United States Government Accountability Office

GAO

Report to Congressional Committees

December 2009

FINANCIAL AUDIT

Office of Financial Stability (Troubled Asset Relief Program) Fiscal Year 2009 Financial Statements

GAO-10-301

FINANCIAL AUDIT

Office of Financial Stability (Troubled Asset Relief Program) Fiscal Year 2009 Financial Statements

GAO Accountability·Integrity·Reliability

Highlights

Highlights of GAO-10-301, a report to congressional committees

Why GAO Did This Study

On October 3, 2008, the Emergency Economic Stabilization Act of 2008 (EESA) was signed into law. EESA authorized the Secretary of the Treasury to implement the Troubled Asset Relief Program (TARP) and established the Office of Financial Stability (OFS) within the Department of the Treasury (Treasury) to do so. EESA requires the annual preparation of financial statements for TARP, and further requires GAO to audit these statements.

GAO audited OFS's fiscal year 2009 financial statements for TARP to determine whether, in all material respects, (1) the financial statements were fairly stated, and (2) OFS management maintained effective internal control over financial reporting. GAO also tested OFS's compliance with selected provisions of laws and regulations.

We will be separately reporting to OFS on additional details concerning the findings in this report along with recommendations for corrective actions. In commenting on a draft of this report, the Assistant Secretary, Office of Financial Stability, stated OFS concurred with the two significant deficiencies in its internal control over financial reporting GAO identified. He also stated that OFS is committed to correcting the deficiencies.

View GAO-10-301 or key components.
For more information, contact Gary T. Engel at (202) 512-3406 or engelg@gao.gov.

What GAO Found

In GAO's opinion, OFS's fiscal year 2009 financial statements for TARP are fairly presented in all material respects. GAO also concluded that, although internal controls could be improved, OFS maintained, in all material respects, effective internal control over financial reporting as of September 30, 2009. GAO found no reportable instances of noncompliance with the provisions of laws and regulations it tested.

Since its inception on October 3, 2008, OFS implemented numerous initiatives under TARP. As of September 30, 2009, net assets related to TARP direct loans, equity investments, and asset guarantees had an estimated value of about $239.7 billion. In addition, for the period ending September 30, 2009, OFS reported an estimated subsidy cost (estimated losses related to its direct loans, equity investments, and asset guarantees) of $41.4 billion and a net cost of operations of $41.6 billion for TARP, which includes the estimated subsidy costs. In valuing TARP direct loans, equity investments, and asset guarantees, OFS management considered and selected assumptions and data that it believed provided a reasonable basis for the estimated costs reported in the financial statements. However, these assumptions and estimates are inherently subject to substantial uncertainty arising from the likelihood of future changes in general economic, regulatory, and market conditions. The estimates have an added uncertainty arising from the uniqueness of transactions for the multiple TARP initiatives and the lack of historical information and program experience upon which to base the estimates. As such, there will be differences between the net estimated values of the direct loans, equity investments, and asset guarantees as of September 30, 2009, and the amounts that OFS will ultimately realize from these assets, and such differences may be material. These differences will also affect the ultimate cost of TARP to the taxpayer.

GAO identified two significant deficiencies in OFS's internal control over financial reporting concerning (1) accounting and financial reporting processes, and (2) verification procedures over the data used for asset valuations. While these deficiencies are not considered material weaknesses, they are important enough to merit management's attention.

Contents

United States Government Accountability Office
Washington, D.C. 20548

December 9, 2009

Congressional Committees

The accompanying auditor's report presents the results of our audit of the fiscal year 2009 financial statements of the Office of Financial Stability (Troubled Asset Relief Program). The Emergency Economic Stabilization Act (EESA) of 2008[1] that authorized the Troubled Asset Relief Program (TARP) on October 3, 2008, requires that TARP, which is implemented by the Office of Financial Stability (OFS),[2] annually prepare and submit to Congress and the public audited fiscal year financial statements that are prepared in accordance with generally accepted accounting principles.[3] EESA further requires that GAO audit TARP's financial statements annually.[4] We also are required under EESA to report at least every 60 days on the findings resulting from our oversight of the actions taken under TARP.[5] This report responds to both of these requirements. Fiscal year 2009 was the first year that OFS prepared and issued audited financial statements for TARP. This accomplishment was made possible by the dedication of significant time and effort from both OFS management and staff.

This report contains our (1) unqualified opinion on OFS's fiscal year 2009 financial statements for TARP; (2) opinion that, although certain controls could be improved, OFS maintained, in all material respects, effective internal control over financial reporting as of September 30, 2009; and (3) conclusion that OFS complied, during the period ended

[1]Pub. L. No. 110-343, Div. A, 122 Stat. 3765 (Oct. 3, 2008), *codified in part, as amended, at* 12 U.S.C. §§ 5201-5261.

[2]Section 101 of EESA, 12 U.S.C. § 5211, established OFS within Treasury to implement TARP.

[3]Section 116(b) of EESA, 12 U.S.C. § 5226(b).

[4]Section 116(b) of EESA, 12 U.S.C. § 5226(b).

[5]Section 116 of EESA, 12 U.S.C. § 5226, requires the U.S. Comptroller General to report at least every 60 days, as appropriate, on findings resulting from oversight of TARP's performance in meeting the act's purposes; the financial condition and internal controls of TARP, its representatives, and agents; the characteristics of asset purchases and the disposition of acquired assets, including any related commitments entered into; TARP's efficiency in using the funds appropriated for its operations; its compliance with applicable laws and regulations; and its efforts to prevent, identify, and minimize conflicts of interest among those involved in its operations.

September 30, 2009, with provisions of laws and regulations we tested. The accompanying report also provides an overview of two significant deficiencies[6] in OFS's internal control over financial reporting that we identified while performing our audit that we believe merit the attention of OFS management and users of OFS's financial statements. We will be reporting separately to OFS on more detailed information concerning these significant deficiencies along with recommended corrective actions.

Since its inception, OFS implemented numerous initiatives under TARP including the (1) Capital Purchase Program, (2) Targeted Investment Program, (3) Asset Guarantee Program, (4) Consumer and Business Lending Initiative, (5) Public-Private Investment Program, (6) American International Group, Inc. Investment Program (formerly known as the Systemically Significant Failing Institutions Program), (7) Automotive Industry Financing Program, and (8) Home Affordable Modification Program. These initiatives are described in more detail in the footnotes to OFS's financial statements and Management's Discussion and Analysis (MD&A) included in this report.

As of September 30, 2009, OFS reported net assets related to TARP direct loans, equity investments, and asset guarantees of about $239.7 billion, which is net of a subsidy cost allowance of about $53.1 billion. The subsidy cost allowance represents the difference between the amounts paid by OFS for the direct loans, equity investments, and asset guarantees and the reported value of such assets. In addition, for the period ended September 30, 2009, OFS reported an estimated subsidy cost[7] of $41.4 billion and a net cost of operations of $41.6 billion for TARP, which includes the estimated subsidy cost.

---

[6]A significant deficiency is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. A material weakness is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis.

[7]The subsidy cost is composed of (1) the subsidy cost allowance, (2) net intragovernmental interest cost, (3) certain inflows from the direct loans and equity investments (e.g., dividends, interest, proceeds from repurchase of warrants by financial institutions, and other realized fees), and (4) the estimated discounted net cash flows related to the Asset Guarantee Program.

OFS management considered and selected assumptions and data that it believed provided a reasonable basis for the estimated costs reported in the financial statements. However, these assumptions and estimates are inherently subject to substantial uncertainty arising from the likelihood of future changes in general economic, regulatory, and market conditions. The estimates have an added uncertainty arising from the uniqueness of transactions for the multiple TARP initiatives and the lack of historical information and program experience upon which to base the estimates. As such, there will be differences between the net estimated values of the direct loans, equity investments, and asset guarantees as of September 30, 2009, and the amounts that OFS will ultimately realize from these assets, and such differences may be material. These differences will also affect the ultimate cost of TARP. Further, the ultimate cost will change as OFS continues to purchase additional assets and incur related subsidy costs as well as incur costs under other TARP initiatives.[8] OFS's authority to purchase or insure additional troubled assets expires on December 31, 2009, but may be extended by the Secretary of the Treasury to up to October 3, 2010.[9]

We are sending copies of this report to the Secretary of the Treasury, Assistant Secretary for Financial Stability, Congressional Oversight Panel, Financial Stability Oversight Board, Special Inspector General for TARP, Office of Management and Budget, interested congressional committees and members, and others. The report is available at no charge on GAO's Web site at http://www.gao.gov.

[8]Under EESA, as amended, OFS is authorized to purchase or insure up to almost $700 billion in troubled assets.

[9]Section 120 of EESA, 12 U.S.C. § 5230, established that the authorities under Sections 101(a), excluding Section 101(a)(3), and Section 102, shall terminate on December 31, 2009. Section 120 of EESA further established that the Secretary of the Treasury, upon submission of a written certification to Congress, may extend the authority provided under these sections of EESA to expire no later than 2 years from the date of the enactment of EESA (Oct. 3, 2008).

If you have questions about this report, please contact me at (202) 512-3406 or engelg@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made key contributions to this report are listed in appendix III.

Sincerely yours,

Gary T. Engel
Director
Financial Management and Assurance

List of Congressional Committees

The Honorable Daniel K. Inouye
Chairman
The Honorable Thad Cochran
Vice Chairman
Committee on Appropriations
United States Senate

The Honorable Christopher J. Dodd
Chairman
The Honorable Richard C. Shelby
Ranking Member
Committee on Banking, Housing, and Urban Affairs
United States Senate

The Honorable Kent Conrad
Chairman
The Honorable Judd Gregg
Ranking Member
Committee on the Budget
United States Senate

The Honorable Max Baucus
Chairman
The Honorable Charles E. Grassley
Ranking Member
Committee on Finance
United States Senate

The Honorable David R. Obey
Chairman
The Honorable Jerry Lewis
Ranking Member
Committee on Appropriations
House of Representatives

The Honorable John M. Spratt, Jr.
Chairman
The Honorable Paul Ryan
Ranking Member
Committee on the Budget
House of Representatives

The Honorable Barney Frank
Chairman
The Honorable Spencer Bachus
Ranking Member
Committee on Financial Services
House of Representatives

The Honorable Charles B. Rangel
Chairman
The Honorable Dave Camp
Ranking Member
Committee on Ways and Means
House of Representatives

GAO

Accountability * Integrity * Reliability

United States Government Accountability Office
Washington, D.C. 20548

To the Assistant Secretary for Financial Stability

In accordance with the Emergency Economic Stabilization Act of 2008 (EESA),[1] we are required to audit the financial statements of the Troubled Asset Relief Program (TARP), which is implemented by the Office of Financial Stability (OFS).[2] In our audit of OFS's financial statements for TARP for the period from October 3, 2008, (date of OFS's inception) through September 30, 2009, we found

- the financial statements are presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles;
- although internal controls could be improved, OFS maintained, in all material respects, effective internal control over financial reporting as of September 30, 2009; and
- no reportable noncompliance in the period ended September 30, 2009, with provisions of laws and regulations we tested.

The following sections discuss in more detail (1) these conclusions; (2) our conclusion on Management's Discussion and Analysis (MD&A) and other required supplementary and other accompanying information; (3) our audit objectives, scope, and methodology; and (4) OFS's comments on a draft of this report. In addition to our responsibility to audit OFS's annual financial statements for TARP, we also are required under EESA to report at least every 60 days on the findings resulting from our oversight of the actions taken under TARP.[3] This report responds to both of these requirements. We

[1]Section 116(b) of EESA, 12 U.S.C. § 5226(b), requires that the Department of the Treasury (Treasury) annually prepare and submit to Congress and the public audited fiscal year financial statements for TARP that are prepared in accordance with generally accepted accounting principles. Section 116(b) further requires that GAO audit TARP's financial statements annually in accordance with generally accepted auditing standards.

[2]Section 101 of EESA, 12 U.S.C. § 5211, established OFS within Treasury to implement TARP.

[3]Section 116 of EESA, 12 U.S.C. § 5226, requires the U.S. Comptroller General to report at least every 60 days, as appropriate, on findings resulting from oversight of TARP's performance in meeting the act's purposes; the financial condition and internal controls of TARP, its representatives, and agents; the characteristics of asset purchases and the disposition of acquired assets, including any related commitments entered into; TARP's efficiency in using the funds appropriated for its operations; its compliance with applicable laws and regulations; and its efforts to prevent, identify, and minimize conflicts of interest among those involved in its operations.

have issued numerous other reports on TARP in connection with this 60-day reporting responsibility which can be found on GAO's Web site at http://www.gao.gov.

Opinion on Financial Statements

OFS's financial statements for TARP, including the accompanying notes, present fairly, in all material respects, in conformity with U.S. generally accepted accounting principles, OFS's assets, liabilities, and net position as of September 30, 2009, and its net cost, changes in net position, and budgetary resources for the period from October 3, 2008, (date of OFS's inception) through September 30, 2009.

As discussed in notes 2 and 6 to OFS's financial statements for TARP, the valuation of TARP direct loans, equity investments, and asset guarantees is based on estimates using economic and financial credit subsidy models. The estimates use entity-specific as well as relevant market data as the basis for assumptions about future performance, and incorporate an adjustment for market risk to reflect the variability around any unexpected losses. In valuing the direct loans, equity investments, and asset guarantees, OFS management considered and selected assumptions and data that it believed provided a reasonable basis for the estimated subsidy allowance and related subsidy costs reported in the financial statements.[4] However, there are a large number of factors that affect these assumptions and estimates, which are inherently subject to substantial uncertainty arising from the likelihood of future changes in general economic, regulatory, and market conditions. The estimates have an added uncertainty resulting from the unique nature of transactions associated with the multiple initiatives undertaken for TARP and the lack of historical program experience upon which to base the estimates. As such, there will be differences between the net estimated values of the direct loans, equity investments, and asset guarantees as of September 30, 2009, that totaled $239.7 billion, and the amounts that OFS will ultimately realize from these assets, and such differences may be material. These differences will also affect the ultimate cost of TARP. Further, the ultimate cost will change as

[4]The subsidy allowance represents the difference between the amounts paid by OFS to acquire the direct loans and equity investments and the reported value of such assets. The subsidy cost is composed of (1) the subsidy cost allowance, (2) net intragovernmental interest cost, (3) certain inflows from the direct loans and equity investments (e.g., dividends, interest, proceeds from repurchase of warrants by financial institutions, and other realized fees), and (4) the estimated discounted net cash flows related to the Asset Guarantee Program.

OFS continues to purchase troubled assets and incur related subsidy costs as well as incur costs under other TARP initiatives.[5] OFS's authority to purchase or insure additional troubled assets expires on December 31, 2009, but may be extended by the Secretary of the Treasury to up to October 3, 2010.[6]

As discussed in note 1 to the financial statements, while OFS's financial statements reflect activity of OFS in implementing TARP, including providing resources to various entities to help stabilize the financial markets, the statements do not include the assets, liabilities, or results of operations of commercial entities in which OFS has a significant equity interest. According to OFS officials, OFS's investments were not made to engage in the business activities of the respective entities and OFS has determined that none of these entities meet the criteria for a federal entity.

Opinion on Internal Control

Although certain internal controls could be improved, OFS maintained, in all material respects, effective internal control over financial reporting as of September 30, 2009, that provided reasonable assurance that misstatements, losses, or noncompliance material in relation to the financial statements would be prevented or detected and corrected on a timely basis. Our opinion on internal control is based on criteria established under 31 U.S.C. § 3512(c), (d), commonly known as the Federal Managers' Financial Integrity Act (FMFIA).

[5] Under EESA, as amended, OFS is authorized to purchase or insure up to almost $700 billion in troubled assets.

[6] Section 120 of EESA, 12 U.S.C. § 5230, established that the authorities under Sections 101(a), excluding Section 101(a)(3), and Section 102, shall terminate on December 31, 2009. Section 120 of EESA further established that the Secretary of the Treasury, upon submission of a written certification to Congress, may extend the authority provided under these sections of EESA to expire no later than 2 years from the date of the enactment of EESA (Oct. 3, 2008).

We identified two significant deficiencies[7] in OFS's internal control over financial reporting, which although not material weaknesses, are important enough to merit management's attention. These deficiencies, described in more detail later in this report, concern OFS's (1) accounting and financial reporting processes, and (2) verification procedures for data used for asset valuations.

We will be reporting additional details concerning these significant deficiencies separately to OFS management, along with recommendations for corrective actions. We also identified other deficiencies in OFS's system of internal control that we consider not to be material weaknesses or significant deficiencies. We have communicated these matters to management and, where appropriate, will report on them separately.

Significant Deficiencies

Since its creation on October 3, 2008, OFS has made significant progress in building a financial reporting structure, including developing an internal control system over TARP activities and transactions and addressing key accounting and financial reporting issues necessary to enable it to prepare financial statements, and receive an audit opinion on those statements, for the period ended September 30, 2009. However, OFS's financial reporting structure continued to evolve throughout the year as new TARP programs were implemented, which posed a challenge to OFS's ability to establish a comprehensive system of internal control while simultaneously reacting to market events and implementing TARP initiatives. This challenge contributed to the following two significant deficiencies in OFS's internal control that we identified.

Accounting and Financial Reporting Processes

While OFS had developed and implemented controls over TARP transactions and activities, we identified several control deficiencies that collectively represented a significant deficiency in OFS's internal control

[7] A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis.

over its accounting and financial reporting processes. Specifically, OFS did not effectively implement its review and approval process for preparing its financial statements and related disclosures for TARP. We identified incorrect amounts and inaccurate, inconsistent, and incomplete disclosures in OFS's draft financial statements, footnotes, and MD&A for TARP that were significant, but not material, and that were not detected by OFS. OFS revised the financial statements, footnotes, and MD&A to address the issues that we identified. In addition, OFS had not finalized its procedures related to its processes for accounting for certain program transactions, preparing its September 30, 2009, financial statements, and its oversight and monitoring of financial-related services provided to OFS by asset managers and certain financial agents. Further, OFS did not have proper segregation of duties over a significant accounting database it uses in valuing its assets in that the same individual was responsible for performing both the data entry and the reconciliation of the data output. However, OFS had other controls over TARP transactions and activities that reduced the risk of misstatements resulting from these deficiencies. Properly designed and implemented controls over the accounting and financial reporting processes are key to providing reasonable assurance regarding the reliability of the balances and disclosures reported in the financial statements and related notes in conformity with generally accepted accounting principles.

Verification Procedures for Data Input for Asset Valuations

OFS did not effectively implement its verification procedures for certain assumptions and related data that were input into the economic and financial credit subsidy models used for the valuation of TARP direct loans, equity investments, and asset guarantees. Specifically, we identified data input errors to the estimation models, such as incorrect dividend rates and maturity dates, that were not detected by OFS's verification procedures. Significant errors that we identified were corrected and amounts were properly reflected in the September 30, 2009, financial statements. OFS did perform procedures to assess the reasonableness of the model outputs, including comparison of the asset valuations calculated by the model with independently performed valuations. We believe that these procedures reduced the risk of misstatements resulting from the data input errors. Nonetheless, we believe the ineffective implementation of data input verification procedures represents a significant deficiency in OFS's internal control warranting management's attention. Effective verification of data inputs used in the subsidy models is key to providing reasonable assurance that the asset valuations and related subsidy cost are reliably reported in the financial statements.

Compliance with Laws and Regulations

Our tests of OFS's compliance with selected provisions of laws and regulations for the period ended September 30, 2009, disclosed no instances of noncompliance that would be reportable under U.S. generally accepted government auditing standards. The objective of our audit was not to provide an opinion on overall compliance with laws and regulations. Accordingly, we do not express such an opinion.

Consistency of Other Information

OFS's MD&A, other required supplementary information, and other accompanying information contain a wide range of information, some of which is not directly related to the financial statements. We did not audit and we do not express an opinion on this information. However, we compared this information for consistency with the financial statements and discussed the methods of measurement and presentation with OFS officials. On the basis of this limited work, we found no material inconsistencies with the financial statements, U.S. generally accepted accounting principles, or the form and content guidance in Office of Management and Budget Circular No. A-136, *Financial Reporting Requirements*.

Objectives, Scope, and Methodology

OFS management is responsible for (1) preparing the financial statements in conformity with U.S. generally accepted accounting principles; (2) establishing and maintaining effective internal control over financial reporting, and evaluating its effectiveness; and (3) complying with applicable laws and regulations. Management evaluated the effectiveness of OFS's internal control over financial reporting as of September 30, 2009, based on the criteria established under FMFIA. OFS management's assertion based on its evaluation is included in appendix I.

We are responsible for planning and performing the audit to obtain reasonable assurance and provide our opinion about whether (1) OFS's financial statements are presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles; and (2) OFS management maintained, in all material respects, effective internal control over financial reporting as of September 30, 2009. We are also responsible for (1) testing compliance with selected provisions of laws and regulations that have a direct and material effect on the financial statements, and (2) performing limited procedures with respect to certain other information accompanying the financial statements.

In order to fulfill these responsibilities, we

- examined, on a test basis, evidence supporting the amounts and disclosures in the financial statements;
- assessed the accounting principles used and significant estimates made by management;
- evaluated the overall presentation of the financial statements;
- obtained an understanding of the entity and its operations, including its internal control over financial reporting;
- considered OFS's process for evaluating and reporting on internal control over financial reporting that OFS is required to perform by FMFIA and Section 116(c) of EESA;
- assessed the risk that a material misstatement exists in the financial statements and the risk that a material weakness exists in internal control over financial reporting;
- evaluated the design and operating effectiveness of internal control over financial reporting based on the assessed risk;
- tested relevant internal control over financial reporting;
- tested compliance with selected provisions of the following laws and regulations: EESA, as amended; the Antideficiency Act, as amended; the Federal Credit Reform Act of 1990; and the Purpose Statute; and
- performed such other procedures as we considered necessary in the circumstances.

An entity's internal control over financial reporting is a process affected by those charged with governance, management, and other personnel, the objectives of which are to provide reasonable assurance that (1) transactions are properly recorded, processed, and summarized to permit the preparation of financial statements in conformity with U.S. generally accepted accounting principles, and assets are safeguarded against loss from unauthorized acquisition, use, or disposition; and (2) transactions are executed in accordance with the laws governing the use of budget authority and other laws and regulations that could have a direct and material effect on the financial statements.

We did not evaluate all internal controls relevant to operating objectives as broadly established under FMFIA, such as those controls relevant to preparing statistical reports and ensuring efficient operations. We limited our internal control testing to testing controls over financial reporting. Because of inherent limitations, internal control may not prevent or detect and correct misstatements due to error or fraud, losses, or noncompliance. We also caution that projecting any evaluation of effectiveness to future periods is subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

We did not test compliance with all laws and regulations applicable to OFS. We limited our tests of compliance to selected provisions of laws and regulations that have a direct and material effect on the financial statements for the period ended September 30, 2009. We caution that noncompliance may occur and not be detected by these tests and that such testing may not be sufficient for other purposes.

We performed our audit in accordance with U.S. generally accepted government auditing standards. We believe our audit provides a reasonable basis for our opinions and other conclusions.

Agency Comments

In commenting on a draft of this report, the Assistant Secretary, Office of Financial Stability, stated OFS concurred with the two significant deficiencies in its internal control over financial reporting that GAO identified. He also stated that OFS is committed to correcting the deficiencies. The complete text of OFS's comments is reprinted in appendix II.

Gary T. Engel

Gary T. Engel
Director
Financial Management and Assurance

December 4, 2009

Executive Summary

This report provides a summary of the activities of the Troubled Asset Relief Program (TARP), which was established under the Emergency Economic Stabilization Act (EESA) last year. The purpose of TARP was to restore the liquidity and stability of the financial system. While we will never know for certain what would have happened without TARP, there is broad agreement today that because of TARP and other governmental actions, the United States averted a potentially catastrophic failure of the financial system.

