BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

December 6, 2011

BEN S. BERNANKE
CHAIRMAN

The Honorable Tim Johnson
Chairman
Committee on Banking, Housing,
and Urban Affairs
United States Senate
Washington, D.C. 20510

The Honorable Richard Shelby
Ranking Member
Committee on Banking, Housing,
and Urban Affairs
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman and Ranking Member:

There have been a series of recent articles--one just last week--concerning the Federal Reserve's emergency lending activities during the financial crisis. These articles have largely repeated the same information in different formats, and have contained a variety of egregious errors and mistakes. The articles recycle information that has been disclosed to the Congress and the American people in various forms for some time, and has been the subject of investigations, reviews, and reports by the Congress, the Government Accountability Office, the Congressional Oversight Panel, the Special Inspector General for the Troubled Asset Relief Program, and others. Moreover, the disclosure issues raised in these articles have already been addressed and settled, first by the Federal Reserve through a variety of reports and public postings, and then by Congress after a public debate. Since the articles bear directly on the Federal Reserve's relationship with the Congress and the American people, I wanted to share with you a memo prepared by Board staff that addresses some of the most serious errors and claims in those articles.

As I have said in speeches and in testimony before the Congress, and as the Government Accountability Office and other reviewing bodies have found, the Federal Reserve implemented these emergency lending programs to provide liquidity and to prevent the collapse of the financial system during a period of tremendous financial stress. Working with the Administration and the Congress, we accomplished that goal. In the process, the nation has instituted important changes in the regulatory arena. Specifically, Congress has provided a variety of tools--including enhanced supervision for large, systemically significant financial institutions and a resolution mechanism to wind down such firms when necessary--and the Federal Reserve and the other financial regulators are working hard to implement these financial crisis management tools.

I hope that you will not hesitate to contact me if we can be of assistance.

Sincerely,

Enclosure

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OF THE
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WASHINGTON, D. C. 20551

December 6, 2011

BEN S. BERNANKE
CHAIRMAN

The Honorable Spencer Bachus
Chairman
Committee on Financial Services
House of Representatives
Washington, D.C. 20515

The Honorable Barney Frank
Ranking Member
Committee on Financial Services
House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman and Ranking Member:

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Correction of Recent Press Reports Regarding Federal Reserve Emergency Lending During the Financial Crisis

Recent press reports contain numerous errors and misrepresentations about Federal Reserve emergency lending during the financial crisis.

First, these articles have made repeated claims that the Federal Reserve conducted "secret" lending that was not disclosed either to the public or the Congress. No lending program was ever kept secret from the Congress or the public. All of the programs were publicly announced when they were initiated, and information about all lending under the programs was publicly released--both on a weekly basis through the Federal Reserve's public balance sheet release and through detailed monthly reports to the Congress, both of which were also posted on the Federal Reserve's website.

It is true that, generally, the names of the counterparties and borrowers from the emergency facilities were not immediately disclosed, consistent with general central banking practice. Releasing the names of these institutions in real-time, in the midst of the financial crisis, would have seriously undermined the effectiveness of the emergency lending and the confidence of investors and borrowers. These matters were discussed extensively at the time in the press, and the Chairman and other members of the Board discussed them numerous times in hearings before the Congress.

In point of fact, the Federal Reserve took great care to ensure that Congress was well-informed of the magnitude and manner of its lending. As required by the Emergency Economic Stabilization Act, passed in late 2008, the Federal Reserve reported regularly on the outstanding balances in its Sec. 13(3) lending facilities as well as on collateral (by type and quality) for the loans. Beginning in June 2009, the Federal Reserve went well beyond these legal requirements in the information it made available in its monthly public reports to the Congress, which were also posted on the Federal Reserve's website.

Moreover, Congress was well informed of the volume of borrowing by large banks. For instance, the monthly reports showed the daily average borrowing during the month in the aggregate for the five largest discount window borrowers, the next five, and the rest. Similar information was also provided for lending at the emergency facilities.

In addition, the issue of counterparty disclosure was well-known to the Congress and was addressed as part of the Dodd-Frank Act. Under provisions of the Sanders Amendment, the names of all counterparties and borrowers from the emergency lending facilities and the Term Auction Facility (TAF) were disclosed on December 1, 2010. Data provided included the names of the borrowers, the date that credit was extended, the interest rate, information about the collateral, and other relevant terms. Similar information is supplied for swap line draws and repayments. Details for each agency MBS purchase included the counterparty to the transaction, the date of the transaction, the amount of the transaction, and the price at which each transaction was conducted. Additional disclosures of discount window borrowers and transactions information were made on March 31, 2011.

Second, one article asserted that the Federal Reserve lent or guaranteed more than $7.7 trillion during the financial crisis. Others have estimated the amounts to be $16 trillion or even $24 trillion. All of these numbers are wildly inaccurate. As disclosed on the Federal Reserve's balance sheet, published weekly and audited annually by independent auditors, total credit outstanding under the liquidity programs was never more than about $1.5 trillion; that was the peak reached in December 2008.

