfer claim) or sold its auto finance business to a third party under Section 363 in a bankruptcy proceeding.⁵⁴⁶ If GMAC's auto finance business is truly viable and profitable, it is not unreasonable to expect that

⁵⁴⁴ GM may welcome the opportunity to establish its own financing subsidiary if it determines that (1) its common equity in GMAC will be wiped out if the taxpayers suffer the loss of any GMAC allocated TARP funds and (2) the expansion of Ally Bank is inconsistent with GMAC's maintenance of a robust auto finance business. On the other hand, GMAC remits royalties and fees to GM pursuant to a services arrangement.

⁵⁴⁵ It appears that GMAC operates three businesses – a retail auto finance and dealer floor planning business, an insurance business and a mortgage finance business. The first business provides financing to retail purchasers of Chrysler and GM vehicles as well as to the dealers themselves. The second underwrites insurance. The third business placed huge un-hedged bets in the residential mortgage and subprime housing markets that blew up and drove GMAC into insolvency.

⁵⁴⁶ As noted in the Panel's report, the structuring, negotiating, and closing of the disposition of GMAC's auto finance business within or outside bankruptcy present an array of daunting business and legal issues. Prior to any such disposition, Treasury should conduct a thorough due diligence investigation including: (1) a careful analysis of the relevant facts and circumstances, (2) a cost benefit analysis comparing recovery pre- and post-bankruptcy, and (3) an analysis of any additional TARP contributions required pre- and post-bankruptcy. GMAC's status as a BHC only adds another layer of complexity. Nevertheless, we remain unconvinced that Treasury could not have structured the bailout of GMAC's auto finance business in a much more taxpayer-friendly manner.

other financial institutions and private equity firms would welcome the opportunity to acquire the business with its captive group of customers and monopolistic market power in the Chrysler and GM dealer floorplan business. GMAC also could have simply sold its auto finance business at fair market value to a third party outside of bankruptcy.⁵⁴⁷ The government may have had little choice in late 2008 and early 2009 but to assist the purchaser of the auto finance business by providing DIP financing or other credit support, but, as noted above, the subsidy rate on the use of TARP funds would have been most likely materially lower since GMAC's auto finance business operates as a profitable going concern and no TARP funds would have been allocated to ResCap. Once the markets stabilized, the auto finance business (as a separate entity under new ownership and management) should have been able to refinance the government-funded bridge facility (with government-sponsored guarantees if absolutely necessary) and the taxpayers would have been repaid in full in cash. Following the transfer of the auto finance business, GMAC could have been reorganized by private market participants (if any were interested) or, most likely, liquidated without the expenditure of any TARP funds.

If the bailout of GMAC was premised on the necessity of saving the company's auto finance business, why was Treasury not capable of doing just that? Why was even one dollar of TARP funds allocated to ResCap? Why was ResCap not left for liquidation? If the automakers Chrysler and GM were capable of surviving bankruptcy proceedings, why was GMAC not similarly restructured? It is beyond disappointing that the taxpayers have been forced to squander many billions of dollars.

Third, even if GMAC carries the burden on both issues, Treasury must also demonstrate why GMAC was too big or too interconnected with the financial system and the overall economy to fail and why GMAC merited such unprecedented largess when so many other American businesses and families are suffering from the worst economic downturn in several generations. It appears quite unlikely that the failure of GMAC would have led directly to the collapse of the American financial system.

Treasury has also justified its bailout of GMAC based upon its undertaking to provide each of the 19 stress-tested financial institutions with TARP funds to the extent they were not able to raise capital in the private markets. We do not agree with this simplistic "our word is our bond" justification for the bailout. Treasury seems to argue that once a financial institution has joined (or was drafted into or was specifically selected for inclusion in) the "elite 19," then the United States government had a duty (or some kind of moral obligation or patriotic commitment) to bail it out *whatever the cost*. It is regrettable for Treasury to assert that it was somehow duty bound to hand a *blank check* to GMAC. Treasury was required to exercise proper judgment and conduct a thorough due diligence analysis with respect to its investment of taxpayer-sourced

⁵⁴⁷ If GMAC pursues the sale of its auto finance business or any other division or subsidiary or the merger of GMAC or any of its subsidiaries, Treasury should ascertain that the transaction is structured in a manner that is the most advantageous for the taxpayers and that no TARP funds are forgiven or subordinated.

TARP funds and not simply throw \$17 billion at a problem in hopes that it would go away. The financial markets do not expect the government to act in an irrational or profligate manner, and any such reaction only creates enhanced moral hazard risks and all but codifies GMAC's implicit guarantee from the United States government. The taxpayers also understand the "don't throw good money after bad" mantra and expect the government to allocate their tax dollars accordingly. In addition, it is not entirely clear why GMAC – a non-systemically significant financial institution – was included in the list of stress-tested financial institutions other than, perhaps, to afford the company an explicit guarantee under the TARP program of its seemingly unlimited capital deficiencies. Such circular reasoning offers little in the way of meaningful insight.