This report also provides an update on the costs of TARP. While EESA provided the Secretary of the Treasury with the authority to purchase or guarantee $700 billion to meet the objectives of the Act, it is clear today that TARP will not cost taxpayers $700 billion. First, the Treasury's Office of Financial Stability (Treasury-OFS) is unlikely to disburse the full $700 billion. In addition, many of the investments under the program, particularly those aimed at stabilizing banks, are expected to deliver returns for taxpayers. This combination of lower spending and higher expected returns is expected to lower the projected costs of TARP from the $341 billion estimate in the President's Mid-session Budget in August 2009.

During the period ended September 30, 2009, the Treasury-OFS disbursed $364 billion of the authorized $700 billion, most of it in the form of investments, and $73 billion of those TARP funds have already been repaid as of such date. In addition, for the period ended September 30, 2009, the investments generated $12.7 billion in cash received through interest, dividends, and the proceeds from the sale of warrants. For those TARP disbursements in FY 2009, the Treasury-OFS reported net cost of operations of approximately $41.6 billion, including administrative expenses. The reported net cost of operations includes the estimated net cost related to loans, equity investments, and asset guarantees. As additional funds are distributed, particularly for the housing initiative, the total cost is likely to rise, although anticipated to remain substantially below the $341 billion estimate in the August 2009 Midsession estimate.

Four TARP programs reported net income in FY 2009: the Capital Purchase Program, the Targeted Investment Program, the Asset Guarantee Program, and the Consumer and Business Lending Initiative. This net income was offset by reported net cost of the investments in AIG and the automotive companies, bringing the net cost for these programs during FY 2009 to approximately $41.4 billion.

As further disbursements are made in FY 2010 and later, the costs of the TARP program are likely to rise. In particular, the $50 billion Home Affordable Modification Program or "HAMP," is not designed to recoup money spent on loan modifications to keep people in their homes. In addition, the Treasury-OFS' assistance to AIG includes an equity facility on which

$27 billion remained undrawn at fiscal year end, and $30 billion of investments and loans under the Public Private Partnership Program will largely be recorded beginning in FY 2010.

The ultimate return on the outstanding TARP investments will depend on how the economy and financial markets evolve. The general improvement in economic and financial environment, early repayments of TARP funds, and refinements to the valuation models have significantly lowered expected costs for the program funds disbursed in FY 2009 by $110 billion below the estimates made when the programs were initiated. About $10 billion of that decline in costs stems from early repayments of TARP funds.

These estimates will change. The design and the precise amounts of additional investments for small banks and to facilitate small business lending have not yet been determined. In addition, the ultimate return on TARP investments is subject to significant uncertainty as market conditions evolve.

While this report provides updated information on TARP's costs, the initiative should be evaluated primarily based on its impact on stabilizing the financial system. These investments were not made to make money but to help prevent a collapse of our financial system and lay the foundation for economic recovery. Today, the financial system and the economy are showing signs of stability. The cost of borrowing has declined to pre-crisis levels for many businesses, states and local governments, the government sponsored enterprises (GSEs), and the banks. Housing markets have shown signs of stabilization, and home prices have ticked up in recent months, after three straight years of declines. The economy grew in the third quarter, and most private economists predict it will grow for the remainder of this year and next.

That improvement in the economic and financial outlook since the spring reflects a broad and aggressive policy response that included the financial stability policies implemented under TARP, efforts to bolster confidence in the housing and mortgage markets under the Housing and Economic Reform Act (HERA), other financial stability policies implemented by the Federal Deposit Insurance Corporation and the Board of Governors of the Federal Reserve System (Federal Reserve), accommodative monetary policy, and the Obama Administration's fiscal stimulus package implemented under the American Recovery and Reinvestment Act of 2009.

While TARP was necessary, it has put the federal government in the unwelcome position of owning sizeable stakes in private sector companies. Given that unusual position as a reluctant shareholder, the Treasury-OFS has established a core set of principles to guide its actions. First and foremost, the Treasury-OFS is seeking to protect taxpayers by minimizing the long-term consequences of the current economic and financial crisis with as little direct cost to the taxpayer as possible. As economic and market conditions improve, Treasury-OFS aims to dispose of its investments as quickly as practicable, in a timely and orderly manner consistent with the duty to promote financial stability and protect taxpayers' interests.

To administer the programs under TARP, the Secretary of the Treasury has established the Treasury-OFS, which is designed to be temporary in nature, but also highly skilled and well equipped to handle the complexity of TARP initiatives. At the same time, Treasury-OFS' process is designed to be highly transparent. Congress and taxpayers are kept informed of TARP's actions, results, investments and costs through frequent and timely public reports, daily communication with oversight bodies, public responses to oversight reports, and direct outreach to taxpayers through its websites: *FinancialStability.gov* and *MakingHomeAffordable.gov*.

Because of the magnitude and importance of these programs, Congress established a strong oversight structure to ensure accountability. The Government Accountability Office (GAO), the Special Inspector General for TARP (SIGTARP), the Congressional Oversight Panel (COP) and the Financial Stability Oversight Board (FINSOB) engage in frequent reviews of TARP activities and have contributed to making the programs stronger and more effective.

Despite TARP's positive record to date, and the improving financial and economic outlook, significant challenges remain for the financial sector and our economy. While the economy is growing again, jobs are still being lost and the unemployment situation continues to worsen. The pace of bank failures, which tends to lag economic cycles, remains elevated. Foreclosure rates also remain very high, and bank lending has contracted, with credit standards tight. Commercial real estate losses weigh heavily on many banks, especially on smaller banks, impairing their ability to extend new loans. Small businesses have been particularly affected because they rely heavily on bank lending and do not have the ability to raise capital through the securities markets.

While a number of TARP initiatives, particularly those for large institutions, have begun to wind down, Treasury-OFS continues to focus on stabilizing the housing markets as well as improving access to credit for small businesses. Treasury-OFS is also mindful of the fact that risks remain, and history suggests that exiting too soon from policies designed to contain a financial crisis can significantly prolong an economic downturn. It is within this larger context that the Secretary of the Treasury will evaluate and decide whether to extend TARP authority past December 31, 2009.

Section One: Background and Creation of TARP

Stresses in U.S. financial markets began to emerge in 2007 as the performance of subprime mortgages deteriorated significantly, and losses on related securities began to climb. With the extent and distribution of losses quite uncertain, concerns surfaced about the financial condition of banks and other financial institutions. Pressures in short-term funding markets escalated and some off-balance sheet funding vehicles were not able to renew their asset-backed commercial paper, raising concerns about the ability of sponsoring banks to meet funding needs. As a consequence, short-term credit markets came under considerable pressure and risk spreads in interbank funding markets and in some segments of the commercial paper (CP) market rose sharply. Announcements of large asset write-downs and weak financial reports for many large financial institutions in late 2007 raised additional concerns about the resilience and capital adequacy of financial counterparties and the likelihood of further large losses.

Continuing declines in mortgage loan performance, market valuations of mortgage-related assets, and the credit ratings of even so-called "super-senior" tranches of structured finance securitizations heightened the pressure on financial institutions with significant known exposures in these areas. Market participants became increasingly cautious and, in some cases, unwilling to extend funding to the most-affected institutions, as in the case of Bear Stearns. In March 2008, the Federal Reserve, with the full support of the Treasury, facilitated a merger of Bear Stearns with JPMorgan Chase to prevent a disorderly collapse of the firm and potentially severe spillover effects in the financial markets. The condition of financial guarantors weakened, calling into question the value of the insurance they had written, leading to declines in the value of products insured by these entities. In March 2008, the Federal Reserve introduced two new liquidity facilities (the Primary Dealer Credit Facility and the Term Securities Lending Facility), which increased the liquidity available to primary dealers.

Pressures in financial markets initially appeared to ease somewhat as a consequence of these actions. However, housing conditions and the broader economy continued to deteriorate, and financial institutions came under renewed stress in the summer of 2008. Capital market dislocations and volatility combined with losses and expectations of further losses on mortgage-related assets resulted in the debt spreads of Fannie Mae and Freddie Mac widening and these two companies becoming unable to raise new capital or long-term debt. In September, the Federal Housing Finance Agency (FHFA) placed these firms into conservatorship while obtaining backup capital and funding support from Treasury under authority granted in July 2008 by the Housing and Economic Recovery Act of 2008.

In mid-September, a series of events caused the crisis to escalate. Lehman Brothers came under heightened funding pressures, and on September 15, 2008, the parent company filed for bankruptcy protection. American International Group, Inc. (AIG), a global insurance company, experienced severe liquidity pressures, necessitating assistance from the Federal Reserve, with the concurrence of Treasury, on September 16, 2008, to prevent the potential for severe systemic consequences from a disorderly failure of the firm. In the wake of the bankruptcy of Lehman Brothers and the near failure of AIG, spreads on interbank borrowing jumped to a record high as banks sought to safeguard their own liquidity and interbank lending volumes contracted sharply. Losses on Lehman Brothers commercial paper caused a money market mutual fund to experience Net Asset Valuations of less than $1 per share (i.e., "breaking the buck") and investors accelerated withdrawals from prime money market funds, forcing sales of their CP holdings. Total CP outstanding fell sharply, leaving many financial and nonfinancial businesses with sharply reduced access to needed short-term funds. Many such institutions tapped existing back-up lines of credit at banks, adding to the pressure on liquidity funding needs of those banks. To support the functioning of money market mutual funds, on September 19, 2008, the Treasury initiated an insurance program for existing balances at money market mutual funds. In addition, the Federal Reserve established the Asset-Backed Commercial Paper Money Market Mutual Fund Liquidity Facility (AMLF) to provide liquidity to money market mutual funds that were holding asset-backed commercial paper.

The loss of confidence in financial institutions also contributed to the failure of Washington Mutual, the largest U.S. thrift institution in September 2008. The FDIC sold the banking operations of the institution to JPMorgan Chase. Wachovia Corporation subsequently came under intense funding pressures, and ultimately was acquired by Wells Fargo & Co. Moreover, as the financial crisis intensified in the U.S. and abroad, risks to the stability of the international financial system increased. To help ease liquidity pressures, the Federal Reserve in coordination with other central banks around the globe provided dollar liquidity to banking institutions through reciprocal currency (or swap) lines.

Accompanying the pressures in interbank and other funding markets, and in light of the weakening economy, banks continued to tighten their credit terms and standards on loans to their customers. The tighter terms and standards reduced credit availability, leaving its imprint on economic activity. In the corporate bond market, borrowing costs increased dramatically and the spread of corporate yields to comparable maturity Treasury yields rose, reflecting financial market stresses and a weakening economic outlook. Broad stock price indexes fell sharply, nearly 15 percent in early October 2008, leaving them down about 40 percent from the beginning of 2008.

This accumulation and confluence of events placed severe financial stresses on financial markets and institutions, and strong pressures on institutions to deleverage and restrain lending. Because of the dependence of our economy on the flow of credit, serious strains on credit providers can impose disproportionately large costs on the broader economy. Responding to these severe conditions, the Treasury, Federal Reserve, Federal Housing Finance Agency (FHFA), Federal Deposit Insurance Corporation (FDIC), and other U.S. government bodies undertook an array of unprecedented actions in accordance with their respective authorities. However, additional resources and authorities were needed to help address the significant problems in the financial markets and the dangers posed by such problems to consumers, businesses, and the broader economy. To provide additional resources and authorities, Congress passed the Emergency Economic Stabilization Act of 2008 (EESA)[1] which was signed into law by President George W. Bush on October 3, 2008. The purposes of EESA were to provide authority and facilities that the Secretary of the Treasury could use to restore liquidity and stability to the financial system of the United States, and to ensure that such authority and facilities were used in a manner that protected home values, college funds, retirement accounts, and life savings; preserved home ownership; promoted jobs and economic growth; maximized overall returns to the taxpayers of the United States; and provided public accountability for the exercise of such authority.

Mission and Organizational Structure

The EESA established the Office of Financial Stability (OFS) within the Office of Domestic Finance of the Treasury Department to implement the TARP. The mission of Treasury-OFS is to carry out the authorities given to the Secretary of the Treasury to implement the Troubled Asset Relief Program (TARP). Section 101 of EESA authorized the Secretary of the Treasury to establish the TARP to "purchase, and to make and fund commitments to purchase, troubled assets from any financial institution, on terms and conditions as are determined by the Secretary". EESA defines the terms "troubled assets" and "financial institution" and provides other requirements that must be met for any such purchase. The statute also provides authority for a guarantee program for troubled assets.

EESA Section 101: Definitions	
Troubled Assets are defined by EESA as residential or commercial mortgages and any securities, obligations or other instruments that are based on or related to such mortgages, that in each case was originated or issued on or before March 14, 2008, the purchase of which the Secretary of the Treasury determines	Financial Institutions are defined by EESA as any institution, including, but not limited to, any bank, savings association, credit union, security broker or dealer, or insurance company, established and regulated under the laws of the United States or any State, territory, or possession of the United States, the

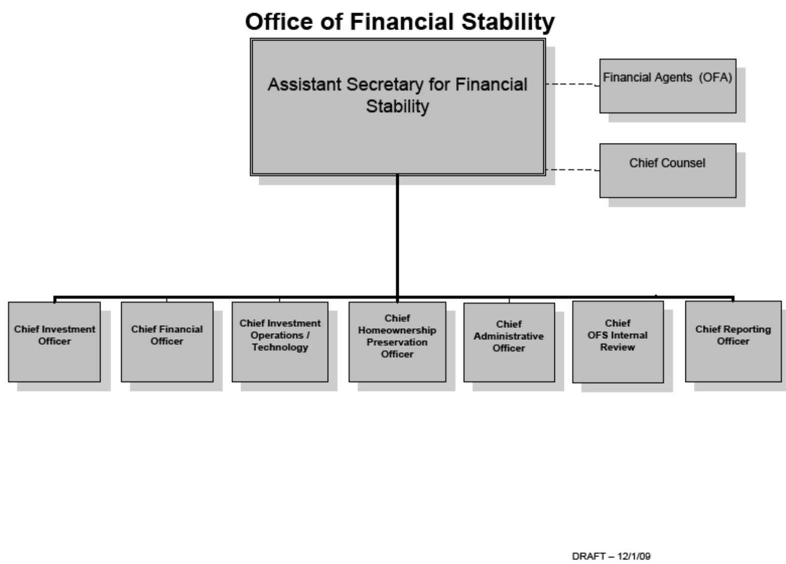
[1] The Emergency Economic Stabilization Act of 2008 (EESA), Pub. L. No. 110-343, 122 Stat.3765 (2008), codified at 12 U.S.C. §§ 5201 et seq.

6

promotes financial market stability; and any other financial instrument that the Secretary of the Treasury, after consultation with the Chairman of the Board of Governors of the Federal Reserve System, determines the purchase of which is necessary to promote financial market stability, but only upon transmittal of such determination, in writing, to the appropriate committees of Congress.	District of Columbia, Commonwealth of Puerto Rico, Commonwealth of Northern Mariana Islands, Guam, American Samoa, or the United States Virgin Islands, and having significant operations in the United States, but excluding any central bank of, or institution owned by, a foreign government.

Treasury-OFS is headed by an Assistant Secretary of the Treasury, appointed by the President with the advice and consent of the Senate. Reporting to the Assistant Secretary for Financial Stability are seven major divisions: the Offices of the Chief Investment Officer, the Chief Financial Officer, the Chief for Investment Operations/Technology, the Chief Homeownership Preservation Officer, the Chief Administrative Officer, the Chief Reporting Officer, and the Chief for OFS Internal Review. A Chief Counsel's Office reports to the Assistant Secretary and to the Office of the General Counsel in the Department of Treasury.

The Treasury-OFS organization chart is shown below:



Additional information regarding the operations of these divisions and other aspects of Treasury-OFS' operations can be found in Section Ten [Other Management Information] of this report.

8

Section Two: Overview and Analysis of the Troubled Asset Relief Program

This section provides a broad overview of the TARP. It begins by placing the program in context, explaining why it was a necessary ingredient of a coordinated government response to contain and resolve the financial crisis. This is followed by a discussion of Treasury-OFS' strategic goals, and how particular programs and activities were developed to meet each of these goals. Next, this section presents the TARP financial summary for the period ended September 30, 2009. Finally, this section concludes with a discussion of the aggregate impact of TARP and other government financial policies on financial markets and institutions. These are the metrics by which we evaluate success or failure of government support policies.

TARP in Context: A Critical Pillar of a Coordinated Government Response

This crisis really began in August 2007. The Federal Reserve, and to a lesser extent the FDIC, led the policy response during the first year of the crisis. Before September 2008, the Federal Reserve was providing sorely-needed liquidity to many financial institutions, which allowed them to meet near-term obligations. The FDIC was insuring deposits, which helped quell traditional bank runs, and it was resolving troubled depository institutions, such as IndyMac.

But when stress in the system dramatically intensified in the wake of the Lehman Brothers failure, investors began to question whether the financial system was solvent and confidence collapsed. A different sort of policy response was needed.

The Federal Reserve does not have the authority to directly inject capital into banks and other financial institutions to address potential capital shortfalls. Although it has expanded the scope of eligible borrowers and collateral over the past few years, the Federal Reserve's liquidity provision is confined to secured lending against good collateral. This is a powerful, but limited tool. The large amount of troubled assets held by financial institutions heightened the markets' fears.

The FDIC has a broader toolset in some respects--including the ability to inject capital or to purchase or guarantee liabilities--but only for depository institutions. This too proved a stabilizing factor. But in the fall of last year the crisis spread well beyond traditional banks, and threatened to exceed the limitations of the FDIC's capacity to effectively respond. Investors feared that U.S. financial institutions needed, in the aggregate, hundreds of billions of dollars to offset potential credit losses.

In this context the passage of EESA was essential. It gave the Secretary of the Treasury temporary authority to purchase and guarantee assets in a wide range of financial institutions and markets. As explained below, that step, combined with the actions of other government agencies and the Federal Reserve, helped prevent the potential collapse of the U.S. financial system. To

9

date, the cost has been considerably less than what was originally projected. Today, EESA programs continue to stabilize and rehabilitate still fragile markets and institutions, while repayments of the government's investments over the past year have already begun.

OFS Strategic Goals

The purpose of EESA is to provide the Secretary of the Treasury with the authorities and facilities necessary to stabilize the U.S. financial system. In addition, the Secretary is directed to ensure that such authorities are used in a manner that protects home values, college funds, retirement accounts, and life savings; preserves homeownership; promotes jobs and economic growth; maximizes overall returns to taxpayers; and provides public accountability. The EESA also provided specific authority to take certain actions to prevent avoidable foreclosures.

In light of this statutory direction, Treasury-OFS established the following as its operational goals:

1. Ensure the overall stability and liquidity of the financial system.
    a. Make capital available to viable institutions.
    b. Provide targeted assistance as needed.
    c. Increase liquidity and volume in securitization markets.
2. Prevent avoidable foreclosures and help preserve homeownership.
3. Protect taxpayer interests.
4. Promote transparency.

1. Ensure the Overall Stability and Liquidity of the Financial System

To ensure the overall stability and liquidity of the financial system, Treasury-OFS developed several programs under the TARP that were broadly available to financial institutions. Under the Capital Purchase Program (CPP), Treasury-OFS provided capital infusions directly to banks and insurance companies deemed viable by their regulators but in need of a stronger asset base to weather the crisis. The Capital Assistance Program (CAP) was developed to supplement the Supervisory Capital Assessment Program (SCAP), or "stress test" of the largest U.S. financial institutions. If these institutions were unable to raise adequate private funds to meet the SCAP requirements, Treasury-OFS stood ready to provide additional capital.

In addition, Treasury-OFS provided direct aid to certain financial industry participants through the Targeted Investment Program (TIP) and the Asset Guarantee Program (AGP), as well as the program originally known as the Systemically Significant Failing Institutions (SSFI) program. These programs were designed to mitigate the potential risks to the system as a whole from the difficulties facing these firms. (Because SSFI was used only for investments in American International Group, Inc. (AIG), such investments are now referred to as the AIG Investment Program.)

10

Similarly, the Automotive Industry Financing Program (AIFP) provided funding for General Motors Corporation (GM) and Chrysler LLC (Chrysler), as well as their financing affiliates in order to prevent a significant disruption of the automotive industry that would have posed a systemic risk to financial markets and negatively affected the real economy. Treasury-OFS' actions helped GM and Chrysler undertake massive and orderly restructurings through the bankruptcy courts that have resulted in leaner and stronger companies.

The Public-Private Investment Program (PPIP) was established to facilitate price discovery and liquidity in the markets for troubled real estate-related assets as well as the removal of such assets from the balance sheets of financial institutions. In addition to these initiatives, Treasury-OFS implemented the Consumer and Business Lending Initiative (CBLI) to enhance liquidity and restore the flow of credit to consumers and small businesses. The primary program through which the CBLI operated in 2009 was the Term Asset-Backed Securities Loan Facility (TALF). Through this combination of tools, the TARP helped strengthen a broad set of financial institutions and markets.

Details on all of these efforts, including program-specific results, can be found in Section Three [Ensuring Stability and Liquidity].

2: Prevent Avoidable Foreclosures and Preserve Homeownership

To prevent avoidable foreclosures and preserve homeownership, Treasury used authority granted under EESA to establish the Home Affordable Modification Program (HAMP) in February 2009. Other government policies have helped keep home mortgage rates at historic lows and allowed millions of Americans to refinance and stay in their homes. But because of falling housing prices, many responsible homeowners are unable to refinance. Meanwhile, job losses and reductions in working hours and benefits are making it harder for these Americans to pay their mortgages. HAMP provides incentives to mortgage servicers, investors, and homeowners to work together to reduce an eligible homeowner's monthly payments to levels that are affordable in light of the homeowner's current income. HAMP operations and program detail are provided in Section Four [Preventing Foreclosures and Preserving Homeownership].

3. *Protect Taxpayer Interests*

Government financial programs, including TARP, helped prevent the U.S. financial system from collapse, which could have resulted in a much more severe contraction in employment and production. The manner in which TARP was implemented is also designed to protect taxpayers and to compensate them for risk. For example, in exchange for capital injections, recipients of TARP funds have to adhere to corporate governance standards, limit executive pay, and provide additional reporting on lending activity. In addition, Treasury-OFS generally received preferred equity, which provides dividends. The dividend rates generally increase over time to encourage repayment.

Further, EESA stipulated that the taxpayer benefit as the institutions which received TARP funds recovered. In connection with most investments, Treasury-OFS also receives warrants for additional securities in the institutions. Under the broad programs described above, the Treasury-OFS has priority over existing shareholders of TARP recipients for which TARP holds equity investments. This gives taxpayers the ability to share in the potential upside along with existing shareholders.

Finally, the Treasury-OFS seeks to achieve the goal of protecting the taxpayer through the effective management and disposition of all TARP investments, as detailed in Section Five [Protecting Taxpayer Interests].