To be sure, that is a very large amount, but it was a necessary response to ensure that the crucial mistake made during the Great Depression--failing to prevent the collapse of the financial system--was not repeated. Importantly, such lending helped support the continued flow of credit to American families and businesses.

The inaccurate and misleading estimates could be based on several errors, including double-counting--for example, including a series of loans, paid and then reissued, as separate loans. Because much of the lending was on a revolving basis and made either overnight or for short durations (30, 60, or 90 days, or even overnight), such double counting could lead to a gross overestimate of the actual amount of lending.

Lending is not spending and thus it is misleading to add up a succession of loans that were paid off on a revolving basis. A good analogy might be a family's mortgage: if a family received a $200,000 mortgage loan, then refinanced two years later to take advantage of lower rates, again borrowing $200,000, it would be misleading to say it had borrowed $400,000. Likewise, if a bank lends $1,000 for a year at a time, $1,000 a month at a time for a year, and $1,000 a day at a time for a year--repaying the loans at the end of each period--the economic result is that the borrower has borrowed just a total of $1,000 in each case, and it would be incorrect to say that the borrower would have borrowed $12,000 in the second instance, and $365,000 in the third instance.

Other inaccuracies may occur if total *potential* lending is counted as *actual* lending. For instance, the TALF program was authorized at $200 billion, but its total lending never exceeded $70 billion. The same mistake would also apply in reference to other lending programs, like the commercial paper funding facility, which were authorized at far higher amounts than were ever provided.

Although the articles do not stress this point, it is important to note that nearly all of the emergency assistance has, in fact, been fully repaid or is on track to be fully repaid. This fact has been verified both by the Board's independent auditors and the Government Accountability Office (GAO).

Importantly, Federal Reserve lending should in no way be compared with government spending. Federal Reserve lending is repaid, with interest, and the Federal Reserve has never suffered a credit loss. As provided in the Dodd-Frank Act, the GAO conducted a review of all of the emergency lending facilities and confirmed in its report on July 21, 2011, that not only were there no material issues with respect to the design, implementation and operation of the facilities, but that all loans to the facilities were fully repaid or expected to be fully repaid.

Third, the articles make *no mention* that the emergency loans and other assistance have generated considerable income for the American taxpayers. As reported in the Annual Report of the Board of Governors, alongside the Board's audited financial statements, the emergency lending programs have generated an estimated $20 billion in interest income for the Treasury. Moreover, in 2009 and 2010, the Federal Reserve returned to the taxpayers over $125 billion in excess earnings on its operations, including emergency lending. These amounts have been publicly announced and are reflected in the Office of Management and Budget's financial statements for the government and have been verified by the Federal Reserve's independent outside auditors. The Federal Reserve is on track to return a comparable amount to taxpayers this year as well.

Fourth, the articles discuss the lending made to large banks but never note that Federal Reserve lending programs went far beyond such institutions--all in furtherance of supporting the provision of credit to U.S. households and businesses. Literally hundreds of institutions borrowed from the Federal Reserve--not just large banks. The TAF had some 400 borrowers and the discount window some 2,100 borrowers. The TALF made more than 2,000 loans, while the commercial paper funding facility provided direct assistance to some 120 American businesses.

The articles also fail to note that the lending directly helped support American businesses by providing emergency funding so that they could meet weekly payrolls and on-going expenses. The commercial paper funding facility, for example, provided support to businesses as diverse as Harley-Davidson and National Rural Utilities, when the usual market mechanism for their day-to-day funding completely dried up.

And the articles fail to mention altogether that one facility, the TALF, supported nearly 3 million auto loans, more than 1 million student loans, nearly 900,000 loans to small businesses, 150,000 other business loans, and millions of credit card loans. Auto lenders that funded their operations in part with asset-backed securities supported by the TALF told us that the program allowed them to provide more credit to consumers and at lower rates than they would have been able to do otherwise. The TALF also facilitated the first issuance of a commercial mortgage-backed security following a year-and-a-half drought, a security that provided an important benchmark for pricing and helped establish the higher credit standards now seen in the market.

Fifth, the articles misleadingly depict financial institutions receiving liquidity assistance as insolvent and in "deep trouble." During a financial panic, otherwise solvent banks and other financial institutions can be forced to sell assets at fire-sale prices in order to meet the demands of depositors and other sources of funding. Central bank liquidity lending is designed to stem the panic by giving financial institutions a source of financing that permits them to refrain from selling assets during the panic. Again, unmentioned in these articles--but a central point--all discount window loans extended during the crisis were fully repaid with interest, indicating that, with rare exceptions, recipients of these loans generally suffered from temporary liquidity problems rather than being fundamentally insolvent. In the handful of instances when discount window loans were extended to troubled institutions, it was in consultation with the Federal Deposit Insurance Corporation to facilitate a least-cost resolution; in these instances also, the Federal Reserve was fully repaid.

Finally, one article incorrectly asserted that banks "reaped an estimated $13 billion of income by taking advantage of the Fed's below-market rates." Most of the Federal Reserve's lending facilities were priced at a *penalty* over normal market rates so that borrowers had economic incentives to exit the facilities as market conditions normalized, and the rates that the Federal Reserve charged on its lending programs did not provide a subsidy to borrowers.