Other significant issues have arisen with respect to the bailout of GMAC, including, without limitation, the following:

1. It remains unclear how GMAC has used the \$17 billion of TARP funds. The company has not provided any meaningful publicly available analysis of how it has employed such taxpayer resources or why it may not be able to repay all of such funds. It would be helpful for the taxpayers to receive a detailed "uses of TARP funds" statement from GMAC with an emphasis on those payments made to persons and entities that are not obligated to reimburse GMAC. In other words, if the taxpayers stand to lose up to \$10 billion on their allocation of TARP funds to GMAC, it is absolutely critical for GMAC to disclose in a prompt, thorough, and public manner specifically where the money went and why it was so allocated.⁵⁴⁸
2. It appears that some (and quite possibly a substantial part) of GMAC's TARP funds were allocated to ResCap to bail out its risky and ill-considered bets in the residential mortgage and subprime markets. Notwithstanding these allocations, we remain concerned as to whether Treasury and GMAC have truly stemmed the tide of losses at ResCap. The taxpayers have received only modest disclosure regarding the operations of and prospects for ResCap including, without limitation, the amount of ResCap originated mortgage loans that Fannie Mae, Freddie Mac, and other purchasers and guarantors are requiring ResCap to repurchase, and whether ResCap will require additional taxpayer-sourced TARP funds and, if so, why, how much, and when? Why ResCap might have merited even one dollar of TARP funds remains entirely murky.
3. Many questions remain unanswered with respect to Ally Bank. For example, has GMAC allocated taxpayer-sourced TARP funds to Ally Bank? If so, why has Treasury committed the taxpayers to underwrite yet another financial institution, particularly one with an unproven business model? Is Ally Bank using TARP funds to pay above-market

⁵⁴⁸ GMAC should not respond with the statement that "money is fungible." Money is also limited and, without the allocation of \$17 billion of TARP funds, GMAC would have no doubt failed.

rates of interest on its retail accounts that it has aggressively advertised over the past few months, or does its implicit guarantee from Treasury enable it to fund these above-market rates? If so, how does Ally Bank plan to pay these rates after the TARP spigot is shut off? If Ally Bank fails to pay the above-market rates of interest and its deposit base deteriorates, how will GMAC finance its floorplan business? How much, if any, of the projected \$10 billion loss of TARP funds allocated to GMAC is attributable to Ally Bank and its payment of above-market rates of interest? If the answer is one dollar or more, why has Treasury committed the taxpayers to subsidize these rates?

4. It was recently announced that the CEO of GMAC will receive a total annual compensation package of \$9.5 million, which consists of cash and deferred and restricted stock.⁵⁴⁹ Although some have focused on the amount of the compensation, more significant from the taxpayers' perspective is the structure of the compensation package and the consequent incentives that may skew decision-making towards particular outcomes, such as building the company, when dissolution and sale might be best.
5. Even though the taxpayers stand to lose up to \$10 billion on the allocation of TARP funds to GMAC, the *pre-bailout* common shareholders of GMAC may nevertheless profit from their investment in the company. The Panel has made clear that if the taxpayers lose one dollar of TARP funds, the pre-bailout common shareholders should be wiped out and receive no return. Representatives from Treasury appear quite sensitive (if not defensive) regarding this issue. We call upon Treasury to issue a formal legal opinion describing the extent to which pre-bailout common shareholders may profit if the taxpayers lose. Treasury has put the taxpayers in an awkward position of suffering a substantial loss but the pre-bailout common shareholders are not wiped out.
6. It is regrettable that the bailouts of GMAC, Chrysler, and GM could raise subsidy issues under WTO rules. As noted in the Panel's report, in September 2009, the People's Republic of China launched a countervailing duty investigation into the assistance given Chrysler and GM where, among other items, the Chinese automotive industry cited aid to GMAC in its complaint. It is possible that other jurisdictions may raise similar claims

⁵⁴⁹ The bulk of the CEO's compensation is structured as deferred or restricted stock with a cash salary of \$950,000. While a stock grant may have appeared attractive to the Special Master, the incentives inherent in a stock grant could cause the CEO to consider actions that may not necessarily be in the best interests of the taxpayers. With a large stock award in GMAC, the CEO may have little interest in pursuing a bankruptcy of GMAC or selling the "crown jewel" auto finance business (to GM and Chrysler among others) and liquidating ResCap. All of these actions could diminish the value of GMAC stock and Mr. Carpenter's stock award. Instead, the CEO appears inclined to pursue a growth strategy at GMAC with Ally Bank. Perhaps it would have been best simply to pay the CEO a higher cash compensation amount so as potentially not to influence his management decisions. It is unfortunate that such an approach might not have been acceptable to the Special Master.

with the WTO. Treasury should thoughtfully analyze these and other trade related issues before allocating TARP funds to any entity.⁵⁵⁰

⁵⁵⁰ This paragraph is not intended to constitute a legal or other analysis regarding the merits of any action brought under WTO or similar rules by the People's Republic of China or any other jurisdiction or entity regarding the allocation of TARP funds to or any other action taken by the U.S. government with respect to GMAC, Chrysler, or GM.