4: Promote Transparency

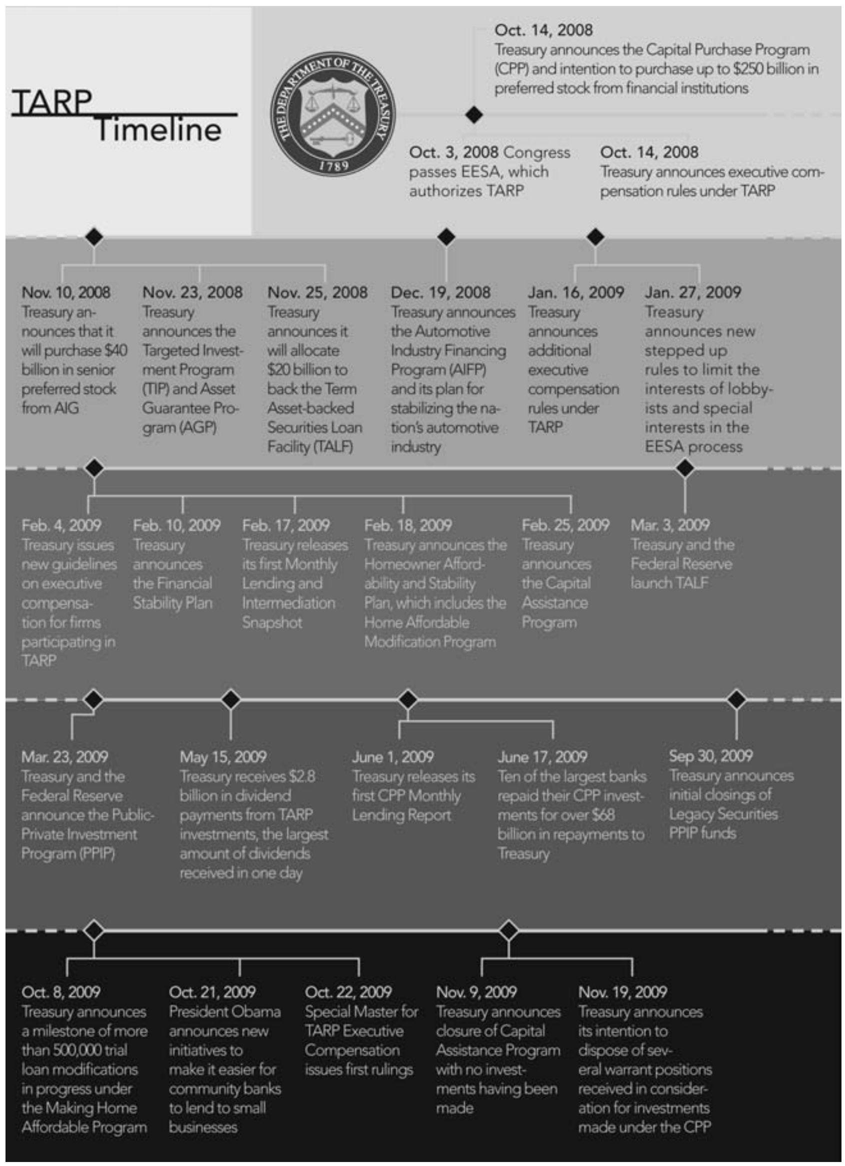
EESA requires transparency and accountability. Specifically, EESA requires Treasury-OFS to provide Congress with a variety of reports. These include a monthly report to Congress on TARP activity, a "tranche" report each time Treasury-OFS reaches a $50 billion spending threshold, and transaction reports posted within two days detailing every TARP transaction. In carrying out its operations, the Treasury-OFS has sought to not only meet the statutory requirements but also to be creative and flexible with respect to additional transparency initiatives. The Treasury-OFS proactively provides to the public monthly Dividends and Interest Reports reflecting dividends and interest paid to Treasury-OFS from TARP investments, loans, and asset guarantees, as well as monthly reports detailing the lending activity of participants in the Capital Purchase Program. All of these reports are publicly available on *www.FinancialStability.gov*.

EESA also provided for extensive oversight of the TARP, including by the Congressional Oversight Panel, the Special Inspector General for the TARP, and the Government Accountability Office. In addition, Treasury-OFS officials frequently testify before Congress on the progress of TARP programs, and Treasury-OFS staff provide briefings to Congressional staff on programmatic developments.

Further details on these efforts are provided in Section Six [Promoting Transparency].

TARP Timeline

The following timeline illustrates major events in the implementation of the TARP.


TARP Timeline
THE DEPARTMENT OF THE TREASURY 1789
Oct. 14, 2008
Treasury announces the Capital Purchase Program (CPP) and intention to purchase up to $250 billion in preferred stock from financial institutions
Oct. 3, 2008 Congress passes EESA, which authorizes TARP
Oct. 14, 2008
Treasury announces executive compensation rules under TARP
Nov. 10, 2008
Treasury announces that it will purchase $40 billion in senior preferred stock from AIG
Nov. 23, 2008
Treasury announces the Targeted Investment Program (TIP) and Asset Guarantee Program (AGP)
Nov. 25, 2008
Treasury announces it will allocate $20 billion to back the Term Asset-backed Securities Loan Facility (TALF)
Dec. 19, 2008
Treasury announces the Automotive Industry Financing Program (AIFP) and its plan for stabilizing the nation's automotive industry
Jan. 16, 2009
Treasury announces additional executive compensation rules under TARP
Jan. 27, 2009
Treasury announces new stepped up rules to limit the interests of lobbyists and special interests in the EESA process
Feb. 4, 2009
Treasury issues new guidelines on executive compensation for firms participating in TARP
Feb. 10, 2009
Treasury announces the Financial Stability Plan
Feb. 17, 2009
Treasury releases its first Monthly Lending and Intermediation Snapshot
Feb. 18, 2009
Treasury announces the Homeowner Affordability and Stability Plan, which includes the Home Affordable Modification Program
Feb. 25, 2009
Treasury announces the Capital Assistance Program
Mar. 3, 2009
Treasury and the Federal Reserve launch TALF
Mar. 23, 2009
Treasury and the Federal Reserve announce the Public-Private Investment Program (PPIP)
May 15, 2009
Treasury receives $2.8 billion in dividend payments from TARP investments, the largest amount of dividends received in one day
June 1, 2009
Treasury releases its first CPP Monthly Lending Report
June 17, 2009
Ten of the largest banks repaid their CPP investments for over $68 billion in repayments to Treasury
Sep 30, 2009
Treasury announces initial closings of Legacy Securities PPIP funds
Oct. 8, 2009
Treasury announces a milestone of more than 500,000 trial loan modifications in progress under the Making Home Affordable Program
Oct. 21, 2009
President Obama announces new initiatives to make it easier for community banks to lend to small businesses
Oct. 22, 2009
Special Master for TARP Executive Compensation issues first rulings
Nov. 9, 2009
Treasury announces closure of Capital Assistance Program with no investments having been made
Nov. 19, 2009
Treasury announces its intention to dispose of several warrant positions received in consideration for investments made under the CPP

13

FY 2009 Financial Summary for TARP

The EESA provided authority for the TARP to purchase or guarantee up to $700 billion in troubled assets.[2] Treasury-OFS used this authority to help strengthen the U.S. financial system, restore health and liquidity to credit markets to facilitate borrowing by consumers and businesses, and prevent avoidable foreclosures in the housing market. While the TARP should be evaluated primarily based on its impact on stabilizing the financial system, a critical factor in the analysis is cost. While EESA provided $700 billion in authority, the TARP has not cost taxpayers $700 billion. Treasury-OFS used the authority to make investments to stabilize the financial system and expects that much of the funding will be repaid. While some of the TARP investments are estimated to result in a cost, others are estimated to produce net income.

Treasury-OFS tracks costs in accordance with Federal budget procedure. First, amounts are allocated or budgeted to certain programs or needs within the TARP. Allocations may change over time as needs are reevaluated. Second, Treasury-OFS enters into legally binding "obligations" to invest or spend the funds. Third, funds are disbursed over time pursuant to the obligations. In any given case, it is possible that the full amount allocated will not be obligated, and that the full amount obligated will not be disbursed.

Based on operations for the period ended September 30, 2009, Treasury-OFS reports the following key results:

- Treasury-OFS entered into obligations with a face value of $454 billion in TARP authority during the fiscal year.
- In fiscal year 2009, Treasury-OFS disbursed $364 billion in TARP funds to make loans and equity investments, and reported net cost of operations of $41.6 billion.
- During fiscal year 2009, Treasury-OFS received $72.8 billion of repayments on certain investments and loans made early in FY 2009.
- At September 30, 2009, Treasury-OFS reported $240 billion for the value of loans, equity investments, and asset guarantees.

Treasury-OFS' FY 2009 net cost of operations of $41.6 billion includes the estimated net cost related to loans, equity investments, and asset guarantees. The total ultimate cost of the TARP is expected to be higher because additional investments and disbursements have been made or will be made after FY 2009. Due to its program structure, the $50 billion HAMP has delayed payments as well as a long disbursement cycle so the FY 2009 amounts include only $2 million in cost. In addition, AIG has drawn an additional $2.1 billion on its $29.8 billion equity capital facility since September 30, 2009 and may draw down the additional funds available to it, which may result in additional costs. Including these costs as well as the Public-Private

[2] The Helping Families Save Their Homes Act of 2009, Pub. L. No. 111-22, Div. A, amended the act and reduced the maximum allowable amount of outstanding troubled assets under the act by almost $1.3 billion, from $700 billion to $698.7 billion.

Investment Program and other costs is likely to significantly increase the estimated lifetime net cost for TARP. For programs where funds have been obligated but not yet disbursed, the future outlays in some cases are dependent on program subscription or other uncertain factors. In addition, new commitments may be made under TARP prior to EESA's expiration. As described further throughout this report, the valuation of the TARP investments will naturally change based on many factors.

As of September 30, 2009, Treasury-OFS currently projects that four programs will produce a net return to taxpayers. The Capital Purchase Program, the Targeted Investment Program, the Asset Guarantee Program, and the Consumer and Business Lending Initiative had reported net income of $19.5 billion. Also, as of September 30, 2009, Treasury-OFS reports that two programs -- the AIG Investment Program and the Automotive Industry Financing Program – have net costs to taxpayers of $60.9 billion. Taking into consideration the gains, the total net cost for TARP to taxpayers, based on disbursements made as of September 30, 2009, is reported as $41.4 billion. Accrued expenses for the HAMP as of September 30, 2009, of $2 million and administrative expenses for the year of $167 million bring the total estimated net costs to $41.6 billion, as shown in Table 1.

Table 1: Net Income (Cost) of TARP Operations
For the period ended September 30, 2009
$ in millions

Programs with Estimated Subsidy Income	
Capital Purchase Program	$15,033
Targeted Investment Program	$ 1,927
Asset Guarantee Program	$ 2,201
Consumer and Business Lending Initiative	$ 339
Net Income (Cost) from Programs Above	$19,500
Programs with Estimated Subsidy (Cost)	
American International Group, Inc. Investments	($30,427)
Automotive Industry Financing Program	($30,477)
Net (Cost) of Two Programs Above	($60,904)
Total Net Subsidy Income (Cost)	($41,404)
Additional TARP (Costs)	
Home Affordable Modification Program	($ 2)
Administrative Costs	($ 167)
Total Net (Costs) of TARP Operations	**($41,573)**

Over time the ultimate cost of the TARP programs may change. As described later in this MD&A, and in the Treasury-OFS audited financial statements, these estimates are based in part on currently projected economic factors. Forecasts for these economic factors will likely

15

change, either increasing or decreasing the ultimate cost of the TARP. HAMP expenses will increase significantly over time, as more modifications of mortgage payments are finalized between mortgage servicers and borrowers, resulting in increased incentive payments. These payments are described in Section Four.

Table 2 provides a financial summary for TARP programs in FY 2009. For each program, the table gives the face value of the amount obligated by each program, the amount actually disbursed during the fiscal year, repayments to Treasury-OFS during the period from program participants, net outstanding balance (the amount on the original investment that is due to be repaid to Treasury) on September 30, 2009, and cash inflows on the investments for each program in the form of dividends, interest or other fees. As of fiscal year end 2009, approximately $317 billion of the $700 billion in purchase and guarantee authority remained available, taking into account $72.8 billion in repayments. However, this does not include the full planned amounts for the HAMP, Public Private Investment Program (PPIP), Consumer and Business Lending Initiative, and other programs.

Table 2: TARP Summary[1]

As of September 30, 2009

$ in billions

	Purchase Price or Guarantee Amounts	Total $ Disbursed	Investment Repayments	Outstanding Balance	Cash Received from Investments
Capital Purchase Program	$204.6	$204.6	$70.7	$133.9	$9.7
Targeted Investment Program	$40.0	$40.0	$0.0	$40.0	$1.9
Asset Guarantee Program	$5.0	$0.0	$0.0	$0.0	$0.5
American International Group Investments[2]	$69.8	$43.2	$0.0	$43.2	$0.0
Term Asset-Backed Securities Loan Facility	$20.0	$0.1	$0.0	$0.1	$0.0
Public Private Investment Program[3]	$6.7	$0.0	$0.0	$0.0	$0.0
Automotive Industry Financing Program	$81.1	$75.9	$2.1	$73.8	$0.7
Home Affordable Modification Program[4]	$27.1	$0.0	NA	NA	$0.0
Totals	**$454.3**	**$363.8**	**$72.8**	**$291.0**	**$12.7**

1/ This table shows the TARP activity for the period ended September 30, 2009, on a cash basis. Cash received from investments includes dividends and interest income reported in the Statement of Net Cost and proceeds from repurchases of warrants and warrant preferred stock.
2/ The disbursed amount is lower than purchase price because of the $29.8 billion facility available to AIG of which only $3.2 billion was drawn at September 30, 2009. AIG drew an additional $2.1 billion from the facility on November 13, 2009.
3/ Reflects the face value of obligations incurred as of September 30, 2009. As of that date, no fund managers had made any investments and Treasury-OFS expects to provide a total of $30 billion in funding to the nine fund managers selected for PPIP.
4/ Reflects legal commitments to servicers as of September 30, 2009. Treasury-OFS has allocated $50 billion in total for the program. Payments are made to servicers once temporary modifications are made permanent.

17

Most of the TARP funds have been used to make investments in preferred stock or make loans. Treasury-OFS has generally received dividend on the preferred stock and interest payments on the loans from the institutions participating in TARP programs. These payments are a return on Treasury's TARP investments. For period ended September 30, 2009, Treasury-OFS received a total of $9.8 billion in dividends, interest and fees. Table 3 shows the breakdown of receipts for the period ended September 30, 2009 for all TARP programs combined.

Table 3: TARP FY 2009 Receipts and Repayments on Investments/Loans [1]

For the period ended September 30, 2009

($ in billions)

Dividends, Interest, Fees and Warrants Repurchases	
Dividends and Fees	$9.6
Interest	$0.2
Repurchases of Warrants and Warrant Preferred Stock	$2.9
Additional Notes	$ 0.0
Subtotal	*$12.7*
Investment/Loan Repayments	
Repurchases/Repayments on preferred stock	$70.7
Loan Principal Repaid	$2.1
Subtotal	*$72.8*
GRAND TOTAL	**$85.5**

1/ This table shows the TARP activity for the period ended September 30, 2009, on a cash basis. The table includes receipts and repayments that do not result in revenue in the Statement of Net Cost.

18

Treasury-OFS also receives warrants in connection with most of its investments, which provides an opportunity for taxpayers to realize an upside on investments. Treasury-OFS has begun to dispose of some of its warrants as institutions repay their preferred share investments. For the period ended September 30, 2009, twenty-four institutions have already repurchased their warrants which generated $2.9 billion in receipts. Table 4 provides information on the institutions that have fully repurchased the CPP preferred shares and repurchased warrants as well as those that have fully repurchased their preferred shares but not their warrants. (Treasury-OFS receives warrants for preferred stock in the case of most private institutions, which are exercised immediately. The receipts from warrants include receipts from the repayment of such preferred shares, or "warrant preferred stock".)

Table 4: Repurchases of Preferred Shares

$ in millions

Institution	Procees from Preferred Shares Redeemed	Total Dividends Received	Proceeds from Warrants Repurchased
Institutions with fully repurchased preferred shares and repurchased warrants or warrant preferred stock			
Alliance Financial Corporation	$ 26.9	$ 0.5	$ 0.9
American Express Company	$ 3,388.9	$ 74.4	$ 340.0
Bancorp Rhode Island, Inc.	$ 30.0	$ 0.9	$ 1.4
Bank of New York Mellon	$ 3,000.0	$ 95.4	$ 136.0
BB&T Corp.	$ 3,133.6	$ 92.7	$ 67.0
Berkshire Hills Bancorp, Inc.	$ 40.0	$ 0.9	$ 1.0
Centra Financial Holdings, Inc.	$ 15.0	$ 0.2	$ 0.8
First Manitowoc Bancorp, Inc.	$ 12.0	$ 0.2	$ 0.6
First Niagara Financial Group	$ 184.0	$ 4.8	$ 2.7
First ULB Corp.	$ 4.9	$ 0.1	$ 0.2
FirstMerit Corporation	$ 125.0	$ 1.8	$ 5.0
Goldman Sachs Group, Inc.	$ 10,000.0	$ 318.1	$ 1,100.0
HF Financial Corp.	$ 25.0	$ 0.7	$ 0.7
IberiaBank Corporation	$ 90.0	$ 1.5	$ 1.2
Independent Bank Corp.	$ 78.2	$ 1.1	$ 2.2
Morgan Stanley	$ 10,000.0	$ 318.1	$ 950.0
Northern Trust Corporation	$ 1,576.0	$ 46.6	$ 87.0
Old Line Bancshares, Inc.	$ 7.0	$ 0.2	$ 0.2
Old National Bancorp	$ 100.0	$ 1.5	$ 1.2
SCBT Financial Corporation	$ 64.8	$ 1.1	$ 1.4

19

Somerset Hills Bancorp	$ 7.4	$ 0.1	$ 0.3
State Street Corporation	$ 2,000.0	$ 63.6	$ 60.0
Sun Bancorp, Inc.	$ 89.3	$ 1.1	$ 2.1
U.S. Bancorp	$ 6,599.0	$ 195.2	$ 139.0
Subtotal	$ 40,597.0	$ 1,220.7	$ 2,900.9
Institutions with fully repurchased preferred shares but warrants are outstanding			
Bank of Marin Bancorp	$ 28.0	$ 0.5	$ -
Capital One Financial Corp	$ 3,555.2	$ 105.2	$ -
Centerstate Banks of Florida Inc.	$ 27.9	$ 1.2	$ -
CVB Financial Corp.	$ 130.0	$ 4.7	$ -
F.N.B. Corporation	$ 100.0	$ 3.3	$ -
First Community Bancshares Inc.	$ 41.5	$ 1.3	$ -
JPMorgan Chase & Co.	$ 25,000.0	$ 795.1	$ -
Manhattan Bancorp	$ 1.7	$ 0.1	$ -
Shore Bancshares, Inc.	$ 25.0	$ 0.3	$ -
Signature Bank	$ 120.0	$ 1.8	$ -
Sterling Bancshares, Inc.	$ 125.2	$ 2.5	$ -
TCF Financial Corporation	$ 361.2	$ 7.9	$ -
Texas Capital Bancshares, Inc.	$ 75.0	$ 1.2	$ -
Washington Federal S and L Association	$ 200.0	$ 5.4	$ -
Wesbanco, Inc.	$ 75.0	$ 2.9	$ -
Subtotal	$ 29,865.6	$ 933.4	$ -
Institutions making partial repurchases of preferred shares and outstanding warrants			
State Bankshares, Inc.	$ 12.5	$ 1.6	$ -
Valley National Bancorp	$ 200.0	$ 11.2	$ -
Westamerica Bancorporation	$ 41.9	$ 2.2	$ -
Subtotal	$ 254.4	$ 15.0	$ -
Total	**$ 70,717.0**	**$ 2,169.1**	**$ 2,900.9**

The ultimate cost of the TARP will not be known for some time. The financial performance of the programs will depend on many factors such as future economic and financial conditions, and the business prospects of specific institutions. Table 5 provides information on the estimated values of the TARP investments by program, as of the end of FY 2009. (HAMP is excluded from the chart because no repayments are required). The estimates in Table 5 are based on assumptions regarding future events, which are inherently uncertain. The estimates are sensitive to a number of factors, including changes in general economic conditions, specific stock price volatility of the entities in which Treasury-OFS has an equity interest, estimates of expected defaults, and prepayments. If Treasury-OFS experiences higher than currently projected early repayments, TARP's ultimate cost will decline further. Sections Seven and Eight of this report describe the methods used to determine the estimates.

20

In Table 5 below, the Outstanding Balance column represents the amounts paid by Treasury-OFS to acquire the loans and equity investments that were outstanding as of fiscal year end. The Estimated Value of Investment column represents the present value of net cash inflows that Treasury-OFS estimates it will receive from the loans and equity investments. For equity securities, this amount represents fair value. The total difference of $53.1 billion between the two columns is considered the "subsidy cost allowance" under the Federal Credit Reform Act methods Treasury-OFS follows for budget and accounting purposes (see Section Seven for further discussion).[3]

Table 5: Summary of TARP Investments
$ in billions

Program	Outstanding Balance [1]	Estimated Value of Investment 9/30/09
Capital Purchase Program	$133.9	$141.7
Targeted Investment Program	$40.0	$40.3
AIG Investment Program	$43.2	$13.2
Automotive Industry Financing Program	$73.8	$42.3
Term Asset-Backed Securities Loan Facility	$0.1	$0.4
Total	$291.0	$237.9

[1] Before subsidy cost allowance.

[3] To reconcile the subsidy cost allowance to the total subsidy cost amount of $41.4 billion shown in Table 1 and on the Statement of Net Cost, the $53.1 billion is adjusted by intragovernmental interest cost, the net present value of the Asset Guarantee Program, and certain inflows from the loans and equity investments (e.g., dividends, interest, proceeds from repurchase of warrants by financial institutions, and other realized fees).

21

Table 6 below shows the estimated net asset value for the top ten CPP investments held as of September 30, 2009. The estimates shown below include only estimates of the value of the preferred stock for each institution. Treasury-OFS also holds warrants for each institution and those warrants have additional value. As the Treasury-OFS will still need to negotiate a sale price for the warrants, the estimated warrant value of each institution cannot be disclosed without harming Treasury-OFS' ability to secure the best return for taxpayers. Through an exchange process, Treasury-OFS received common shares at $3.25 per share for the originally issued preferred shares in Citigroup which had an initial investment of $25 billion. The holdings of Citigroup common shares had a market value of $37.23 billion ($4.84 per share) as of September 30, 2009.

Table 6: Top Ten CPP Investments
($ in billions)

Institution	Original Investment	Estimated Net Asset Value (excluding warrants) as of 9/30/09
Citigroup (Common Shares)	$ 25.00	$ 37.23
Bank of America	$ 25.00	$ 22.45
Wells Fargo	$ 25.00	$ 23.47
PNC Financial	$ 7.58	$ 7.17
SunTrust Bank	$ 4.85	$ 4.14
Regions Bank	$ 3.50	$ 3.01
Fifth Third Bancorp	$ 3.41	$ 3.05
Hartford Financial	$ 3.40	$ 3.11
Keycorp	$ 2.50	$ 1.94
CIT Group	$ 2.33	$ 0
Total	**$102.57**	**$105.57**

[1] Does not reflect the impact of management's expectation of an additional $30 billion in early repayments.

Market conditions and the performance of specific financial institutions will be critical determinants of the TARP's final cost. The changes in the Treasury-OFS estimates during the period ended September 30, 2009 provide a good illustration of this impact. The estimated net cost of programs implemented to date declined by approximately $110 billion as compared to the estimates made while the programs were being initiated in the heart of the financial market crisis last winter in large part due to market stabilization seen to date and actual and forecast repayments occurring at a faster rate than originally anticipated. In the CPP program for example, when the cost of the program was first estimated by the Congressional Budget Office and Treasury-OFS last winter, the expectation was that the program would lose about 18-22 percent.[4] In large part because of the improved market conditions, Treasury-OFS reported net income of about $15.0 billion for the period ended September 30, 2009. Based on the repayments to date and current market conditions, the major bank stabilization programs, including the CPP and the TIP, are currently estimated to provide a net financial return to the taxpayer. The outstanding $174 billion in CPP and TIP balances are estimated to be worth approximately $182 billion. However, the outlook for repayments from the auto industry investments and the AIG Investment Program is less positive. Treasury-OFS estimates the $117 billion originally invested in these programs is currently valued at approximately $56 billion. These programs may result in a net financial loss to taxpayers.

Table 7 provides information as to how the estimated cost of the TARP has changed during for the period ended September 30, 2009. The positive amounts reflect an estimated income whereas negative amounts reflect a cost or expense. For example, the $204.6 billion invested in the CPP program was originally expected to cost about $57 billion (in net present value cost). For the period ended September 30, 2009, Treasury-OFS reported net income of about $15 billion for CPP. This amount represents primarily the combination of actual dividends, interest and realized fees, and the excess of estimated fair value as of September 30, 2009 of the CPP investments over original cost. Additional explanatory material on how these estimates were developed can be found in Sections Seven [Financial Accounting Policy] and Eight [TARP Valuation Methodology].

[4] "The Troubled Asset Relief Program: Report on Transactions Through December 31, 2008." Congressional Budget Office. January 2009.

