Executive Summary[*]

In creating the Troubled Asset Relief Program (TARP) in late 2008, Congress provided Treasury with a wide range of tools to combat the financial crisis. In addition to purchasing assets directly from financial institutions, Treasury was also authorized to support the value of assets indirectly by issuing guarantees.

In the legal sense, a guarantee is simply a promise by one party to stand behind a second party's obligation to a third. For example, when a worker deposits his paychecks in an account at his local bank, his money is guaranteed by the U.S. government through the Federal Deposit Insurance Corporation (FDIC). If a bank fails – that is, if the bank cannot give the worker his money later, when he needs it – then the FDIC will step in to fill in the gap. The FDIC guarantees the bank's debt to its customer.

During the financial crisis of late 2008 and early 2009, the federal government dramatically expanded its role as a guarantor. Congress raised the maximum guaranteed value of FDIC-insured accounts from $100,000 to $250,000 per account, and the FDIC also established the Debt Guarantee Program (DGP), standing behind the debt that banks issued in order to raise funds that they could use to lend to customers. Treasury reassured anxious investors by guaranteeing that money market funds would not fall below $1.00 per share, and Treasury, the FDIC, and the Federal Reserve Board together negotiated to secure hundreds of billions of dollars in assets belonging to Citigroup and Bank of America. All told, the federal government's guarantees have exceeded the total value of TARP, making guarantees the single largest element of the government's response to the financial crisis.

From the taxpayers' perspective, guarantees carry several advantages over the direct purchases of bank assets. Most significantly, guarantees bear no upfront price tag. When government agencies agreed to guarantee $300 billion in Citigroup assets in late 2008, taxpayers paid no immediate price – and now appear likely to earn a profit from fees assuming economic conditions do not deteriorate further.

The low upfront cost of guarantees also allowed Treasury, in coordination with other federal agencies, to leverage a limited pool of TARP resources to guarantee a much larger pool of assets. The enormous scale of these guarantees played a significant role in calming the financial markets last year. Lenders who were unwilling to risk their money in distressed and uncertain markets became much more willing to participate after the U.S. government promised to backstop any losses.

[*] The Panel adopted this report with a 5-0 vote on November 5, 2009. Additional views are available in Section Two of this report.

Despite these advantages, guarantees also carry considerable risk to taxpayers. In many cases, the American taxpayer stood behind guarantees of high-risk assets held by potentially insolvent institutions. It was possible that, if the guaranteed assets had radically declined in value, taxpayers could have suffered enormous losses.

At its high point, the federal government was guaranteeing or insuring $4.5 trillion in face value of financial assets under the three guarantee programs discussed in this report. (The majority of that exposure came from Treasury's guarantee of money market accounts that held high concentrations of government debt in the form of Treasury securities. Therefore, the total exposure is less than the full face value guaranteed because government debt is already backed by the full faith and credit of the United States.) Despite the likelihood that the U.S. government will receive more revenue in fees than will ultimately be paid out under the guarantees, the taxpayers bore a significant amount of risk.

Just as significantly, guarantees carry moral hazard. By limiting how much money investors can lose in a deal, a guarantee creates price distortion and can lead lenders to engage in riskier behavior than they otherwise would. In addition to the explicit guarantees offered by Treasury, the FDIC, and the Federal Reserve, the government's broader economic stabilization effort may have signaled an implicit guarantee to the marketplace: the American taxpayer would bear any price, and absorb any loss, to avert a financial meltdown. To the degree that lenders and borrowers believe that such an implicit guarantee remains in effect, moral hazard will continue to distort the market in the future. The cost of moral hazard is not as easily measured as the price of guarantee payouts or the income from guarantee fees, but it remains a real and significant force influencing the financial system today. As Treasury contemplates an exit strategy for TARP and similar financial stability efforts such as these explicit guarantees, unwinding the implicit guarantee of government support is critical to ensuring an efficiently functioning marketplace.

After a wide-ranging review of TARP and related guarantees, the Panel has not identified significant flaws in Treasury's implementation of the programs. To the contrary, the Panel has noted a trend towards a more aggressive and commercial stance on the part of Treasury in safeguarding the taxpayers' money. Nonetheless, in light of these guarantees' extraordinary scale and their risk to taxpayers, the Panel believes that these programs should be subject to extraordinary transparency. The Panel urges Treasury to disclose greater detail about the rationale behind guarantee programs, the alternatives that may have been available and why they were not chosen, and whether these programs have achieved their objectives.

Finally, the Panel recommends that Treasury provide regular disclosures relating to Citigroup's asset guarantee – the single largest TARP guarantee offered to date. These disclosures should be detailed enough to provide a clear picture of what is happening, including information on the status of the final composition of the asset pool and total asset pool losses to date, as well as what the projected losses of the pool are and how they have been calculated.

The following table summarizes the principal elements of the programs that the Panel has examined for the purposes of this report:

Agency	Program	Authority	Who is Protected?	What is Guaranteed?	Sum Currently Guaranteed	Fees Earned	Losses to Date
Treasury	Asset Guarantee Program (AGP)	Emergency Economic Stabilization Act of 2008 (EESA)	Citigroup (Bank of America – never used)	Specified asset classes of Citigroup	Up to $5 billion	$3.8 billion	$0
Treasury	Temporary Guarantee Program for Money Market Funds (TGPMMF)	Gold Reserve Act of 1934, as amended EESA, § 131	Money market fund investors	Investors' holdings in participating funds as of September 19, 2008	$0 (current) ($3.22 trillion peak commitment)	$1.2 billion	$0
Federal Reserve Board	Asset Guarantee Program (AGP)	Federal Reserve Act, § 13(3)	Citigroup (Bank of America – never used)	Specified assets of Citigroup	Undetermined; non-recourse loans to be made available	$57 million	$0
Federal Deposit Insurance Corporation (FDIC)	Temporary Liquidity Guarantee Program (TLGP) – includes Debt Guarantee Program (DGP)	Federal Deposit Insurance Act	Holders of debt issued by banks and other financial institutions issuing debt	Debt issued by banks and other financial institutions	$307 billion principal, plus interest	$9.6 billion	$2 million[1]
FDIC	Asset Guarantee Program (AGP)	Federal Deposit Insurance Act	Citigroup (Bank of America – never used)	Specified assets of Citigroup	Up to $10 billion	$2.7 billion	$0

[1] According to the Federal Deposit Insurance Corporation, as of October 22, 2009, there has been one failure of a Temporary Liquidity Guarantee Program -participating institution, an affiliate of which had issued guaranteed debt. While the FDIC anticipates up to a $2 million loss on that issuance, no losses have been paid out yet with respect to the Debt Guarantee Program.