Table 7: Estimated Change in Net Cost for the TARP Programs $ in billions			
	Original Estimate[1]	Current Estimate	Net Change
Capital Purchase Program	- 57.4	+ 15.0	+ 72.4
Targeted Investment Program	- 19.6	+ 1.9	+ 21.5
Asset Guarantee Program	+ 1.0	+ 2.2	+ 1.2
AIG Investment Program	- 31.5	- 30.4	+ 1.1
Automotive Industry Financing Program	- 43.7	- 30.4	+ 13.3
Term Asset-Backed Securities Loan Facility	+ 0.1	+ 0.3	+ 0.2
Subtotal	- 151.1	- 41.4	+ 109.7
Home Affordable Modification Program	- 27.1	- 27.1	0.0
Total	- 178.2	- 68.5	+ 109.7

[1] Original estimates completed on or near the initiation of each program and adjusted for modifications. Amounts shown in both original and current estimates are based on the same total program disbursements through FY 2009.

The Impact of TARP

Measuring the impact of the TARP in isolation is challenging. The health of the overall system and its impact on the U.S. economy are the most important metrics by which Treasury-OFS can measure the effectiveness of these policies. However, the cost of the financial system collapse that was likely averted by TARP and the other government actions taken in the fall of 2008 and since then will never be known. Moreover, it is difficult to measure separately the impact of TARP as it was part of a coordinated government response to restore confidence in our financial system. A few TARP programs were uniquely targeted to specific markets and institutions. In those instances, Treasury-OFS can measure performance more directly.

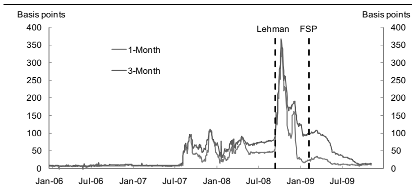
Confidence in the stability of our financial markets and institutions has improved dramatically. Interbank lending rates, which reflect stress in the banking system, have returned to levels associated with more stable times. For example, the spread of one-month Libor to the overnight index swap fell from a peak of about 340 basis points[5] last fall to roughly 10 basis points at the end of October 2009, as shown in Figure 1. Credit-default swap spreads for financial institutions, which measure investor confidence in their health, have also fallen significantly. A measure of credit-default swaps for the largest U.S. banks reached 450 basis

[5] A basis point is one hundredth of a percentage point or 0.01 percent so 100 basis points equals 1 percent. Basis points are often used to measure small changes in interest rates or yields on financial instruments.

24

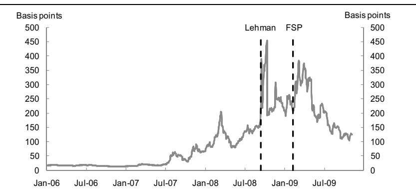
points last fall as shown in Figure 2, and just over 100 basis points today. The TARP was a necessary step, but not the only step, to achieving this recovery.

Figure 1. Libor-OIS Spread (basis points)



Source: Bloomberg

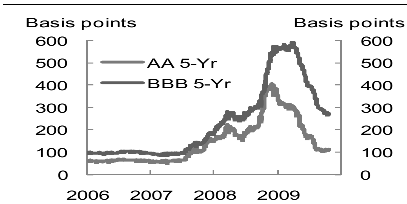
Figure 2. Credit Default Spreads for Financial Institutions (basis points)



Sources: Bloomberg.
Notes: Includes Bank of America, Citigroup, Goldman Sachs, JPMorgan, Morgan Stanley, and Wells Fargo.

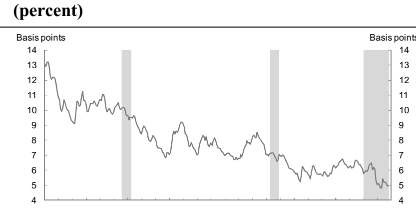
At the same time, borrowing costs have declined for many businesses, homeowners, and municipalities. Investment-grade corporate bond rates have fallen by over 70 percent since last fall, and high-yield bond rates have fallen by more than half. Fears of default on these bonds have receded, providing further relief on prices. The CDX investment-grade index (see Figure 3), an aggregate measure of credit-default swaps for highly-rated companies, has fallen about 35 percent from its October 2008 peak. Further, conventional 30-year mortgage rates (see Figure 4) remain under five percent at historic lows. AAA municipal bond rates are three percent, down from five percent last fall.

Figure 3. Corporate Bond Spreads (basis points)



Source: Bloomberg

Figure 4. Conventional 30-Year Mortgage Rate (percent)



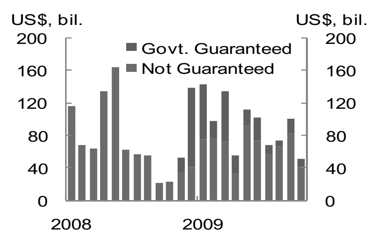
Source: Federal Reserve

As borrowing costs have come down, businesses have raised about $900 billion in investment-grade debt and over $100 billion in high-yield debt this year. While much of the new issuance early this year was supported by the federal government, private investors have funded

25

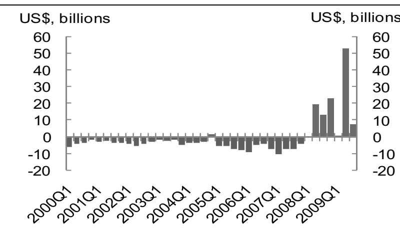
most new corporate debt in recent months. In particular, banks have raised substantial capital from private sources following the release of the results from the federal government "stress test" of major U.S. financial institutions. Since the results were released, banks have raised $80 billion in new common equity and over $40 billion in debt that is not guaranteed by the federal government.

Figure 5. Corporate Bond Issuance (US$ billions)



Source: JPMorgan

Figure 6. Net Common Issuance by U.S. Banks (US$, billions)

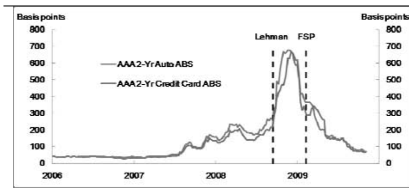


Source: SNL Financial.
Notes: Excludes equity generated through asset sales and preferred conversions. Negative figures represent net repurchases of equity.

Securitization markets that provide important channels of credit for consumers and small businesses have also improved, in large part because of programs launched under the TARP. Announcements about TALF helped narrow spreads in these markets even before the program began operating. This trend has continued, with spreads on TALF-eligible asset-backed securities (ABS) back to pre-crisis levels today, and spreads on non-TALF-eligible ABS more than 90 percent off their peaks from last fall. Issuance of ABS backed by consumer and business loans has averaged $14 billion per month since the government launched TALF in March 2009, compared to about $1.6 billion per month in the six months prior to the program's launch. Issuance not supported by the federal government program accounted for about 40 percent of all such issuance in October 2009. However, the overall size of securitization markets remains small, relative to pre-crisis levels.

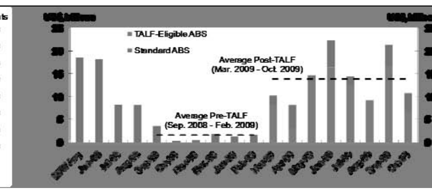
26

Figure 7. Spreads Between TALF-Eligible ABS and Treasury Securities (basis points)



Source: JPMorgan

Figure 8. Issuance of ABS Backed by Consumer and Small Business Loans (US$, billions)



Source: Federal Reserve

Legacy security prices have improved significantly this year. This is due in part to general market improvement and in part to announcements for the Securities PPIP. Most of the Public-Private Investment Funds (PPIFs) have now been formed and are starting to purchase legacy assets from banks. The PPIFs should continue to contribute to price improvements in these markets.

Stock markets have recovered substantial ground since March, following 18 months of steep declines. The S&P 500 has risen over 60 percent over the past six months, and share prices for financial companies in the S&P 500 have doubled. At the same time, volatility in stock markets is trending lower and approaching historical norms. The implied volatility of the S&P 500, as measured by the Chicago Board Options Exchange's Market Volatility (VIX), has fallen by over 70 percent since its peak in October and is roughly at its average since 1990. These improvements reflect broad-based confidence not only in the financial system, but also the prospects for economic recovery.

Indeed, the American economy is growing again. It expanded at an annual rate of 2.8 percent in the third quarter of 2009, snapping four consecutive quarters of negative growth. And private economists generally expect moderate growth over the next year.

Meanwhile, housing markets are showing some signs of stabilizing and household wealth is recovering, which should stimulate consumer spending -- vital to American economic growth. Thanks in part to federal government financial policies, mortgage rates remain near historic lows. Home prices have ticked up over the past six months, after showing consistent declines since 2006. For example, the seasonally adjusted S&P/Case-Shiller U.S. National Home Price Index rose by 1.8 percent and 1.9 percent in the second and third quarters, respectively. Since March, sales of existing single-family homes have increased by 20 percent and over 2.7 million mortgages have been refinanced. Since Treasury-OFS announced its Making Home Affordable program, over 650,000 trial modifications under HAMP have been initiated, with roughly a few

27

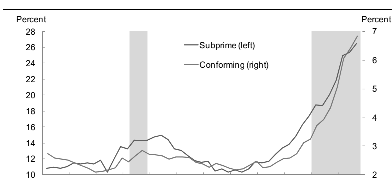
hundred completing the trial period by September 30, 2009. Household net worth increased by $2 trillion in the second quarter, the first increase since the third quarter of 2007.

However, the financial and economic recovery faces significant headwinds. Although the unemployment rate fell in November, it remains high at 10 percent. This places enormous pressure on homeowners and American families. Indeed, delinquencies of subprime residential mortgages reached over 26 percent and conforming mortgages nearly seven percent in the third quarter, as illustrated in Figure 9. And although RealtyTrac's October report shows a third straight month of decreasing foreclosure activity, foreclosures are still up nearly 19 percent since October 2008. Moreover, according to First American CoreLogic, roughly one in four homeowners owed more on their mortgages than the properties were worth in the third quarter of 2009.

Bank lending also continues to contract, as shown in Figure 10. In the third quarter, commercial and industrial (C&I) loans outstanding contracted at an annual rate of 27 percent, and commercial real estate (CRE) loans outstanding at 8 percent. Small businesses rely on banks for 90 percent of their financing. Unlike large corporations, few can substitute credit from securities issuances.

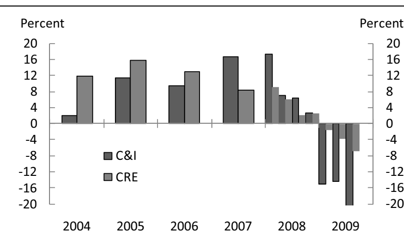
The contraction in bank lending reflects a combination of weak demand for credit and tightening standards at the banks. The former is a function of the recession preceded by a period of over expansion. The latter is in part a function of the fact that many banks face continued losses on outstanding exposures, in particular in commercial real estate. FDIC-insured commercial banks reported that net charge-offs—that is, losses that have occurred—increased to 2.9 percent as a share of loans and leases in the third quarter, up from 0.6 percent before the recession. And delinquencies of commercial real estate loans were nine percent in the third quarter and increasing.

Figure 9. Mortgage Delinquencies (percent)



Source: Mortgage Bankers Association

Figure 10. Bank Loans, C&I and CRE (percent change, end of period)



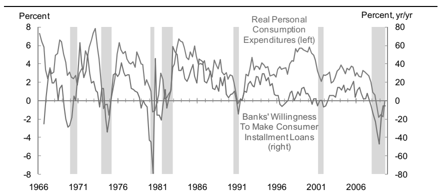
Source: Federal Reserve

28

Bank failures and the number of problem banks continue to increase. There have been over 120 bank failures this year through November 20, 2009, compared with 41 over the decade that preceded the current recession. And the number of banks that the FDIC classifies as "problem institutions" has reached 552 this year, compared with 76 in 2007 and 252 in 2008.

Banks' willingness to lend also has a significant impact on consumer spending and, consequently, economic growth. Macroeconomic Advisors, a consulting firm, found that a 10-point increase in bank's willingness to make consumer installment loans yields a 0.3 percentage point increase in personal consumption expenditures.[6] Figure 11 illustrates this relationship between bank lending attitudes and consumer spending.

Figure 11. Banks' Willingness to Lend and Personal Consumption Expenditures (percent)



Source: Federal Reserve, BEA

In this context, some federal government financial support is still necessary. In particular, the TARP can help stimulate credit for small businesses and assist responsible homeowners in avoiding foreclosures. As discussed in more detail below, Treasury-OFS is redirecting the TARP to meet these needs. Treasury-OFS recently launched initiatives to provide capital to small and community banks, which are important sources of credit for small businesses. Treasury-OFS is also working with the Small Business Administration, Congress, and the small business community to design other programs that will use TARP funds to get credit flowing again to these important engines of economic growth.

External Assessments of TARP Performance

The United States Government Accountability Office (GAO) is one of four oversight bodies explicitly designated by Congress to provide oversight of the TARP. GAO's October 2009 anniversary report on the TARP provides a comprehensive and independent assessment of various aspects of the TARP.[7] The GAO also acknowledges that isolating and estimating the effect of TARP programs is challenging and that improvements in credit markets cannot be attributed solely to TARP programs. The indicators that the GAO has monitored over the past year suggest that there have been broad improvements in credit markets since the announcement of CPP, the first TARP program. The GAO notes, specifically, that:

[6] Macroeconomic Advisers, "Banks' Willingness to Lend and PCE Growth," Oct. 8, 2008.

[7] Troubled Asset Relief Program: One Year Later, Actions Are Needed to Address Remaining Transparency and Accountability Challenges. Government Accountability Office. GAO-10-16. October 8, 2009.

29

- the cost of credit and perceptions of risk declined significantly in interbank, corporate debt, and mortgage markets;
- the decline in perceptions of risk (as measured by premiums over Treasury securities) in the interbank market could be attributed in part to several federal programs aimed at stabilizing markets that were announced on October 14, 2008, including CPP; and
- the institutions that received CPP funds in the first quarter of 2009 saw more improvement in their capital positions than banks outside the program.

Additional information on the assessments and activities of the TARP oversight entities can be found in Section Nine [Systems, Controls, and Legal Compliance].

Section Three: Ensuring Stability and Liquidity

This section provides a description of each of the programs established under the TARP to ensure stability and liquidity, including results for each program to date.

Capital Purchase Program

EESA was originally proposed as a means to buy mortgage loans, mortgage-backed securities and certain other assets from banks. However, the authorities granted under EESA were broadened in the legislative process to cover any financial instrument whose purchase the Secretary of the Treasury, after consultation with the Chairman of the Federal Reserve, determines necessary to promote financial market stability. Shortly following passage of EESA, it became clear to the leaders of many G-7 nations that rapid action was needed to provide capital to the financial system as a whole. Lending even between banks had practically stopped, credit markets had shut down, and many financial institutions were facing severe stress. There was not sufficient time to implement a program to buy mortgage related assets, which posed difficulties related to valuing such assets and getting the holders of such assets to sell them at current prices. In this context, immediate capital injections into financial institutions were a necessary step to avert a potential collapse of the system.

Given the high level of uncertainty in financial markets and the economy, even strong financial institutions began to hoard capital. Based on various market indicators, it became clear that financial institutions needed additional capital to sustain a normal flow of credit to businesses and consumers during the financial turmoil and economic downturn. As a result, Treasury-OFS launched the Capital Purchase Program (CPP), its largest and most significant program under EESA, on October 14, 2008. Treasury-OFS initially committed over a third of the total TARP funding, $250 billion, to the CPP, which it lowered to $218 billion in March 2009.

The CPP was designed to bolster the capital position of viable institutions and, in doing so, to build confidence in these institutions and the financial system as a whole. With the additional capital, CPP participants were better equipped to undertake new lending, even while absorbing write downs and charge-offs on loans that were not performing.

Of the $250 billion commitment, Treasury-OFS invested $125 billion in eight of the country's largest financial institutions. The remaining $125 billion was made available to qualifying financial institutions (QFIs) of all sizes and types across the country, including banks, savings associations, bank holding companies and savings and loan holding companies. QFIs interested in participating in the program had to submit an application to their primary federal banking regulator. The minimum subscription amount available to a participating institution was

1 percent of risk-weighted assets. The maximum subscription amount was the lesser of $25 billion or 3 percent of risk-weighted assets.

Over the weeks and months that followed the announcement of the CPP, Treasury-OFS provided capital to 685 institutions in 48 states, including more than 300 small and community banks, helping to enable them to absorb losses from bad assets while continuing to lend to consumers and businesses. The largest investment was $25 billion while the smallest was $301,000. To encourage continued participation by small and community banks, the application window for CPP was reopened on May 13, 2009, for banks with less than $500 million in assets, with an application deadline of November 21, 2009.

Most banks participating in the CPP are to pay Treasury-OFS a dividend rate of 5 percent per year, increasing to 9 percent a year after the first five years. In the case of S-corporations, Treasury-OFS acquires subordinated debentures. Treasury-OFS has received $6.8 billion in CPP dividend and interest payments for the period ended September 30, 2009. As of September 30, 2009, 38 institutions had not paid full dividends or interest payments. Under the CPP, Treasury-OFS has a right to elect two directors to the board of directors of an institution that misses six or more dividend payments.

One measure of the CPP's performance is the effect on lending by CPP participants. Lending typically falls during a recession, and the current cycle is no exception. The Federal Reserve Board's recent article *U.S. Credit Cycles: Past and Present* examines how credit volumes have evolved in the current economic downturn relative to previous business cycle downturns using the Federal Reserve's Flow of Funds data.[8] Significant among the Federal Reserve's findings is that despite many unprecedented aspects of the current financial and economic turbulence, movements in credit volumes in the current recession are similar to historical patterns. In terms of looking more specifically at CPP bank lending, each month Treasury-OFS asks CPP participants to provide information about their lending activity. As illustrated by Treasury-OFS' Lending and Intermediation Survey, the 22 largest CPP participants have been able to sustain their lending activities during this crisis, despite the significant headwinds posed by the recession, including increased bankruptcies, higher unemployment and falling home prices. Details on the Bank Lending Surveys can be found at http://www.financialstability.gov/impact/surveys.htm.

[8] The article "U.S. Credit Cycles: Past and Present" can be found at the following link: http://www.financialstability.gov/docs/CPP/Report/Fed%20US%20Credit%20Cycles%20072409.pdf.

Capital Assistance Program and the Supervisory Capital Assessment Program

In early 2009, the Federal banking agencies conducted a one-time, forward-looking assessment or "stress test" -- known as the Supervisory Capital Assessment Program (SCAP) -- on the nineteen largest U.S. bank holding companies (BHCs). The stress test assessed whether these BHCs had the capital to continue lending and absorb all potential losses resulting from a more severe decline in economic conditions than projected by economic forecasters. After completion of the SCAP, the banking agencies concluded that ten of these BHCs needed to raise a total of an additional $75 billion in capital to establish a buffer for more adverse conditions. The remaining nine BHCs were found to have sufficient capital to weather more adverse market conditions.

In conjunction with this forward-looking test, Treasury-OFS announced that it would provide capital through the Capital Assistance Program (CAP) to banks that needed additional capital but were unable to raise it through private sources. The capital provided by the CAP would take the form of convertible preferred stock. This program was made available to all QFIs, not solely to those banks that underwent the SCAP.

The design of the tests and their results were made public, a highly unusual step that was taken because of the unprecedented need to reduce uncertainty and restore confidence. By identifying and quantifying potential capital shortfalls and requiring that additional capital be raised to eliminate any deficiencies, the SCAP ensured that these financial institutions would have sufficient capital to sustain their role as intermediaries and continue to provide loans to creditworthy borrowers even if economic conditions suffered a severe and extended deterioration.

Of the ten bank holding companies that were identified as needing to raise more capital, nine have met or exceeded the capital raising requirements through private efforts. In the aggregate, these firms have increased requisite capital by over $77 billion since the results of the SCAP were announced. Treasury-OFS may provide additional capital to GMAC under the Auto Industry Financing Program to assist its fundraising efforts to meet the requirements of the SCAP.

Since the stress test results were released in early May, banks of all sizes have raised over $80 billion in common equity and $40 billion in debt that is not guaranteed by the government. Importantly, that capital raising has enabled more than 40 banks to repay the TARP investments made by Treasury-OFS. Treasury-OFS has received over $70 billion in principal repayments, and $9.7 billion in dividends, interest, warrants, and fees from CPP participants. In addition, Treasury-OFS estimates that another $70 billion in repayments from all TARP investments will occur over the next 12 to 18 months. Another measure of the effectiveness of SCAP and the

CPP, as well as other government efforts, is that Treasury-OFS did not receive any applications for CAP which terminated on November 9, 2009.

Targeted Investment Program

Treasury-OFS established the Targeted Investment Program (TIP) under the TARP in December 2008. The TIP gave the Treasury-OFS the necessary flexibility to provide additional or new funding to financial institutions that were critical to the functioning of the financial system. Through TIP, Treasury-OFS sought to prevent a loss of confidence in critical financial institutions, which could result in significant financial market disruptions, threaten the financial strength of similarly situated financial institutions, impair broader financial markets, and undermine the overall economy.

Eligibility to participate in the TIP was determined on a case-by-case basis, depending on a number of factors. Treasury-OFS considered, among other things:

- The extent to which the failure of an institution could threaten the viability of its creditors and counterparties because of their direct exposures to the institution;

- The number and size of financial institutions that are perceived or known by investors or counterparties as similarly situated to the failing institution, or that would otherwise be likely to experience indirect contagion effects from the failure of the institution;

- Whether the institution is sufficiently important to the nation's financial and economic system that a disorderly failure would, with a high probability, cause major disruptions to credit markets or payments and settlement systems, seriously destabilize key asset prices, or significantly increase uncertainty or loss of confidence, thereby materially weakening overall economic performance; and

- The extent and probability of the institution's ability to access alternative sources of capital and liquidity, whether from the private sector or other sources of government funds.

Treasury-OFS invested $20 billion in each of Bank of America (BofA) and Citigroup under the TIP. These investments provide for annual dividends of 8 percent. These investments also impose greater reporting requirements and harsher restrictions on the companies than under the CPP terms, including restricting dividends to $0.01 per share per quarter, restrictions on executive compensation, restrictions on corporate expenses, and other measures. Assistance under the TIP is also considered "exceptional assistance", which means that the recipient is also subject to greater restrictions under the executive compensation rules.

American International Group, Inc. (AIG) Investment Program

Since September 2008, the Federal Reserve and Treasury-OFS have taken a series of actions related to AIG in order to prevent AIG's disorderly failure and mitigate systemic risks. These actions addressed the liquidity and capital needs of AIG, helping to stabilize the company. Treasury-OFS provided this assistance by purchasing preferred shares in AIG and also received warrants to purchase common shares in the institution. The assistance provided to AIG was deemed "exceptional assistance" which means that the recipient is subject to greater restrictions under the rules relating to executive compensation. Further details on the AIG Investment Program can be found in the AIG box.

AIG

In September 2008, prior to the passage of EESA, AIG faced severe liquidity pressures and potential insolvency. These pressures grew acute the day after the bankruptcy filing of Lehman Brothers, as financial and credit markets ceased to function. Treasury and Federal Reserve officials feared that a disorderly failure of the company at that time posed a systemic risk to the financial system and the U.S. economy. The company had global operations and was a significant participant in many financial markets. Through its subsidiaries, the company provided insurance protection to more than 100,000 entities, including small businesses, municipalities, 401(k) plans, and Fortune 500 companies who together employ over 100 million Americans. The company was also a significant counterparty to a number of major financial institutions. These commitments were reflected in tens of thousands of contracts that touched millions of Americans and businesses.

The complexity of these insurance contracts and the exposure of the financial system and economy to their default required government intervention. The Federal Reserve provided an $85 billion credit facility in the form of secured loans to AIG on September 16, 2008 to contain the financial panic at least cost to the American taxpayer. At the time, the government was constrained by the tools at its disposal. The Federal Reserve was not in a position to selectively impose haircuts on AIG counterparties, or to know the long-term costs of its liquidity provision. Time was of the essence and the Federal Reserve faced a binary choice: allow AIG to default on tens of thousands of contracts, further eroding confidence in U.S. financial institutions and perpetuating market freezes, or provide secured credit to allow AIG to meet its near-term contractual obligations with millions of insurance holders. The Federal Reserve chose the latter option, and, along with Treasury, has managed its investment in AIG to facilitate an orderly restructuring of the company and to maximize repayments to taxpayers.

In November 2008, this assistance was restructured so that the company had more equity and less debt. Treasury-OFS purchased $40 billion in cumulative preferred stock from AIG under the TARP, the proceeds of which were used to repay the Federal Reserve loan in part. In April 2009, Treasury-OFS exchanged the $40 billion in cumulative preferred stock for $41.6 billion in non-cumulative preferred stock and created an equity capital facility, under which AIG may draw up to $29.8 billion as needed in exchange for issuing additional preferred stock to Treasury-OFS. As of September 30, 2009, AIG had drawn approximately $3.2 billion from the facility. The preferred stock pays a noncumulative dividend, if declared, of 10 percent per annum. The Federal Reserve Bank of New York (FRBNY) has also provided additional assistance to AIG by funding special purpose entities which purchased certain derivative contracts from AIG. In connection with its assistance to AIG, the FRBNY received convertible preferred stock representing approximately 79.8 percent of the fully diluted voting power of the AIG common stock.

The preferred stock was deposited in a trust, which exists for the benefit of the U.S. taxpayers. The FRBNY has appointed three independent trustees who have the power to vote the stock and dispose of the stock with prior approval of FRBNY and after consultation with Treasury. The trust agreement provides that the trustees cannot be employees of Treasury or the FRBNY. The Department of the Treasury does not control the trust and cannot direct the trustees. Treasury-OFS, through its TARP investment, owns other preferred stock that is not held in the trust and does not have voting rights except in certain limited circumstances.

Asset Guarantee Program

Pursuant to section 102 of EESA, Treasury-OFS established the Asset Guarantee Program (AGP) with the same objective as the TIP of preserving financial market stability. The AGP, like the TIP, is a targeted program aimed at maintaining the stability of systemically important financial institutions and, thereby, reducing the potential for problems at such an institution to "spillover" to the broader financial system and economy. More specifically, the AGP may be used to provide protection against the risk of significant loss in a pool of assets held by a systemically significant financial institution that faces a risk of losing market confidence due in large part to its holdings of distressed or illiquid assets. By helping limit the institution's exposure to losses on illiquid or distressed assets, the AGP can help the institution maintain the confidence of its depositors and other funding sources and continue to meet the credit needs of households and businesses.

The AGP has been applied with extreme discretion and Treasury-OFS does not anticipate wider use of this program. To date, Treasury-OFS has used this program to assist Citigroup and began negotiations with Bank of America (BofA) under the AGP which BofA subsequently terminated. Further details on this assistance can be found in the BofA and Citigroup separate presentations.

Bank of America

Under the CPP, in October 2008, Treasury-OFS agreed to purchase $15 billion of preferred stock from Bank of America and $10 billion from Merrill Lynch. When Bank of America completed its acquisition of Merrill Lynch at the end of 2008, the Treasury-OFS held a total of $25 billion of preferred in Bank of America. This preferred stock has a dividend rate of 5 percent per annum for the first five years and increases to 9 percent thereafter. Under the TIP, Treasury-OFS purchased an additional $20 billion in preferred stock from Bank of America in January 2009, which pays a dividend of 8 percent per annum. Treasury-OFS also received warrants in both transactions.

In January 2009, Treasury-OFS, the Federal Reserve and the FDIC entered into a term sheet for a potential loss sharing arrangement under the AGP on a $118 billion pool of financial instruments owned by Bank of America. In May 2009, Bank of America announced its intention to terminate negotiations with respect to the loss-sharing arrangement and in September 2009, Treasury, the Federal Reserve, the FDIC and Bank of America entered into a termination agreement pursuant to which (i) the parties terminated the related term sheet and (ii) Bank of America agreed to pay a termination fee of $425 million to the government parties, with $276 million going to Treasury-OFS. The fee compensated the government parties for the value that Bank of America had received from the announcement of the negotiations with government parties to guarantee and share losses on the pool of assets from and after the date of the term sheet. The termination fee was determined by taking the fee that would have been payable had the guarantee been finalized.

Citigroup

Under the CPP, Treasury-OFS purchased $25 billion in preferred stock from Citigroup in October 2008. This preferred stock had a dividend rate of 5 percent per annum. Under the TIP, Treasury-OFS purchased $20 billion in additional preferred stock from Citigroup, Inc. in December 2008. That preferred stock had a dividend rate of 8 percent per annum. Treasury-OFS also received warrants in both transactions. As part of an exchange offer designed to strengthen Citigroup's capital, Treasury-OFS recently exchanged all of its preferred stock in Citigroup for a combination of common stock and trust preferred securities.

In January 2009, Treasury-OFS and Citigroup entered into an agreement for Citigroup's participation in the AGP. Treasury-OFS guaranteed up to $5 billion of potential losses incurred on a $301 billion pool of loans, mortgage-backed securities, and other financial assets held by Citigroup. The Federal Reserve and the FDIC are also parties to this arrangement. Treasury-OFS will not become obligated to pay on its guarantee unless and until Citigroup has absorbed $39.5 billion of losses on the covered pool. Treasury-OFS would then cover 90 percent of all losses on the covered pool, up to a maximum of $5 billion. In consideration for the guarantee, Treasury-OFS received $4.03 billion in preferred stock that pays an annual dividend of 8 percent. Treasury-OFS also received a warrant to purchase approximately 66 million shares of common stock at a strike price of $10.61 per share.

As part of the exchange offer noted above, Treasury-OFS exchanged preferred stock received under the AGP for an equivalent amount of trust preferred securities paying interest at the same rate.

Consumer and Business Lending Initiative

Treasury-OFS designed two initiatives to restore consumer and business lending in the period ended September 30, 2009, the Term Asset-Backed Securities Loan Facility (TALF) and the Unlocking Credit for Small Business Initiative. Both programs are discussed in more detail below.

1. *Term Asset-Backed Securities Loan Facility*

The asset-backed securities (ABS) and commercial mortgage-backed securities (CMBS) markets over time have funded a substantial share of credit to consumers, businesses and real estate owners. In the third quarter of 2008, the ABS market and commercial mortgage-backed securities markets came to nearly a complete halt. Interest rate spreads on the most highly-rated AAA tranches of ABS and CMBS rose to levels outside their historical range, in certain cases well over 7 to 15 times their average, respectively. CMBS had accounted for almost half of all new commercial mortgage originations in 2007. The disruption of these markets contributed to the lack of credit to households and businesses of all sizes, impacting U.S. economic activity.

In November 2008, the Federal Reserve and Treasury announced the creation of the Term Asset-Backed Securities Loan Facility (TALF) and launched TALF under the Financial Stability Plan on February 10, 2009. The TALF's objective was to stimulate investor demand for certain types of eligible ABS, specifically those backed by loans to consumers and small businesses, and ultimately, bring down the cost and increase the availability of new credit to consumers and businesses. Under the TALF, the Federal Reserve extends up to $200 billion in three- and five-year non-recourse loans to investors that agree to purchase eligible consumer or small business ABS. Treasury-OFS provides up to $20 billion of TARP monies in credit protection to the Federal Reserve for losses arising under TALF loans.

The TALF was initially designed for newly or recently originated AAA-rated ABS backed by student loans, auto loans, credit card loans, and loans guaranteed by the SBA. On March 19, 2009, Treasury-OFS and the Federal Reserve announced that the TALF would be expanded to include newly or recently issued AAA-rated Asset Backed Securities (ABS) backed by four additional types of consumer and business loans – mortgage servicing advances, loans or leases relating to business equipment, leases of vehicle fleets, and floor plan loans. These new categories of collateral were eligible for inclusion in the April 2009 TALF subscription and funding process.

The Treasury-OFS and the Federal Reserve structured the TALF to minimize credit risk to the U.S. government to the greatest extent possible, consistent with achieving the program's purpose of encouraging lending to consumers and businesses. Investors take risk by providing some of the capital to purchase the securities. The amount of private capital is measured in the form of haircuts, which represents the investor's equity contribution. For example, if a borrower purchases an ABS for $100 and that ABS has an assigned haircut of 15 percent, the borrower must put $15 at risk and can receive only $85 in financing. The haircut level varies across asset class and maturity to take into account any differences in risk. Finally, the borrower must also make monthly or quarterly interest payments to the federal government. The cost of the loan is 100 basis points over a fixed or floating rate benchmark, such as the London Interbank Offered Rate ("LIBOR").

The Federal Reserve had originally authorized using the TALF to make loans through December 31, 2009. To promote the flow of credit to businesses and households and to facilitate the financing of commercial properties, the Federal Reserve announced on August 17, 2009 that the TALF will continue to make loans against newly issued ABS and previously issued CMBS through March 31, 2010. In addition, TALF will make loans against newly issued CMBS through June 30, 2010. The inclusion of CMBS as eligible collateral helps prevent defaults on economically viable commercial properties, increases the capacity of current holders of maturing mortgages to make additional loans, and facilitates the sale of distressed properties.

TALF Results

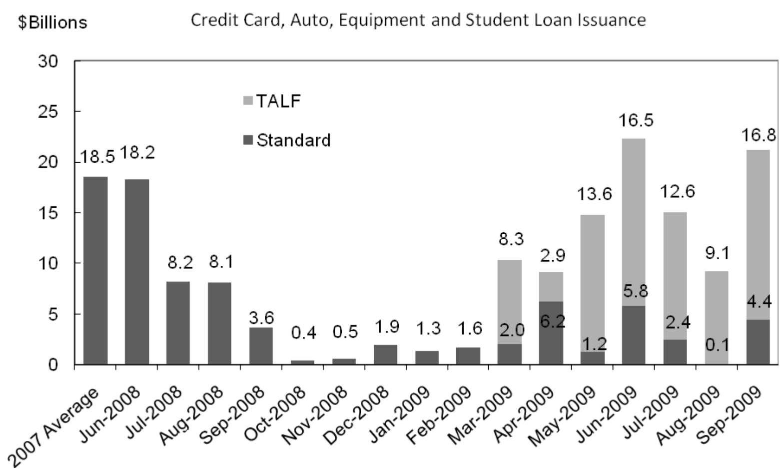
TALF's impact on the securitization markets can be measured by a number of indicators, including ABS issuance – both TALF and non-TALF eligible, the percentage decline in ABS and SMBS spreads from the height of the financial crisis, and the number and composition of investors in the securitization market.

ABS Issuance: The market for new issuance of ABS had shut down at the end of 2008 and remained effectively closed until TALF became operational. Since March 2009, offerings in the ABS markets have gradually increased with nearly $86 billion of new ABS issuance through October 2009. Of that amount, $49 billion of securities were purchased with TALF loans.

These securities supported over 3.6 million consumer and small business loans and leases, and over 132 million active credit card accounts. TALF has also provided loans to purchase about $4.1 billion of legacy CMBS securities (issued before January 1, 2009).

This re-starting of the securitization market translates into increased consumer and small business lending and, in some cases, lower loan rates for consumers. In addition, investors are gaining confidence in the market's ability to function without federal government support. In March 2009, approximately 60 percent of new ABS issuance was purchased with the support of the TALF. By September 2009, that was down to 40 percent. The following chart (Figure 12) shows total consumer ABS issuance and the portion backed by TALF.

Figure 12: Total Consumer ABS Issuance through September



Secondary market spreads: Since the peak of the credit crisis, spreads for the asset classes eligible for the program have decreased by 60 percent or more. Spreads on credit card and auto loans have fallen from a peak of 600 basis points to less than 100 basis points over their benchmarks, the same levels that existed before Lehman Brothers' bankruptcy filing in September 2008. Spreads in the secondary market for CMBS have come in from 1500 basis points over its benchmark to 300 basis points today. Prior to the beginning of the crisis in August 2007, highly rated CMBS were priced on average approximately 100 basis points over its benchmark.

40

Borrower Composition: At the peak of the credit crisis, there was little confidence among institutional investors in the capital markets. Investors effectively were standing on the sidelines. Since the implementation of TALF, there has been renewed confidence in the market. A range of institutional investors have become active participants, including hedge funds, asset managers, pension funds, and insurance companies.

With an increase in investor participation and thus investor demand, required returns have fallen more than half, in some cases, suggesting a return of risk premiums to more "normalized" levels. Cash participation, specifically for TALF-eligible prime auto and equipment transactions, has also increased, suggesting investors' decreasing reliance on TALF support. Further, some transactions for specific asset classes with shorter durations are being successfully completed without TALF financing, suggesting investor confidence in shorter-duration transactions.

TALF Loans to Date: As of September 30, 2009, no securities used as collateral for TALF loans had been surrendered to the Federal Reserve. In addition, as of September 30, 2009, 13.6 percent of the total amount of TALF loans, or $6.3 billion, had been repaid. Given that the term of the TALF loans is three to five years, this reflects the increasing health of the securitization markets.

2. *Unlocking Credit for Small Businesses Program*

To help restore the confidence needed for financial institutions to increase lending to small businesses, Treasury announced a program to unlock credit for small businesses on March 16, 2009. Under the program, Treasury announced that it would make up to $15 billion in TARP funds available to purchase securities backed by the Small Business Administration (SBA)-guaranteed portions of loans made under the SBA's 7(a) loan program. The SBA's 7(a) program is the SBA's most basic and widely used loan program.

Since Treasury's announcement of this program, the credit markets for small businesses have improved somewhat. The secondary market for guaranteed SBA loans, for example, had essentially ceased working last fall and had only $86 million in January re-sales. That market improved notably this spring in the wake of Treasury's announcement, with $399 million settled from lenders to broker-dealers in September 2009. As a result of this improvement, as well as reluctance on the part of market participants to accept TARP funds, Treasury-OFS found that demand for its proposed program declined. As of September 30, 2009, no funds had been disbursed under the program, although it remains available.

Public-Private Investment Program

Treasury, in conjunction with the Federal Reserve and the FDIC, announced the Public-Private Investment Program (PPIP) on March 23, 2009, as a part of the Financial Stability Plan. The PPIP is designed to improve the condition of financial institutions by facilitating the removal of legacy assets from their balance sheets. Legacy assets include both real estate loans held on banks' balance sheets (legacy loans) as well as securities backed by residential and commercial real estate loans (legacy securities).

The PPIP should help restart the market and provide liquidity for legacy assets, enabling financial institutions to make new loans available to households and businesses. Legacy assets became a stumbling block to the normal functioning of credit markets with the bursting of the housing bubble. With the housing market in decline, financial institutions and investors suffered significant losses on these legacy assets. These losses drove financial institutions to conserve capital, reduce leverage and minimize exposure to riskier investments. Many institutions did so by selling assets, triggering a wide-scale deleveraging in these markets. As the supply of assets being sold increased, prices declined and many traditional investors exited these markets, causing further declines in the demand and the liquidity for these assets. This lack of liquidity created significant uncertainty regarding the value of these legacy assets, which in turn raised questions about the balance sheets of these financial institutions, compromising their ability to raise capital and continue lending.

The PPIP helps address this valuation concern. Through PPIP, Treasury-OFS partners with experienced investment managers and private sector investors to purchase legacy assets. Rather than resolving the uncertainty by having the government set the price for these assets, the private sector investors compete with one another to establish the price of the legacy assets purchased under the PPIP. By drawing new private sector capital into the market for legacy assets and facilitating price discovery, the PPIP should increase the liquidity for these legacy assets.

Treasury-OFS initially announced that it would provide up to $100 billion for the PPIP. Because of improvements in the market, this amount was reduced to $30 billion. Under the PPIP, Treasury-OFS provides equity and debt financing to newly-formed public-private investment funds (PPIFs) established by private fund managers with private investors for the purpose of purchasing legacy securities. These securities are commercial mortgage-backed securities and non-agency residential mortgage-backed securities. To qualify for purchase by a Legacy Securities PPIP (S-PPIP), these securities must have been issued prior to 2009 and have originally been rated AAA – or an equivalent rating by two or more nationally recognized statistical rating organizations – without ratings enhancement and must be secured directly by the actual mortgage loans, leases, or other assets.

The S-PPIP allows the Treasury-OFS to partner with private investors in a way that increases the flow of private capital into these markets while maintaining equity "upside" for the taxpayers. Under the principal terms of the S-PPIP, Treasury-OFS partners with pre-qualified fund managers that raise a minimum amount of capital from private sources. Each manager forms a Public Private Investment Fund or PPIF. Treasury-OFS invests equity capital from the

TARP in each PPIF on a dollar-for-dollar basis, matching the funds raised by these managers. In addition, Treasury-OFS also provides debt financing up to 100 percent of the PPIF's total equity capital, subject to certain restrictions on leverage, withdrawal rights, disposition priorities and other customary financing protections. Treasury-OFS not only participates pro rata in any profits or losses of the PPIF but also receives additional potential equity upside in the form of warrants, as required by EESA. Each fund manager will seek to generate attractive returns for the PPIF through a predominately long-term buy and hold strategy.

On July 8, 2009, following a comprehensive two-month application, evaluation and selection process, Treasury-OFS pre-qualified nine fund managers to participate in the S-PPIP based, in part, on a demonstrated ability to invest in legacy assets and to raise private capital for such investments. On September 30, 2009, two PPIFs signed limited partnership agreements and loan agreements with Treasury-OFS, resulting in a $6.7 billion commitment for Treasury-OFS. As of September 30, 2009, these two PPIFs had approximately $1.13 billion in private sector capital commitments, which were matched 100 percent by Treasury-OFS, representing total equity capital commitments of $2.26 billion. Treasury-OFS is providing debt financing up to 100 percent of the total capital commitments of each PPIF, representing in the aggregate approximately $4.52 billion of total equity and debt capital commitments. As of November 30, 2009, eight PPIFs have signed agreements with Treasury-OFS. Following signature of these agreements, each fund manager has up to six months to raise additional private capital to receive the full allocation of the $3.3 billion in matching equity and debt capital from Treasury-OFS. Assuming that each of the nine fund managers raises enough private capital to receive the full allocation from Treasury-OFS, the total purchasing power of the PPIFs will be $40 billion, including $10 billion in private capital and the $30 billion Treasury-OFS commitment. As of September 30, 2009, no fund managers had made any investments and Treasury-OFS had not disbursed any funds.

PPIP Results

Although purchases of assets under the program are just beginning, the announcement of the program itself helped reassure investors. Since the announcement, prices for non-agency mortgage-backed securities have gone up substantially. Prime fixed-rate securities issued in 2006 that traded as low as $60 in March have increased in value by over 40 percent as markets have become more liquid. That improvement in financial market conditions has created the positive backdrop that caused Treasury-OFS to proceed with the program at a scale smaller than initially envisioned.

Automotive Industry Financing Program

Treasury-OFS established the Automotive Industry Financing Program (AIFP) on December 19, 2008, to help prevent a significant disruption to the American automotive industry, which would have posed a systemic risk to financial market stability and had a negative effect on the economy. Treasury-OFS announced a plan to make emergency loans available from the TARP under the AIFP to General Motors Corporation (GM) and Chrysler LLC (Chrysler) to provide a path for these companies to go through orderly restructurings and achieve viability.

Treasury-OFS' investments in the auto companies were determined to be consistent with both the purpose and specific requirements of EESA. Treasury-OFS determined that the auto companies were and are interrelated with entities extending credit to consumers and dealers because of their financing subsidiaries and other operations, and that a disruption in the industry or an uncontrolled liquidation would have had serious effects on financial market stability, employment and the economy as a whole. In addition, Congress provided the Secretary of the Treasury broad authority by defining "financial institutions" in EESA flexibly so as not to be limited to banks, savings institutions, insurance companies and similar entities. The auto companies qualified as "financial institutions" under EESA as they met the basic requirements of the definition. In each case, they were organized under Delaware law, had significant U.S. operations, were subject to extensive federal and state regulation, and were not a central bank or institution owned by a foreign government.

Treasury-OFS initially provided loans of $13.4 billion to GM and $4 billion to Chrysler under the AIFP to give the companies time to negotiate with creditors and other stakeholders in order to prevent disorderly bankruptcies. Under the terms of the loans, each company was required to prepare a restructuring plan that included specific actions aimed at assuring: (i) the repayment of the loan extended by TARP; (ii) the ability of the company to comply with applicable federal fuel efficiency and emissions requirements and commence the domestic manufacturing of advanced technology vehicles in accordance with federal law; (iii) achievement of a positive net present value; (iv) rationalization of costs, capitalization, and capacity with respect to the manufacturing workforce, suppliers and dealerships of the company; and (v) a product mix and cost structure that is competitive in the U.S. marketplace.

To oversee the federal financial assistance—including evaluating the restructuring plans—and to make decisions about future assistance to the automakers, the loan agreements provided for a presidential designee. Under the terms of the loan agreements, because no presidential designee has been appointed to date, the Secretary of the Treasury makes decisions on all matters involving financial assistance to the automakers, with input from the National Economic Council.

To date, the Treasury-OFS has provided approximately $76 billion in loans and equity investments to GM, Chrysler, and their respective financing entities. Further details on these loans and the valuation of these investments can be found in Section Eight [Valuation Methodology]

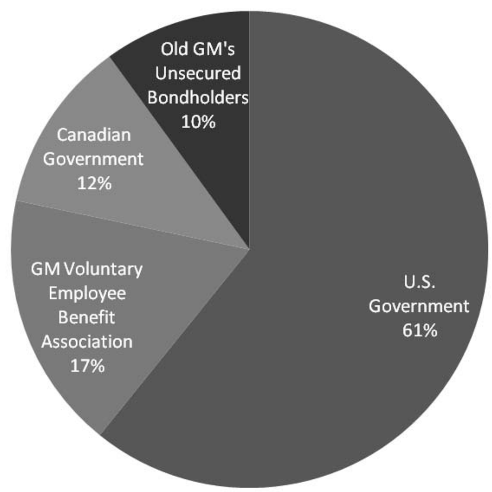
General Motors

On December 31, 2008, Treasury-OFS agreed to make loans of $13.4 billion to General Motors Corporation to fund working capital. Under the loan agreement, GM was required to implement a viable restructuring plan by March 30, 2009. The Administration determined that the first plan GM submitted failed to establish a credible path to viability, and the deadline was extended to June 1, 2009. Treasury-OFS loaned an additional $6 billion to fund GM during this period. To achieve an orderly restructuring, GM filed bankruptcy proceedings on June 1, 2009. Treasury-OFS provided $30.1 billion under a debtor-in-possession financing agreement to assist GM through the restructuring period. The new entity, General Motors Company (New GM) purchased most of Old GM's assets and began operating on July 10, 2009.

Treasury-OFS converted most of its loans to the Old GM to $2.1 billion of preferred stock and a 60.8 percent share of the common equity in the New GM and a $7.1 billion debt security note. $380 million of Treasury-OFS' debt in New GM was immediately repaid with the termination of the Auto Warranty Program, leaving $6.7 billion of loans outstanding as of September 30, 2009. The New GM currently has the following ownership: Treasury-OFS (60.8 percent), GM Voluntary Employee Benefit Association (17.5 percent), the Canadian

Government (11.7 percent), and Old GM's unsecured bondholders (10 percent).

Figure 13: New GM Ownership



Chrysler

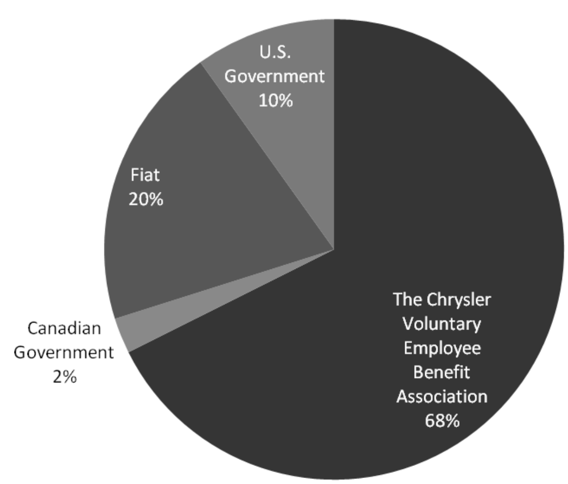
On January 2, 2009, Treasury-OFS loaned $4 billion to Chrysler. On March 30, 2009, the Administration determined that the business plan submitted by Chrysler failed to demonstrate viability and announced that in order for Chrysler to receive additional taxpayer funds, it needed to find a partner with whom it could establish a successful alliance. Chrysler made the determination that forming an alliance with Fiat was the best course of action for its stakeholders. Treasury-OFS continued to support Chrysler as it formed an alliance with Fiat. In connection with Chrysler's bankruptcy proceedings filed on April 30, 2009, Treasury-OFS

46

provided an additional $1.9 billion under a debtor-in-possession financing agreement to assist Chrysler in an orderly restructuring. On June 10, 2009, substantially all of Chrysler's assets were sold to the newly formed entity, Chrysler Group LLC (New Chrysler). Treasury-OFS committed to loan $6.6 billion to New Chrysler in working capital funding, and as of September 30, 2009, New Chrysler has drawn $4.6 billion of this amount.

As of September 30, 2009, Treasury-OFS had a $7.1 billion debt security from New Chrysler and held 9.9 percent of the equity in New Chrysler. The original loans to Chrysler remain outstanding, but have been reduced by $500 million of debt that was assumed by New Chrysler. Current equity ownership in New Chrysler is as follows: the Chrysler Voluntary Employee Benefit Association (67.7 percent), Fiat (20 percent), Treasury-OFS (9.9 percent) and the Government of Canada (2.5 percent).

Figure 14: New Chrysler Ownership



In addition to the AIFP funds committed to the two auto manufacturers, Treasury-OFS determined that TARP assistance was also needed for the financing companies affiliated with these manufacturers. The vast majority of automobile purchases in the U.S. are financed, including an estimated 80 to 90 percent of consumer purchases and substantially all dealer inventory purchases. Without the TARP's assistance, it is unlikely that the tightened credit markets would have been able to provide the critical financing needed for consumers to purchase autos. A description of the assistance provided to GMAC and Chrysler Financial is provided below.

GMAC

GMAC is an important source of auto-related credit for consumers and dealers and, through a subsidiary, is the country's fifth largest mortgage servicer. It is also one of the largest U.S. bank holding companies. On December 29, 2008, Treasury-OFS purchased $5 billion in preferred equity from GMAC, and received an additional $250 million in preferred equity through warrants that Treasury-OFS exercised at closing. At the same time, Treasury-OFS also agreed to lend up to $1 billion of TARP funds to GM (one of GMAC's owners), to enable GM to participate in GMAC's rights offering. GM drew $884 million under that commitment on January 16, 2009.

In May 2009, banking regulators required GMAC to raise additional capital by November 2009 in connection with the SCAP or stress test. On May 21, 2009, Treasury-OFS purchased $7.5 billion more of convertible preferred shares from GMAC and received warrants that Treasury-OFS exercised at closing for an additional $375 million in convertible preferred shares. GMAC is in discussions with the Treasury-OFS regarding additional financing to complete GMAC's post-SCAP capital needs up to the amount of $5.6 billion, as previously discussed in May.

On May 29, 2009, Treasury-OFS exercised its option to exchange the $884 million loan for the ownership interest that GM had purchased, amounting to about 35 percent of the common membership interests in GMAC. As of September 30, 2009, Treasury-OFS owns $13.1 billion in preferred shares in GMAC, through purchases and the exercise of warrants, in addition to 35 percent of the common equity in GMAC.

Chrysler Financial

On January 16, 2009, Treasury-OFS announced that it would lend up to $1.5 billion to a special purpose vehicle created by Chrysler Financial to enable Chrysler Financial to finance the purchase of Chrysler vehicles by consumers. To satisfy the EESA warrant requirement, the Chrysler Financial special purpose vehicle issued additional notes entitling Treasury-OFS to an amount equal to 5 percent of the maximum loan amount. Twenty percent of those notes vested upon the closing of the transaction, and additional notes were to vest on each anniversary of the transaction closing date. The loan was fully drawn by April 9, 2009. On July 14, 2009, Chrysler Financial fully repaid the loan, including the vested additional notes and interest.

Auto Supplier Support Program

Because of the credit crisis and the rapid decline in auto sales, many of the nation's auto parts suppliers were struggling to access credit and faced uncertainty about the prospects for their businesses. Suppliers that ship parts to auto companies generally receive payment approximately 45-60 days after shipment. In a normal credit environment, suppliers can either sell or borrow against those commitments, or receivables, in the interim period to pay their workers and fund their ongoing operations. However, due to the uncertainty about the ability of the auto companies to honor their obligations, banks were unwilling to extend credit against these receivables. On March 19, 2009, Treasury-OFS announced the Auto Supplier Support Program (ASSP) to help address this problem by providing up to $5 billion to domestic auto manufacturers to purchase supplier receivables. With the emergence of New GM and New Chrysler from bankruptcy proceedings and with the threat of liquidation greatly reduced, credit market access for suppliers has improved. As of July 1, 2009, the base commitment under the ASSP was decreased to $3.5 billion. As of September 30, 2009, Treasury-OFS has funded $413 million under the ASSP. The loans used to finance the program must be repaid within a year, unless extended. Treasury-OFS expects these loans to be fully repaid by or before April 2010. The companies may still draw on the loans but they are not expected to.

Auto Warranty Program

On March 30, 2009, Treasury-OFS announced an Auto Warranty Program designed to give consumers considering new car purchases from domestic manufacturers the confidence that warranties on those cars would be honored regardless of the outcome of the restructuring process. As of July 10, 2009, the program was terminated after New GM and New Chrysler completed the purchase of substantially all of the assets of GM and Chrysler from their respective bankruptcies. The $640 million advanced to GM and Chrysler under the program has been repaid to Treasury-OFS; Chrysler repaid the full amount with interest while GM repaid only principal.

Section Four: Preventing Foreclosures and Preserving Homeownership

To mitigate foreclosures and help ensure homeownership preservation, Treasury announced a comprehensive $75 billion program, the Home Affordable Modification Program (HAMP), in February 2009. Treasury-OFS will provide up to $50 billion in funding through the TARP, while Fannie Mae and Freddie Mac agreed to provide up to $25 billion of additional funding. HAMP focuses on creating sustainably affordable mortgage payments for responsible home owners who are making a good faith effort to make their mortgage payments, while mitigating the spillover effects of preventable foreclosures on neighborhoods, communities, the financial system and the economy.

HAMP is built around three core concepts. First, the program focuses on affordability. Every modification under the program must lower the borrower's monthly mortgage payment to no more than 31 percent of the borrower's monthly gross income, the "target monthly mortgage payment ratio". Second, the HAMP's pay-for-success structure aligns the interests of servicers, investors and borrowers in ways that encourage loan modifications that will be both affordable for borrowers over the long term and cost-effective for investors and taxpayers. Third, the HAMP establishes detailed guidelines for the industry to use in making loan modifications with the goal of encouraging the mortgage industry to adopt a sustainably affordable standard, both within and outside of the HAMP.

HAMP operates through the combined efforts of the Treasury Department, Fannie Mae, Freddie Mac, mortgage loan servicers, investors and borrowers to help qualifying homeowners who commit to making modified monthly mortgage payments to stay in their homes. In addition, the federal bank, thrift, and credit union regulatory agencies have encouraged all federally regulated financial institutions that service or hold residential mortgage loans to participate in the HAMP.

The following highlights some of the key terms and conditions of HAMP:

- Eligible Homeowners: The modification plan was designed to be inclusive, with a loan limit of $729,750 for single-unit properties, and higher limits for multi-unit properties. Over 97 percent of the mortgages in the country have a principal balance within these limits.
- Servicers' Obligation to Extend Modification Offer: Servicers participating in HAMP are required to apply a standardized net present value (NPV) test to each loan that is at risk of foreclosure -- defined as either at risk of imminent default or in default. The NPV test compares the net present value of cash flows from the mortgage if modified under HAMP and the net present value of the cash flows from the mortgage without modification. If the NPV test is positive – meaning that the net present value of expected

cash flows is greater if modified under the HAMP than if the loan is not modified – the servicer must extend an offer to modify the loan in accordance with HAMP guidelines, absent fraud or a contractual prohibition limiting modification of the mortgage.

- Reductions in Monthly Payments: Servicers are required to follow the waterfall outlined in the program contracts in reducing the borrower's monthly payment to no more than 31 percent of their monthly gross income. The interest rate floor under HAMP is 2 percent. Further flexibility is provided if reducing the loan rate to 2 percent, by itself, does not achieve the 31 percent threshold. In that case, the servicers can extend the term of the loan, up to 480 months, in order to achieve the 31 percent payment threshold. The HAMP also provides the servicer the option to reduce principal on a stand-alone basis to help reduce the borrower's monthly payment

The HAMP includes a standardized set of procedures that servicers must follow in modifying eligible loans under the program and in estimating the expected cash flows of modified mortgages. The borrower must remain current on their modified mortgage payments for at least 90 days in order for a HAMP loan modification to become permanent.

To increase participation in HAMP and encourage borrowers to remain current on loan modifications under the program, Treasury-OFS provides targeted incentives to borrowers, investors, and servicers that participate in the program. These incentives include an up-front payment of $1,000 to the servicer for each successful modification after completion of the trial period, and "pay for success" fees of up to $1,000 per year for three years, provided the borrower remains current. Additional one-time incentives of $500 to the servicers and $1,500 to the investors are paid if loans are modified for borrowers who are current but are in danger of imminent default are successfully modified. Homeowners will also earn up to $1,000 towards principal balance reduction each year for five years if they remain current and pay on time. Investors are entitled to payment reduction cost-share compensation for up to five years for half the cost of reducing the borrower's payment from a 38 percent to 31 percent threshold, provided the borrower remains current. Investors must pay for reducing the borrower's payment down to the 38 percent threshold before they are able to benefit from the cost-share incentive. This requires investors to take the first loss for unaffordable and unsustainable loans that were extended to borrowers.

HAMP Results

The incentives offered under HAMP have had a substantial impact in helping American homeowners and stabilizing the housing market, as detailed below:

- As of October 31, 2009, 71 servicers have signed up for the HAMP. Between loans covered by these servicers and loans owned or guaranteed by the GSEs, approximately 85 percent of first-lien residential mortgage loans in the country are now covered by the program. As of September 30, 2009, Treasury-OFS has made commitments to fund up to $27.1 billion in HAMP payments.
- As of October 31, 2009, these participating servicers have extended offers on over 919,665 trial modifications.
- Over 650,994 trial modifications are already underway, as of October 31, 2009.

HAMP Snapshot through October 2009

Number of Trial Modifications Started[1]	***650,994***
Number of Trial Period Plan Offers Extended to Borrowers[2]	***919,665***
Number of Requests for Financial Information Sent to Borrowers[2]	***2,776,740***

[1]Active trial and permanent modifications as of October 31; based on numbers reported by servicers to the HAMP system of record.

[2] Source: Survey data provided by servicers, through October 29

52

Section Five: Protecting Taxpayer Interests

The government's response to the financial crisis including the actions taken under TARP, were necessary to avoid an even greater deterioration or collapse of the U.S. and global financial systems , which would have resulted in a far worse recession or even depression. TARP provided a form of taxpayer protection by helping to achieve that basic objective. Treasury-OFS is committed to ensuring that taxpayers are also protected with respect to how the TARP is implemented. The taxpayers clearly assumed downside risk in the TARP purchases and guarantees of troubled assets, thus Treasury-OFS also seeks to protect the taxpayer through the effective management and disposition of all TARP investments. EESA also stipulated that the taxpayer benefit from any potential upside on any assistance transaction by requiring that Treasury receive warrants in most investments. This section addresses portfolio management topics such as:

1) Portfolio Overview
2) Guiding Principles
3) Portfolio Management Approach
4) Exchange Offers and Restructurings
5) Treasury-OFS' Actions as a Shareholder
6) Compliance
7) Program Specific Considerations.

<u>Portfolio Overview</u>

Treasury-OFS' TARP investments include:

1) Preferred stock: a majority of the TARP investments are in nonvoting perpetual preferred stock;
2) Common stock: currently, Treasury-OFS holds common stock in GM, GMAC, Chrysler and Citigroup;
3) Warrants and senior debt instruments: in connection with its investments in publicly traded companies, Treasury-OFS has received, pursuant to Section 113 of EESA, warrants to purchase common stock at market price as of the time of the investment. In the case of investments in privately held companies, Treasury-OFS has received warrants to purchase preferred stock at a nominal price, which it exercised at closing, or debt instruments issued by the TARP recipient;

4) Loans: Treasury-OFS has made loans to GM, Chrysler, and the special purpose vehicles under TALF, AIFP, ASSP, and WCP as well as signed definitive loan agreements for the Public Private Investment Funds (PPIFs); and

5) Fund investments: Treasury-OFS has signed limited partnership agreements to make equity investments in the PPIFs.

Guiding Principles

Pursuant to Section 2 of EESA, Treasury-OFS has made investments and entered into guarantee agreements to "restore liquidity and stability to the financial system of the United States" in a manner which "maximizes overall returns to the taxpayers of the United States". Consistent with the statutory requirements, Treasury-OFS' four overarching portfolio management guiding principles are as follows:

- Protect taxpayer investments and maximize overall investment returns within competing constraints,
- Promote stability for and prevent disruption of financial markets and the economy,
- Bolster market confidence to increase private capital investment, and
- Dispose of investments as soon as practicable, in a timely and orderly manner that minimizes financial market and economic impact.

Treasury-OFS' asset management approach is designed to implement the guiding principles. Treasury-OFS protects taxpayer investments and promotes stability through evaluating systemic and individual risk from standardized reporting and proactive monitoring and ensuring adherence to EESA and compliance with contractual agreements. By avoiding involvement in day to day company management decisions and exercising its rights as a common shareholder only on core governance issues, Treasury-OFS seeks to bolster market confidence to increase private capital investment. Treasury-OFS also adheres to certain principles in connection with restructurings or exchange offers involving TARP recipients, including minimizing taxpayer loss, enhancing and preserving institutional viability, treating like investments across programs consistently, and minimizing negative governmental impact. Such efforts help to prevent disruption of financial markets and the economy.

Treasury-OFS seeks to exit investments as soon as practicable to remove Treasury-OFS as a shareholder, eliminate or reduce Treasury-OFS downside tail risk exposure, return TARP funds to reduce the federal debt, and encourage private capital formation to replace federal government investment. The desire to achieve such objectives must be balanced against a variety of other objectives, including avoiding further financial market and/or economic disruption, and the potentially negative impact to the issuer's health and/or capital raising plans from Treasury-OFS' disposition. Treasury-OFS must also consider the limited ability to sell an investment to a third party due to the absence of a trading market or lack of investor demand, and the possibility of achieving potentially higher returns through a later disposition. An issuer typically needs the approval of its primary federal regulator in order to repay Treasury-OFS and therefore regulatory approvals also affect how quickly an institution can repay.

Because of the size of certain positions as well as the overall portfolio, successful disposition will take time, as well as expertise. In addition, information about Treasury-OFS' intentions with respect to its investments could be material information and premature release of such information could adversely affect the ability of Treasury-OFS to achieve its objectives. Therefore, Treasury-OFS will make public announcements of its disposition plans when it is appropriate to do so in light of these objectives and constraints.

Portfolio Management Approach

In managing the TARP investments, Treasury-OFS takes a disciplined portfolio approach with a review down to the individual investment level. Treasury-OFS aims to monitor risk and performance at both the overall portfolio level and the individual investment level. Given the unique nature and the size of the portfolio, risk and performance are linked to the overall financial system and the economy. Therefore, Treasury-OFS conducts sensitivity analyses to contextualize the results. Such analyses by their very nature are based upon significant assumptions.

In conducting the portfolio management activities, Treasury-OFS employs a mix of dedicated professionals and external asset managers. These external asset managers provide market specific information such as market prices and valuations as well as detailed credit analysis using public information on a periodic basis. A portfolio management leadership team oversees the work of asset management employees organized on a program basis, under which investment and asset managers may follow individual investments.

Treasury-OFS tracks the fair market value of the assets in the TARP portfolio on a regular basis. The value of publicly traded common stock can be measured by market quotations. Most of Treasury-OFS' investments, however, consist of securities and instruments for which no market exists. Such securities include preferred stocks, warrants, loans and other debt securities, as well as common stock of private companies. As a result, Treasury-OFS has developed internal, market-based valuation models in consultation with Treasury-OFS' external asset managers and in compliance with EESA. For purposes of its financial statements, Treasury-OFS calculates valuations in accordance with the Federal Credit Reform Act of 1990, as well as OMB guidelines. The methodology is discussed further in Section Eight [Valuation Methodology].

Risk Assessment

Treasury-OFS has developed procedures to identify and mitigate investment risk. These procedures are designed to identify TARP recipients that are in a significantly challenged financial condition to ensure heightened monitoring and additional diligence and to determine appropriate responses by Treasury-OFS to preserve the taxpayers' investment and minimize loss as well as to maintain financial stability. Specifically, Treasury-OFS' external asset managers review publicly available information to identify recipients for which pre-tax, pre-provision earnings and capital may be insufficient to offset future losses and maintain required capital. For certain institutions Treasury-OFS and its external asset managers engage in heightened monitoring and due diligence that reflects the severity and timing of the challenges.

Although Treasury-OFS relies on the recommendations of federal banking regulators in connection with reviewing and approving applications for assistance, Treasury-OFS does not have access to non-public information collected by federal banking regulators on the financial condition of TARP recipients. To the contrary, there is a separation between the responsibilities of Treasury-OFS as an investor and the duties of the government as regulator.

The data gathered through this process is used by Treasury-OFS in consultation with its external managers and legal advisors to determine a proper course of action. This may include making recommendations to management or working with management and other security holders to improve the financial condition of the company, including through recapitalizations or other restructurings. These actions are similar to those taken by large private investors in dealing with troubled investments. Treasury-OFS does not seek to influence the management of TARP recipients for non-financial purposes.

Exchange Offers and Restructurings

TARP recipients may also seek Treasury-OFS' approval for exchange offers, recapitalizations or other restructuring actions to improve their financial condition. Treasury-OFS evaluates each such proposal based on its unique facts and circumstances, and takes into account the following principles in all cases:

- Pro forma capital position of the institution,
- Pro forma position of Treasury-OFS investment in the capital structure,
- Overall economic impact of the transaction to the government,

- Guidance of the institution's primary federal supervisor, and
- Consistent pricing with comparable marketplace transactions.

Treasury-OFS' Actions as a Shareholder

Treasury-OFS' role as a shareholder is to manage the government's investment and not to manage the related company. Most of Treasury-OFS' equity investments have been in the form of preferred stock. As is typical for a preferred stock investor, Treasury-OFS does not have voting rights except on certain limited issues such as amendments to the charter and certain transactions that could adversely affect Treasury-OFS' rights as an investor. In the event preferred dividends are unpaid for six quarters (or four quarters in the case of AIG preferred stock), Treasury-OFS has the right to elect two directors to the board. Treasury-OFS holds common shares in GM, GMAC, Chrysler and Citigroup. In addition, the taxpayers are the beneficiaries of a trust that exercises 80 percent of the voting rights of the outstanding AIG common stock. This trust is controlled by three independent trustees who exercise voting rights on behalf of the taxpayers and do not report to Treasury-OFS.

Treasury-OFS has established the following four principles to guide its actions as a common shareholder:

- Reluctant shareholder: The government is a reluctant owner as a consequence of the financial crisis and the current recession. Treasury-OFS intends to dispose of its investments as soon as practicable and in conformity with the aforementioned portfolio management principles;

- Treasury-OFS will not interfere in the day-to-day management decisions of a company in which it is an investor. Such interference might actually reduce the value of those investments, impede the companies' successful transition to the private sector, expose taxpayers to third party lawsuits, and frustrate the federal government's broader economic policy goals;

- Strong board of directors: Establishing an effective board of directors that selects management with a sound, long-term vision should restore a company to profitability and end the need for government support expeditiously. In cases where Treasury-OFS has the ability to establish strong upfront conditions at the time of investment, these may include changes to the existing board of directors and management; and

- Limited voting rights: The government intends to exercise its voting rights as a common shareholder only with respect to core shareholder matters such as board membership; amendments to corporate charters or bylaws; mergers, liquidations, substantial asset sales; and significant common stock issuances.

Compliance

Treasury-OFS also takes steps to ensure that TARP recipients comply with their TARP-related statutory and contractual obligations. Statutory obligations include executive compensation restrictions. Contractual obligations vary by investment type. For most of Treasury-OFS' preferred stock investments, TARP recipients must comply with restrictions on payment of dividends and on repurchases of junior securities, so that funds are not distributed to junior security holders prior to repayment of the government. Recipients of exceptional assistance must comply with additional restrictions on executive compensation, lobbying, corporate expenses and internal controls and must provide quarterly compliance reports. For AIFP loans, additional restrictions and enhanced reporting requirements are imposed, which is typical with debt investments compared to equity investments. Such enhanced reporting requirements include bi-weekly status reports (rolling 13-week cash forecast), monthly liquidity analysis reports, and monthly budget reports covering the current fiscal year.

Program Specific Considerations

The following briefly describes key contractual terms and other characteristics of each program that affect how Treasury-OFS will recover the TARP funds invested in each institution.

Capital Purchase Program (CPP)

The majority of Treasury's investments under TARP were made under the CPP program. Treasury-OFS received preferred stock and warrants in return for the capital it provided each institution. The preferred stock is redeemable at the option of the issuer at any time, subject to the approval of the primary federal bank regulator. This means that the primary federal bank regulator, such as the Federal Reserve Bank or the FDIC, must determine that the issuer has sufficient capital to repay Treasury-OFS. If permitted to repay Treasury-OFS, the issuer must repay the full amount of the investment plus any accrued dividends. As of September 30, 2009, 42 issuers have repaid a total of $70.7 billion of CPP investments. Treasury-OFS did not require issuers to repay the preferred stock by a particular date, because the preferred stock would not have met the requirements for Tier 1 capital had such a fixed date been imposed. However, there are incentives for issuers to repay. First, issuers are subject to restrictions on executive compensation for as long as the preferred stock is outstanding. In addition, they are restricted in their ability to pay dividends to common stockholders and to make other distributions and repurchases. In addition, the dividend rate on the preferred stock increases from five percent to nine percent after five years.

Treasury-OFS also has the right to sell the preferred stock to a third party. Treasury-OFS also has registration rights, which are rights to require the issuer to assist Treasury-OFS in

58

making a public sale of the securities which can facilitate transfer. Although Treasury-OFS has not exercised these rights, it may do so in the future. In the case of Citigroup, Treasury-OFS exchanged the CPP preferred shares for common stock of Citigroup. Because the common stock is not redeemable and because there is a large trading market for Citigroup common stock, one potential manner in which Treasury-OFS may exit this investment would be by selling the stock in the market.

Much of Treasury-OFS' warrant portfolio pertains to CPP investments. Pursuant to the requirements of EESA, Treasury receives warrants from TARP recipients in order to give the taxpayers an opportunity to participate in any increase in shareholder value that follows the investment. In the case of a CPP investment in a company that is publicly traded, Treasury-OFS receives warrants to acquire common stock with a price equal to 15 percent of the senior preferred investment. The exercise price on the warrants is the market price of the participating institution's common stock at the time of preliminary approval calculated on a 20-trading day trailing average. In the case of an investment in a privately-held company, Treasury-OFS receives warrants to purchase, at a nominal cost, additional preferred stock equivalent to 5 percent of the senior preferred investment. Treasury-OFS exercises the latter kind of warrants at closing of the senior preferred investment.

CPP Sale of Warrants

Issuers have a contractual right to repurchase the warrants upon redemption of the preferred stock issued to Treasury-OFS. In the event they do not repurchase, Treasury-OFS will sell the warrants to third parties.

If an issuer wishes to repurchase its warrants, the issuer and Treasury-OFS must agree on a price. The contract provides for an independent appraisal procedure that can be invoked by either party to determine this price. Treasury-OFS has established a methodology for valuing warrants for purposes of this process that it uses for all banks, regardless of the size of the bank or the warrant position. Treasury-OFS' determination of the value of any warrant is based on three categories of input: market prices, financial modeling, and outside consultants. Further details on this valuation approach are provided in Section Eight. If the bank and Treasury-OFS do not agree on price and the appraisal procedure is invoked by either party, then each party selects an independent appraiser. These independent appraisers will conduct their own valuations and attempt to agree upon the fair market value. If they agree on a price, that price becomes the basis for repurchase of the warrants by the bank. If these appraisers fail to agree, a third appraiser is hired, and subject to some limitations, a composite valuation of the three appraisals is used to establish the sale price.

Even if agreement is not reached within the aforementioned timeframe, an institution that has redeemed its preferred stock can always bid to repurchase its warrants at any time, and

Treasury-OFS can choose whether to accept a bid. Similarly, Treasury-OFS retains the right to sell the warrants to a third party at a mutually agreed price. If following repayment of the preferred stock, an institution notifies Treasury-OFS that it does not intend to repurchase its warrants, or if an agreement is not reached, Treasury-OFS intends to dispose of the warrants through public auctions. Treasury-OFS has announced that the first such auctions would take place in early December. These auctions are conducted as modified "Dutch" auctions which are registered under the Securities Act of 1933. Only one issuer's warrants will be auctioned in each auction. In this format, qualified bidders may submit one or more independent bids at different price-quantity combinations and the warrants will be sold at a uniform price that clears the market.

Targeted Investment Program (TIP)

Treasury-OFS invested $20.0 billion in each of Citigroup and Bank of America under TIP and acquired preferred stock. In the case of Citigroup, Treasury-OFS exchanged the preferred stock for trust preferred securities, which are senior in right of repayment to preferred stock but otherwise have many similar terms. Both the Citigroup trust preferred securities and the Bank of America preferred stock pay dividends at 8 percent per year. Treasury-OFS also received warrants in connection with both investments. The disposition considerations are similar to those for CPP, including the fact that the issuers need the approval of the primary banking regulators to repay the trust preferred securities and preferred stock.

Automotive Industry Investments (AIFP/ASSP)

Treasury-OFS' auto industry investments consist of equity investments, largely in the form of common stock, as well as loans. The loans must be repaid by certain dates. The GM loan was recently amended to require quarterly mandatory prepayments of $1 billion from existing escrow amounts in addition to the obligation for such funds to be applied to repay the loan by June 30, 2010, unless extended. In addition, the loan matures in July 2015. A portion of the Chrysler loan also matures in December 2011 and the balance in June 2017. Chrysler has recently announced that it plans to repay the loan fully prior to maturity.

In the case of the equity investments, Treasury-OFS holds primarily common stock in GM, Chrysler, and GMAC. Because the companies are not publicly traded at this time, there is no market for the common stock. Treasury-OFS also holds preferred stock in GM and GMAC. Of the $13.1 billion in preferred shares in GMAC held by Treasury-OFS, $7.875 billion is convertible at the option of GMAC subject to certain conditions.

Contractual agreements govern disposition options and timetables, and participants in AIFP are subject to enhanced reporting requirements relative other TARP recipients (discussed under "Compliance"). Treasury-OFS will periodically evaluate both public and private options to exit the equity investments under the AIFP. For GM the most likely exit strategy is a gradual sell off of shares following a public offering. Pursuant to its operating agreement, General Motors will attempt a reasonable best efforts initial public offering by July 10, 2010. This date marks the one-year anniversary of the automaker's exit from bankruptcy. For Chrysler and GMAC, the exit strategy may involve either a private sale or a gradual sell off of shares following a public offering. In each case, Treasury-OFS' goal is to dispose of the government's interests as soon as practicable consistent with EESA goals. As described below, Treasury will sell down, and ultimately sell off completely its interests in a timely and orderly manner that minimizes financial market and economic impact. At the same time, Treasury cannot control market conditions and have an obligation to protect taxpayer investments and maximize overall investment returns within competing constraints.

Treasury-OFS has reduced the Automotive Supplier Support Program (ASSP) aggregate commitment from $5.0 billion to $3.5 billion. Treasury-OFS' current funding equates to $0.4 billion, with GM and Chrysler accounting for $0.3 billion and $0.1 billion, respectively. Treasury-OFS does not anticipate increased participation prior to the program's April 2010 expiration.

American International Group (AIG)

Treasury-OFS holds preferred stock in AIG. As with the CPP preferred, there is no mandatory repayment date. AIG has replaced most of its board of directors, as well as its chief executive officer since September 2008, and is presently engaged in a variety of restructuring initiatives, including the divestment of assets to enable repayment of loans made by the FRBNY, as well as Treasury-OFS' investment and the wind-down of exposure to certain financial product and derivative trading activities to reduce excessive risk taking.

Term Asset Backed Loan Facility (TALF)

Although Treasury-OFS has committed to provide up to $20 billion in credit protection to the TALF special purpose vehicle, Treasury-OFS has only funded $0.1 billion as of September 30, 2009. Additional funding will be required only if borrowers default on their non-recourse loans and surrender the collateral for such loans, which consists of asset-backed securities to the FRBNY), which made the loans. In that event, Treasury-OFS' funds are used to reimburse the Federal Reserve Bank, and the asset-backed securities would then be sold to repay Treasury-OFS.

Asset Guarantee Program (AGP)

This program, which currently includes only Citigroup differs from other TARP financial institution support programs in that Treasury-OFS, does not invest TARP funds in the institution directly. Rather, TARP funds are reserved to cover a portion of the possible losses in the selected assets. In conjunction with the transaction, Treasury-OFS received $4.0 billion of preferred stock with identical terms as Citigroup's agreement under TIP. This investment is managed and monitored in conjunction with TIP. As of September 30, 2009, no payment had been made to Citigroup related to the covered asset pool. The preferred stock can be redeemed or sold in the same manner as CPP and TIP preferred stocks. Treasury-OFS also received warrants in connection with this investment.

Treasury-OFS has a cross functional team of staff overseeing and monitoring the covered asset pool under the Citigroup AGP. Given the nature of the transaction, the Treasury-OFS, FRBNY and FDIC work collaboratively on overseeing the Citigroup AGP. Additionally, U.S. Federal Parties have engaged outside independent service providers to perform various business, compliances/audit activities with respect to the covered asset pool.

Public-Private Investment Program (PPIP)

Treasury-OFS' investments in Public-Private Investment Funds (PPIFs) are subject to different disposition considerations given the nature of the investments. Treasury-OFS provides funds which are used by the PPIF managers, together with private capital, to purchase asset-backed securities. These asset-backed securities then yield principal, interest and dividend payments to the PPIFs which are used to repay Treasury-OFS for its loans, and provide distributions to Treasury and the private investors for their equity investments.

Treasury-OFS' management of these investments is therefore focused on ensuring that the asset managers comply with the requirements of the program, including the detailed compliance rules that govern matters such as conflicts of interest. Fund managers are required to disclose to and seek the approval of Treasury-OFS with respect to certain fundamental corporate policies that could impact the PPIFs. In addition, there are restrictions on dealings with affiliates and other interested parties, which will help ensure that the PPIFs only enter into arm's-length transactions.

Section Six: Promoting Transparency

Treasury-OFS is committed to providing full disclosure regarding the TARP. This includes information on how the money has been spent, who has received it, and the results of those investments. Providing such information promotes transparency and insures accountability. In order to meet these objectives, Treasury-OFS operates under a core set of principles. First, Treasury-OFS will provide detailed information on its programs on a timely basis, including information on specific institutions. Second, Treasury-OFS will provide that information in accessible and usable formats. Finally, Treasury-OFS will focus on answering the questions that are most important to the public, the Congress or the oversight bodies.

1. Providing detailed and timely information

Treasury-OFS publishes a variety of reports that provide information about TARP programs and transactions, and Treasury-OFS activities. For the period ended September 30 2009, Treasury-OFS published the following reports and information, which are available publicly at :

- 86 transaction reports, in accordance with section 114 of EESA, which include details on every investment in every institution under every program, including dates and amounts invested, as well as payments received with respect to TARP investments.
- 10 Section 105(a) monthly congressional reports which provide qualitative program updates and detailed financial information on all programs
- 7 Tranche Reports in accordance with section 105(b) of EESA, which outline the details of the transactions related to each $50 billion increment of TARP investments.
- 3 Dividend and interest reports.
- 2 Making Home Affordable program reports,
- 7 Monthly Lending and Intermediation Snapshot reports and 7 CPP Monthly Lending Reports and
- 2 Section 104(g) Financial Stability Oversight Board quarterly reports to the Congress.

All program descriptions, including term sheets and forms of contracts, are also posted. Treasury-OFS has used standard forms of contracts and thus within a program there is little variation among the contracts for all institutions. Treasury-OFS has also posted investment contracts on the Treasury-OFS' website within two business days of each transaction's closing.

The monthly report to Congress, also known as the Section 105(a) report, provides one of the most useful ways to track the activities of TARP. It contains easy-to-read charts showing how much money has been spent and where the money is going by program. It also contains charts on how much money has been repaid or returned to Treasury-OFS, descriptions of each TARP program as well as highlights of new developments. For those who want more detail, the transaction reports give details on each investment.

2. *Making information usable and accessible*

A key element in the Treasury-OFS public outreach effort is providing user-friendly resources online. Earlier this year, Treasury-OFS launched a new website -- www.FinancialStability.gov -- that provides a wealth of information about the TARP. FinancialStability.gov provides all of the TARP reports, lists the institutions participating in the Treasury-OFS' programs, and makes available detailed contracts defining those investments. As of today, Treasury-OFS has posted nearly 700 investment contracts, in addition to terms and program guidelines for all programs under EESA. Treasury-OFS also launched the website www.MakingHomeAffordable.gov to provide specific information to homeowners on the Making Home Affordable Program and efforts to mitigate the foreclosure crisis. In addition, Treasury-OFS has launched an initiative to ensure that its website meets the needs of all its users to provide easily accessible data and information.

HAMP Reporting

Treasury-OFS is improving performance and enhancing transparency on the HAMP.

1. **Servicer-specific results are now reported on a monthly basis.** These reports provide a transparent and public accounting of individual servicer performance by detailing the number of trial modification offers extended.
2. **Treasury-OFS is establishing specific operational metrics.** These metrics will measure the performance of each servicer, such as average borrower wait time in response to inquiries, and the response time for completed applications; and servicer performance will be included in our monthly public report.
3. **Treasury-OFS directed that Freddie Mac review declined modifications.** In its role as compliance agent, Freddie Mac has developed a "second look" process by auditing samples of HAMP modification applications that have been declined. This will minimize the likelihood that borrower applications are overlooked or that applicants are inadvertently or incorrectly denied a modification. In addition, the "second look" program is examining servicer non-performing loan (NPL) portfolios to identify eligible borrowers that should have been solicited for a modification, but were not.

3. Answering the right questions

In being transparent with information, Treasury-OFS has designed reports not only to be detailed and timely, but also to answer the questions that observers most frequently ask. For example, Treasury-OFS is often asked about what banks are doing with their TARP funds. So, in January 2009, Treasury-OFS launched an important initiative to help the public easily assess the lending and intermediation activities of the largest CPP participants and more limited information for smaller CPP participants. Treasury-OFS now publishes monthly and quarterly lending surveys that contain information on the lending and other activities of over 670 institutions that have received TARP funds.

Performance Metrics for FY 2010

Treasury-OFS has developed performance measures related to each of its strategic goals for FY 2010.

- Additional performance measures will evaluate the change in the capital ratios and lending of CPP participants by comparing them to a control set of banks with similar characteristics.
- Treasury-OFS will continue to evaluate performance of the SCAP bank holding companies (BHCs). Performance measures will includes changes in capital ratios and lending of the SCAP

65

BHCs versus control banks with similar characteristics.

- Treasury-OFS will continue to track various performance measures for the TALF. These measures will include the TALF-eligible ABS issuance, spreads in the secondary markets of RMBS, and CMBS securities, as well as the spread between secondary ABS and benchmarks.
- Performance measures of the number of HAMP modifications (trial and permanent) entered into, the redefault rate, and the change in average borrower payments will be tracked.
- Several specific measures will address taxpayer protection. First, Treasury-OFS will seek to have a clean audit opinion on its financial statements. In addition, the financial return for each program will be evaluated against its benchmark (subsidy rate). Finally, Treasury-OFS will report performance data on how oversight issues are addressed and resolved.
- Several indicators will measure performance on promoting transparency. First, Treasury-OFS will track on-time reporting performance. Second, Treasury-OFS will measure the degree of user satisfaction with the TARP's website, www.financialstability.gov, to determine areas for improvement. Finally, a request response index will be created to provide the public with a clear measure of timely performance.

Section Seven: Financial Accounting Policy

Under TARP, Treasury-OFS has made equity investments, loans and asset guarantees in a range of financial institutions. In exchange for these investments, loans, and asset guarantees, Treasury-OFS, on behalf of the taxpayer, has received financial instruments – equity, debt and warrants – from these companies. In this report, Treasury-OFS is presenting a transparent accounting of the current estimated cost of TARP, which reflects estimates of the value of those investments, loans and asset guarantees. Treasury-OFS has developed and presented the estimates in a way that is consistent with the statutory reporting requirements.

The statutory reporting requirements for TARP in this area are in some respects unique. Under EESA,Treasury-OFS is required to determine the budgetary cost of TARP under the general framework of credit reform. Treasury-OFS has determined it was appropriate to also use the credit reform framework for financial reporting purposes. EESA also requires that the budgetary cost of TARP programs be determined using a methodology that incorporates market risk. This requirement means that TARP equity investments similar to those that are publicly traded are valued in a way that is analogous to the "fair value" standard that private sector firms are required to use.

This section explains the applicable reporting requirements, discusses how Treasury-OFS has met the requirements, and describes how this reporting methodology relates to commercial reporting concepts.

Applicable Budget and Accounting Standards

The Emergency Economic Stabilization Act of 2008 (EESA) requires that the cost of troubled assets purchased or guaranteed be determined for budgetary accounting purposes in accordance with the Federal Credit Reform Act of 1990 (FCRA). EESA also requires that the cost calculations be adjusted for market risk.

FCRA established a methodology for budgeting for loans or loan guarantees issued by the federal government. Under the FCRA, the budgets for loans and loan guarantee programs reflect the expected cost of these financial arrangements, rather than just the cash flows as is typically the case for federal budgeting. For example, when a federal agency enters into a loan guarantee, no actual cash outflow from the government typically occurs, however, the cash outflows and the expected cost over the life of the guarantee may be substantial. In contrast, when a federal agency provides a loan, there is a substantial cash outflow at loan origination, but the ultimate cost of that loan to the government will depend on future repayments.

Rather than using a cash basis for credit programs, which can be misleading, the FCRA calls for agencies to record the "subsidy" cost of a loan or loan guarantee at the time of the disbursement of the loan or loan. The subsidy cost is the net present value of all cash flows associated with the credit transaction, usually calculated by discounting all payments back to the current period at the appropriate Treasury rate. Subsidy estimates reflect both the terms of the underlying instrument and the likelihood of repayment. For example, if a loan carries a rate below the comparable Treasury rate, that loan will generate a subsidy cost even if the loan is expected to be fully repaid. The subsidy calculation also reflects the risk that the borrower may not repay the entire amount of the loan. The potential for less than full repayment is reflected in the *expected* cash flows, which should reflect historical defaults on similar instruments, and assumptions about possible future economic performance.

The original subsidy cost estimate made at the time the transaction occurs is updated each year to reflect the actual cash flows that occurred as well as any changes in the expected future repayments from the borrower.

EESA mandated that the FCRA be used to determine the cost of all TARP investments for budgetary purposes, although the FCRA as originally designed did not cover equity investments. Treasury-OFS concluded that it was appropriate to apply FCRA to its preferred stock purchases since preferred stock has a dividend rate and regularly scheduled dividend payments, similar to debt instruments.

The Federal Accounting Standards Advisory Board (FASAB) has promulgated extensive accounting guidance that establish Federal accounting practices for loans and guarantees consistent with the FCRA method of budgeting for credit programs. TARP investments in direct loans, such as those to the auto industry, and asset guarantees are covered by existing accounting standards. Specifically Statement of Federal Financial Accounting Standards 2, *Accounting for Direct Loans and Loan Guarantees* (SFFAS 2) provides relevant accounting guidance for direct loans and loan guarantees issued by federal entities and closely parallels the FCRA provisions. Federal entities must record loans disbursed as an asset, valued at the net present value of expected future cash inflows. The difference between the amount disbursed and the net present value of expected cash inflows for loans is recorded as a subsidy cost at the time of the loan disbursement. Federal entities must book outstanding guarantees as an asset or a liability, valued at the net present value of the expected future cash flows, with the corresponding amount reflected in subsidy cost. Estimates of future cash flows are revised on an annual basis with changes reflected as an increase or decrease in the subsidy allowance and reflected in the Statement of Net Costs.

FASAB standards do not cover equity investments by federal entities in private enterprises as the Federal government generally does not make these types of investments. Consistent with the accounting policy for equity investments made by Treasury in private entities, Treasury-OFS accounts for its equity investments at fair value, defined as the estimated amount of proceeds Treasury-OFS would receive if the equity investments were sold to a market participant. Treasury-OFS uses the present value accounting concepts embedded in SFFAS No.

2 to derive fair value measurements. Treasury-OFS concluded that the equity investments were similar to direct loans in that there is a stated interest rate and a redemption feature which, if elected, requires repayment of the amount invested. Furthermore, the EESA requirement to consider market risk provides a basis to arrive at a fair value measurement. Therefore, Treasury-OFS uses SFFAS No. 2 for reporting and disclosure requirements of it equity investments. Treasury-OFS accounts for the warrants received under Section 113 of EESA as fees under SFFAS No. 2, as such the value of the warrants is a reduction of the subsidy allowance.

Market Risk

EESA departed from the FCRA by requiring that an adjustment for market risk be made to the interest rate used to discount future expected cash flows rather than using the interest rate on comparable maturity Treasury debt as the FCRA requires. This distinction values the TARP equity investments as closely as possible to how they would be priced in private markets. The incorporation of market risk is a departure from the standard FCRA methodology and is an important factor in the valuations included in the Treasury-OFS financial statements. The loan and asset guarantee models include an adjustment for market risk which is intended to capture the risk of unexpected losses, but is not intended to represent fair value.

TARP holds a variety of investments. The Citigroup common stock is a standard financial instrument that trades in public markets and has a market price that can be directly observed. Certain other TARP investments are closely related to tradable securities. Wherever possible, Treasury-OFS has sought to use market prices of traded equity securities in estimating the fair value of TARP equity investments.

Most TARP equity investments do not have direct analogs in private markets so Treasury-OFS uses internal market-based models to estimate the fair value of these investments. These models have been benchmarked to actual securities with observable market prices to try and ensure, to the maximum extent possible, that the model's results actually reflect how the private markets are pricing risk. As described in Section Eight [Valuation], the valuation of the Treasury-OFS' equity investments comes as close as possible to how private financial markets would price those instruments.

Comparison to Commercial Reporting Concepts

While commercial reporting standards vary, fair value is the most common valuation approach for reporting relatively liquid equity investments like preferred stock. For Treasury-OFS, adjusting our estimates to reflect market risk ensures that the asset values reflect a reasonable assessment of fair value, which can be readily compared and evaluated based on commercial investment information.

Section Eight: TARP Valuation Methodology

This section describes the methodologies used to estimate the value of the diverse set of TARP investments made under EESA. Wherever possible, Treasury-OFS has sought to use market prices of tradable securities to make direct estimates of the market value of TARP investments. Use of market prices was possible for TARP investments that are standard financial instruments that trade in public markets or are closely related to tradable securities. For those TARP investments that do not have direct analogs in private markets, Treasury-OFS uses internal market-based models to estimate the market value of these investments as detailed below.

Incorporating "Market Risk" in Valuation Models

Risk can be taken into account in a number of ways when estimating the value of an asset. EESA requires that the budgetary cost and risk of troubled assets acquired under TARP be estimated in accordance with the Federal Credit Reform Act of 1990 (FCRA) and using a market adjusted discount rate. Where possible, market prices are used to benchmark the values of TARP investments.

The standard methodology under FCRA is to estimate asset values as the net present value of *expected* cash flows, using Treasury rates for discounting. In that approach, risk is reflected in the expected cash flows. For example, default risk on a loan would be reflected in the fact that the expected cash flows are less than the contractual obligations.

EESA also requires for budgetary purposes that the FCRA methodology be modified to include an adjustment for market risk. Specifically, EESA requires that instead of discounting future expected cash flows at the interest rate on comparable maturity Treasury debt, an additional adjustment for market risk must be made. For financial reporting purposes, the market risk is incorporated in the future expected cash flows.

In effect, the requirement to adjust the standard FCRA methodology to reflect "market risk" means that for the purposes of budget and accounting, TARP equity investments are valued as closely as possible to how they would be priced in private markets. This requirement is relatively easy to implement for TARP investments that are closely related to securities with observable market prices. However, where empirical models are needed to estimate the value of non-standard TARP investments those models must be benchmarked to ensure, to the extent possible, that their results reflect the way public markets price risk. This benchmarking is an important part of valuation methodology.

The adjustment for "market risk" can be reflected in either expected cash flows or the discount rate used to calculate net present values. Regardless of where the adjustment is made, it should not have a material impact on the results as long as those models are benchmarked to suitable measures of market risk in an appropriate manner.

CPP Investments

Under the CPP as detailed in Section Three [Ensuring Stability], Treasury-OFS has provided capital to 685 qualified financial institutions and received preferred stock and warrants in return. To estimate the value of these investments, Treasury-OFS has built two separate statistical models: one to value the preferred stock and one to value the warrants. Both valuation models use standard methods employed in academe and the financial sector. An important aspect of these models is the treatment of the implicit options embedded in the assets; i.e., the financial institution's decision to repurchase the asset and Treasury-OFS' decision to exercise the warrants. These models make use of a variety of information, including historical and current information on the institution's balance sheets, the term-structure of interest rates, and equity prices and dividends.

The estimated values of CPP preferred equity investments are the net present values of the expected dividend payments and repurchases. The model is used to estimate the likely distribution of dividend payments over time. Estimates of the ultimate cost of TARP will decline further if early repayments are higher than those currently built into the models. It is assumed that the key decisions that affect whether or not banks pay their preferred dividends are made by each bank based on the strength of their balance sheet. The model assumes a probabilistic evolution of each bank's asset to liability ratio. Each institution's assets are subject to uncertain returns and institutions are assumed to manage their asset to liability ratio in such a way that it reverts over time to a target level. Historical volatility is used to scale the likely evolution of each banks' assets-to-liabilities ratio.

In the model, when equity decreases, i.e. the asset-to-liability ratio falls; institutions are increasingly likely to default, either because they enter bankruptcy or are closed by regulators. The probability of default is estimated based on the performance of a large sample of US banks over the period 1990-2008. At the other end of the spectrum, institutions call their preferred shares when the present value of expected future dividends exceeds the call price; which occurs when equity is high and interest rates are low.

The warrants for the purchase of common stock are priced using an option-pricing model augmented for the fact that exercising warrants infuses cash into an institution and also dilutes current stockholders. The model assumes optimal warrant exercise by Treasury-OFS; that is, the warrants are exercised if the expected present value of income from future optimal warrant exercise is less than the current in-the-money value. The key input to the model -- the future volatility of bank stock prices -- is derived from the model for preferred stock.

The basic preferred equity model is benchmarked to the market pricing of risk. The model was used to estimate the value of preferred equity instruments issued by 18 of the CPP banks that trade actively in public markets. These particular instruments were chosen because they share important characteristics with the CPP instruments. In particular, these traded instruments have very long maturities and are callable. The stochastic assumptions that drive the evolution of bank balance sheets in the model were then adjusted so the model's valuation of this portfolio of tradable securities matched the observed market prices.

The only other adjustment to the model relates to the banks' repurchases of preferred securities from Treasury-OFS. Treasury-OFS management, based on public statements by individual banks, believes that a significant volume of CPP and TIP preferred shares is likely to be repaid earlier than the model predicts. To reflect this judgment, the model is adjusted to generate approximately $70 billion in CPP and TIP repurchases over the next twelve to eighteen months.[9]

Treasury-OFS exchanged the CPP preferred shares purchased from Citigroup for common stock. The exchange rate was $3.25 per share resulting in Treasury-OFS obtaining approximately 7.7 billion shares. The value of these shares is the amount of shares held times its market price.

TIP

Treasury-OFS provided funds to both Citigroup and Bank of America under the Targeted Investment Program through the purchase of additional preferred shares. These investments are valued in the same manner that Treasury-OFS uses to value CPP investments in large institutions. As noted above, the model assumes $70 billion in CPP and TIP repurchases.

AIG Investment Program

The method used to value AIG preferred shares is broadly analogous to the approach used to value CPP investments. However, greater uncertainty exists for the valuation of preferred shares for AIG. First, the size of Treasury-OFS' holding of preferred shares relative to AIG's total balance sheet makes the valuation extremely sensitive to assumptions about the recovery ratio for preferred shares should AIG enter default. Second, no comparable traded preferred shares exist. Therefore, Treasury-OFS based the AIG valuation on the observed market values of publicly traded assets on either side of the liquidation preference of the preferred stock; common

[9] Without this adjustment the CPP preferred equity model predicts roughly $20 billion in repurchases over the next year. The valuation model is altered both by directly imposing the repurchases of those institutions that have stated plans to repurchase soon, and by adding a small additional benefit for any institution that repays its TARP funds and exits the CPP. This adjustment increases rates slightly to be consistent with a reasonable forecast of future repurchases.

stock (paid after preferred stock), and the most junior subordinated debt (paid before preferred stock). Further, based on certain publicly available third party sources, assumptions about payouts in different outcomes and the probability of some outcomes were made. Finally, external asset managers provided estimated fair value amounts, premised on public information, which also assisted Treasury-OFS in its valuation. These different factors were all used in determining the best estimate of the fair value of AIG assets. The AIG Investment Program also includes an equity capital facility that can be drawn upon at the discretion of AIG.

AIFP

The valuation of equity-type investments was performed in a manner that is broadly analogous to the methodology used for CPP investments, with reliance on publicly traded securities to benchmark the assumptions of the valuation exercise. Debt with potential value is valued using rating agency default probabilities.

As part of the General Motors (GM) bankruptcy proceedings, Treasury-OFS received a 60.8 percent stake in the common equity of General Motors Company (New GM). Because the unsecured bond holders in General Motors Corporation (Old GM) received 10 percent of the common equity ownership and warrants in New GM, the expected recovery rate implied by the current trading prices of the Old GM bonds provides the implied value of the New GM equity. Treasury-OFS used this implied equity value to account for its equity stake in New GM.

For the GMAC equity instruments, Treasury-OFS used the model to estimate the value of GMAC subordinated debt that trades actively in public markets. The stochastic assumptions that drive the evolution of the institution's balance sheet in the model were then adjusted so the model's valuation of this security matched the observed market price.

Treasury-OFS values direct loans using an analytical model that estimates the net present value of the expected principal, interest, and other scheduled payments taking into account potential defaults. In the event of a financial institution's default, these models include estimates of recoveries, incorporating the effects of any collateral provided by the contract. The probability of default and losses given default are estimated by using historical data when available, or publicly available proxy data, including credit rating agencies historical performance data.

Treasury-OFS also benchmarks the valuation of its holdings of auto securities against the assumptions about the dynamics of future revenues and costs provided by an inter-agency working group dealing with the automotive industry.

TALF

Under the TALF program, Treasury-OFS will provide funding of up to $20 billion as necessary for the purchase of TALF collateral through a direct loan to a Special Purpose Vehicle (SPV). The SPV collects monthly interest spreads on all outstanding TALF loans, as well as any income or sale proceeds from purchased collateral. When the program is wound down, Treasury-OFS will be repaid principal and interest on the loan if funds are available, and will collect 90 percent of any proceeds remaining in the SPV. The value of the Treasury-OFS' loan to the TALF SPV is the estimated net present value of the expected principal, interest, and additional proceeds.

To derive the cash flows to the SPV, and ultimately, Treasury-OFS, the model simulates the performance of underlying collateral. Loss probabilities on the underlying collateral are calculated based on analysis of historical loan loss and charge off experience by credit sector and subsector. Historical mean loss rates and volatilities are significantly stressed to reflect recent and projected performance. Simulated losses are run through cash flow models to project impairment to the TALF eligible securities. Impaired securities are projected to be purchased by the SPV, requiring additional Treasury-OFS funding. Simulation outcomes consisting of a range of loss scenarios are probability-weighted to generate the expected net present value of future cash flows.

AGP

Under the AGP, Treasury-OFS received preferred shares and warrants in exchange for providing a guarantee on a pool of Citigroup's assets. The value of the AGP preferred shares and warrants is determined in exactly the same manner that Treasury-OFS uses to value CPP investments in large institutions. The cost that Treasury-OFS expects to incur is based on projected losses on the asset pool under a weighted average of different possible loss scenarios.

The value of the AGP is the discounted expected cash inflows from the preferred shares and warrants less the expected costs of the TARP expenditures to make good on the asset pool guarantees and adjusted for market risk.

Sensitivity Analysis

The ultimate value of TARP investments will only be known in time. Realized values will vary from current estimates in part because economic and financial conditions will change. Many TARP investments do not have readily observable values and their values can only be estimated by Treasury-OFS.

Sensitivity analysis is one way to get some feel for the degree of uncertainty around the Treasury-OFS estimates. In the analysis reported here, Treasury-OFS focuses on the largest components of the TARP, the assets held under the Capital Purchase Program (CPP), as well as preferred stock investments made under the Targeted Investment Program (TIP). Second, the Treasury-OFS focuses on two of the most important inputs to the valuation: i) whether and when the banks repay the preferred stock, and ii) whether there are changes in the market price of publicly-traded preferred stock used as a benchmark for valuing the preferred stock held in the TARP.

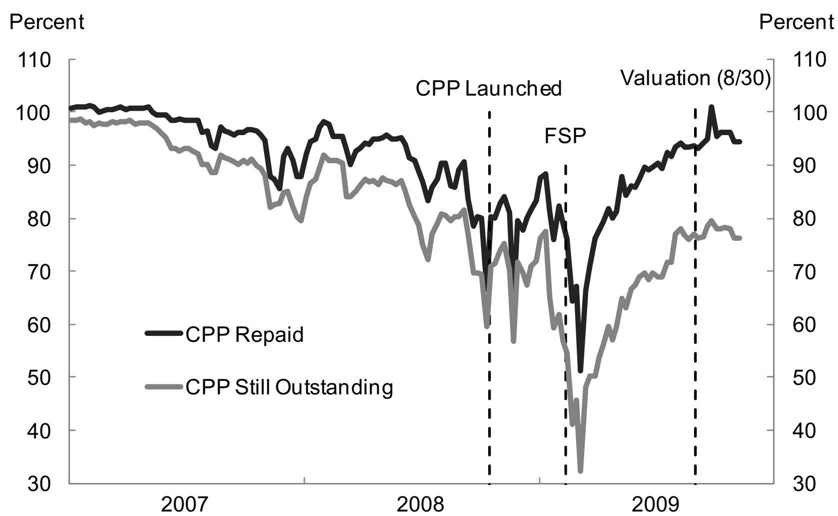
Prepayments: The CPP preferred stock carries a 5 percent dividend, which increases to 9 percent after 5 years. Banks able to repay would be likely to do so at the 5-year point. However, some banks have repaid early. Over $70 billion of the $204 billion of preferred stock has already been repaid. The model forecasts additional repayments over the next 18 months of $19.5 billion. Treasury-OFS increased that forecast by $50 billion for CPP and TIP combined to reflect additional anticipated repayments over the next 12 months. As a sensitivity analysis, Treasury-OFS computed the CPP and TIP values without the additional $50 billion of anticipated repayments. The result is shown in Scenario 1 of Table 1.

Benchmark Preferred Stock: The valuation procedure entails observing the market price of publicly-traded preferred stock and calibrating the model (in particular the risk premium) to match those prices. The calibrated model is then used to price the non-publicly traded preferred stock held by the TARP. The benchmark preferred stock consists of a portfolio of claims issued by some of the same institutions with TARP preferred stock. It is generally the larger institutions that have issued preferred stock. The TARP preferred stock for smaller institutions may not be exactly comparable, but the bulk of TARP investments, as measured on a dollar basis, are in large institutions.

The preferred stock calibration procedure imposes a strict discipline on the model. If one parameter in the model is changed, calibration to the market benchmark will induce an offsetting change in other parameters, with the result that the final valuation is not altered much. Changes in the price of the benchmark, however, have the potential to significantly alter the valuations. As a sensitivity analysis, Treasury-OFS increases and decreases the value of the benchmark preferred stock in the CPP and TIP by 10 percent. The result is shown in Scenarios 2 and 3 of the following table.

To put this sensitivity analysis in perspective it is useful to consider the range over which actual preferred shares have moved in this crisis. Figure 15 shows the prices of callable preferred shares of those CPP banks that have such instruments outstanding. Since their troughs in early March, these shares have recovered substantially. Currently the basket of callable preferred shares for CPP banks is trading at about 76 percent of their call prices which leaves opportunity for further improvement. Of course just last March these instruments were trading for less than half their current value. This considerable volatility, along with the sensitivity analysis presented here, gives a good sense of the degree of unavoidable uncertainty around the estimates of the valuation of TARP investments presented here.

Figure 15: Prices of Callable Preferred Shares Issues by CPP Banks, (Percent of Call Price)



Note: Weighted averages of prices of callable preferred shares issued by three CPP banks that have already repaid their TARP capital injections and 14 CPP banks that have not. Prices are expressed as a percent of the call price. Source Bloomberg.

76

Program	Market Value Sensitivity (Dollars in Billions)			
	Current Market Value [1]	Scenario 1	Scenario 2	Scenario 3
	Additional Repayments[2]	No Additional Repayments	10% Financial Stock Price Increase	10% Financial Stock Price Decrease
CPP	133.0	127.7	141.8	123.7
% change from current	*N/A*	*-4.03%*	*6.58%*	*-7.01%*
TIP	38.6	36.3	39.8	37.4
% change from current	*N/A*	*-5.96%*	*3.05%*	*-2.98%*
Total	171.6	164.0	181.5	161.1
% change from current	*N/A*	*-4.46%*	*5.78%*	*-6.10%*

[1] The difference between the values contained in this table and the financial statements is that the financial statement values include the warrants.

[2] Assumes $70 billion in repayments over the next 12 to 18 months.

Other Sources of Sensitivity

Wherever possible, Treasury-OFS has used direct market proxies to estimate the value of TARP investments. The volatility of the market prices of the related securities is an important indicator of the uncertainty of our estimates of what the returns on TARP investments ultimately will be. For example, the price of Citigroup common shares has fluctuated in a range from $2.6 to $5.2 per share just since the SCAP results were announced in early May.

77

Section Nine: Systems, Controls, and Legal Compliance

Management Assurance Statement

The Treasury Office of Financial Stability's (Treasury-OFS) management is responsible for establishing and maintaining effective internal control and financial management systems that meet the objectives of the Federal Managers' Financial Integrity Act (FMFIA), 31 U.S.C. Section 3512(c), (d). Treasury-OFS has evaluated its management controls, internal controls over financial reporting, and compliance with the federal financial systems standards. As part of the evaluation process, Treasury-OFS considered the results of extensive documentation, assessment and testing of controls across Treasury-OFS, as well as the results of independent audits. Treasury-OFS conducted its reviews of internal controls in accordance with the FMFIA and the Office of Management and Budget (OMB's) Circular A-123, Management's Responsibility for Internal Control.

As a result of its reviews, Treasury-OFS management concludes that the management control objectives described below, taken as a whole, were achieved as of September 30, 2009. Specifically, this assurance is provided relative to Sections 2 (internal controls) and 4 (systems controls) of FMFIA. Treasury-OFS further assures that the financial management systems relied upon by Treasury-OFS are in substantial compliance with the requirements imposed by the Federal Financial Management Improvement Act (FFMIA). Treasury-OFS does not rely on any financial systems beyond those maintained by the Department of the Treasury and Fannie Mae.

Treasury-OFS' internal controls are designed to meet the management objectives established by Treasury and listed below:

a) Programs achieve their intended results effectively and efficiently;
b) Resources are used consistent with the overall mission;
c) Programs and resources are free from waste, fraud, and mismanagement;
d) Laws and regulations are followed;
e) Controls are sufficient to minimize any improper or erroneous payments;
f) Performance information is reliable;
g) Systems security is in substantial compliance with all relevant requirements;
h) Continuity of operations planning in critical areas is sufficient to reduce risk to reasonable levels; and
i) Financial management systems are in compliance with federal financial systems standards, i.e., FMFIA Section 4/FFMIA.

In addition, Treasury-OFS management conducted its assessment of the effectiveness of internal control over financial reporting, which includes safeguarding of assets and compliance with applicable laws and regulations, in accordance with OMB Circular A-123, Management's Responsibility for Internal Control, Appendix A, Internal Control over Financial Reporting.

Based on the results of this evaluation, Treasury-OFS provides unqualified assurance that internal control over financial reporting is appropriately designed and operating effectively as of September 30, 2009, with no related material weaknesses noted.

Sincerely,

Herbert M. Allison, Jr.

Assistant Secretary for Financial Stability

Internal Control Program

The Emergency Economic Stabilization Act (EESA) established the Office of Financial Stability (Treasury-OFS) on October 3, 2008. Shortly thereafter, Treasury-OFS funded $115 billion to eight financial institutions as part of the Capital Purchase Program. From the inception of that initial program to the current day, the importance of effective internal controls in safeguarding the use of taxpayer dollars to provide financial stability through the Troubled Asset Relief Program (TARP) has remained a top priority of Treasury-OFS management.

Whether deploying operational processes to support new TARP programs or implementing complex budget and financial reporting processes to support its first year of operations, Treasury-OFS endeavors to establish an effective initial operating capability for internal controls that are first and foremost effective at mitigating risk. Then, Treasury-OFS enhances the initial operating capability to a sustainable level that is effective and efficient, and designed to meet the long-term needs of its programs.

Treasury-OFS is committed to implementing an effective internal control program and has established a Senior Assessment Team (SAT) to guide the office's efforts to meet the statutory and regulatory requirements surrounding a sound system of internal control. The SAT is chaired by the Deputy Chief Financial Officer (DCFO) and includes representatives from all Treasury-OFS functional areas. Further, Treasury-OFS has defined an Internal Control Framework that is based on the principles of The Committee of Sponsoring Organizations of the Treadway Commission (COSO). The SAT leverages this framework in communicating control objectives across the organization and its third party service providers.

Treasury-OFS established an Internal Control Program Office (ICPO) under the Office of the Chief Financial Officer that is guided by the SAT and focuses on managing the office's internal control efforts. The ICPO monitors the implementation of the Internal Control Framework and ensures the achievement of management control objectives. The ICPO monitors Treasury-OFS activities to ensure management control objectives are achieved by:

- Integrating management controls into Treasury-OFS business processes through:
  - Developing internal control documentation,
  - Reviewing internal control responsibilities with process owners before major program execution events, and,
  - Real-time monitoring of key control effectiveness during and after significant program execution events;
- Conducting "lessons learned" sessions to identify and remediate areas requiring improvement;
- Periodic testing of key controls; and,
- Monitoring feedback from third party oversight bodies.

In addition, the internal control environment supporting TARP programs and Treasury-OFS activities undergoes continuous improvement to remain effective and is subject to significant third party oversight by the Government Accountability Office (GAO) and the Special Inspector General for the Troubled Asset Relief Program (SIGTARP).

The Assistant Secretary for Financial Stability must report annually to the Under Secretary for Domestic Finance on the adequacy of the various internal controls throughout the Office of Financial Stability, to include financial management systems compliance. The Assurance Statement is required by the Federal Managers' Financial Integrity Act (FMFIA). In order to support the Assistant Secretary's letter of assurance, the respective Treasury-OFS divisions prepare individual statements of assurance. These individual statements of assurance provide evidence supporting the achievement of Treasury-OFS-wide internal control objectives and disclose any noted weaknesses.

Information Technology Systems

For fiscal year 2009, Treasury-OFS did not directly support any Information Technology (IT) systems. Significant IT systems used by TARP are supported by various Departmental Offices or bureaus that are part of Treasury.

Other IT systems are supported by Financial Agents which provide services to the U.S. Treasury. The Financial Agency Agreements maintained by the Treasury Office of the Fiscal Assistant Secretary in support of Treasury-OFS require the Financial Agents to design and implement suitably robust IT security plans and internal control programs, to be reviewed and approved by the Treasury at least annually.

Compliance with the Improper Payments Information Act (IPIA)

The elimination of improper payments is a major focus of Treasury-OFS executive management. Managers are held accountable for developing and strengthening financial management controls to detect and prevent improper payments, and thereby better safeguard taxpayer dollars.

Treasury-OFS carried out its fiscal year 2009 IPIA assessment per Treasury-wide guidance and did not identify any programs or activities susceptible to significant erroneous payments. Treasury-OFS did not identify any payments to incorrect payees or ineligible recipients. Management will continue to monitor disbursements and re-assess IPIA compliance as new programs are initiated.

Areas for Improvement

Over the next year, Treasury-OFS management is focused on enhancing the maturity of its internal control environment in several key areas as follows:

- Because of limited staffing and competing priorities among the various compliance activities and TARP programs, independent monitoring of contract requirements for TARP programs has been constrained. Treasury-OFS has been challenged to develop sufficient resources to respond to the number of requirements imposed by TARP programs, the large number of participants in those programs, and recommendations by the oversight entities. Management is building the personnel resources to aggressively address a number of compliance priorities, including, for example, monitoring the Treasury-OFS contract compliance status of CPP recipients' compliance.
- The system of record used to manage the Home Affordable Modification Program (HAMP) requires increased functionality to meet the control requirements of the

program. Weaknesses in these systems are currently mitigated by our detective internal controls. However, management recognizes that these system shortfalls must be addressed in the near term, as the volume and complexity of these system functions increase.

- EESA required the preparation of stand-alone financial statements that would be audited by the GAO. As a new entity, neither Treasury-OFS nor our GAO auditors had previously been through the statement preparation and auditing process for this complicated entity. An additional complication resulted from EESA and OMB's interpretation of the statute to require the application of complex accounting required by the Federal Credit Reform Act of 1990 (FCRA) to all of the Treasury-OFS acquisitions (i.e. equities, loans and asset guarantees).

  Given these facts, Treasury-OFS faced a number of challenges, including a shortage of experienced credit reform staff and evolving and untested financial reporting processes and controls. Given the pace and evolution of the TARP programs throughout the year and subsequent impact on the accounting and financial reporting areas, certain accounting practices continued to evolve throughout the period ended September 30, 2009. In an effort to keep pace with these changes, management continues to focus its attention on the development of robust processes that meet business needs and internal control requirements. In developing its accounting processes and controls, management has sought to balance effective risk mitigation, flexibility to respond to new programs, and efficiency through shared resources. Accordingly, the maturation and formalization of financial capabilities and controls will continue into fiscal year 2010.

- As noted in Section Seven, EESA mandated that the FCRA be used to determine the cost of all TARP investments for budgetary purposes. The FCRA calls for agencies to record the "subsidy" cost of an investment at the time of the disbursement, which requires the use of detailed models following the methodology described in Section Eight. Due to a compressed timeframe, management was not able to execute the planned controls around manual data inputs in the credit subsidy models in such a manner so as to prevent non-material errors from occurring in the final re-estimate production process. Significant errors identified were corrected and amounts were properly reflected in the financial statements. In year one, our internal controls over data inputs were intended to provide full coverage of the models, but of necessity our resources focused more on the high risk programs and items. In fiscal year 2010, we will focus more attention on improving internal control effectiveness in mitigating the risk of errors in data inputs for all models.

Oversight Entities

Per the EESA requirements, Treasury-OFS has four oversight entities with specific responsibilities with regard to TARP, which are the Financial Stability Oversight Board, the GAO, the Special Inspector General for TARP, and the Congressional Oversight Panel. A summary of the responsibilities and activities of each of these entities is provided below.

Financial Stability Oversight Board

The Oversight Board was established by section 104 of the EESA to help oversee the Troubled Asset Relief Program and other emergency authorities and facilities granted to the Secretary of the Treasury under the EESA. The Oversight Board is composed of the Secretary of the Treasury, the Chairman of the Board of Governors of the Federal Reserve System, the Director of the Federal Housing Finance Agency, the Chairman of the Securities and Exchange Commission, and the Secretary of the Department of Housing and Urban Development. Through Oversight Board meetings and consultations between the staffs of the agencies represented by each Member of the Oversight Board, the Oversight Board reviews and monitors the development and ongoing implementation of the policies and programs under TARP to restore liquidity and stability to the U.S. financial system. The Oversight Board meets each month, and receives presentations and briefings from Treasury officials and, where appropriate, other government officials, including officials from the other agencies represented on the Oversight Board, concerning the implementation and the effects of the programs established under TARP.

The Oversight Board also monitors Treasury's responses to the recommendations made by SIGTARP and the GAO. Throughout FY 2009, the Oversight Board received updates on Treasury's progress in addressing the issues raised by these oversight bodies with respect to transparency, the establishment of internal controls, compliance and risk monitoring, staffing and Treasury's communication strategy. In addition, staff of the Oversight Board and of the agencies represented by each Member of the Oversight Board continued to have regular discussions with representatives from the SIGTARP and GAO to discuss recent and upcoming activities of the oversight bodies. These efforts continued to help facilitate coordinated oversight and minimize the potential for duplication.

The Oversight Board issues a Quarterly Report for each three-month period. Copies of approved minutes of the Oversight Board's meetings and the Quarterly Reports are made available on the internet at: http://www.financialstability.gov/about/oversight.html.

GAO

Section 116(a)(3) of EESA stipulates that "the Comptroller General [who heads the GAO] shall submit reports of findings … regularly and no less frequently than once every 60 days, to the appropriate committees of Congress." "The Comptroller may also submit special reports … as warranted by the findings of its oversight activities."

Treasury-OFS has a statutory obligation under Section 116(b)(3) of EESA to take corrective actions in response to audit deficiencies identified by the Comptroller General or other auditor engaged by the TARP or certify to the appropriate committees of Congress that no action is necessary or appropriate. In addition, under Section 236 of the Legislative Reorganization Act of 1970, Treasury is required to respond in writing to Congress within 60 days of the issuance date of a GAO report.

Currently, the GAO is engaged in eight audits related to TARP. Treasury-OFS responds to information requests from the GAO by providing responsive documents and other information and facilitating comprehensive briefings on TARP programs with senior Treasury staff. In addition, Treasury-OFS apprises the GAO of key developments in current and proposed programs and policies under EESA.

To date, the GAO has issued 41 recommendations in its reports issued in December 2008 and January, March, June, July, October, and November 2009. The recommendations have focused on the following themes: (1) transparency, reporting, and accountability; (2) management infrastructure; and (3) communication. In response to the recommendations, the Treasury-OFS has developed remediation plans and actively communicates the status of its remediation efforts to the GAO and will continue to do so in FY 2010. Treasury-OFS has fully or partially implemented 32 of the recommendations and has responded or is in the process of responding to six recommendations; the remaining recommendations have been deemed closed by the GAO and/or Treasury-OFS has taken no action.

Treasury-OFS' actions in response to GAO recommendations include:

- Treasury-OFS delivered draft internal controls policies and procedures to GAO on June 30, 2009. Many of the final policies and procedures were delivered to GAO on September 30, 2009. The bulk of the remainder of the Treasury-OFS policies and procedures will be delivered by December 31, 2009.
- Treasury-OFS has completed draft risk assessments of TALF, CPP, HAMP, contracting and human resources. Plans have been developed for high risk areas.
- Treasury-OFS continues to expeditiously hire personnel to carry out and oversee HAMP as well as finalizing a comprehensive system of HAMP internal controls.

Additional detail regarding Treasury-OFS's progress on the GAO's recommendations can be found at http://www.financialstability.gov/docs/SummaryResponseGAO10-8-2009.pdf.

84

SIGTARP

SIGTARP was created by section 121 of EESA. The objectives of SIGTARP are to investigate and prevent fraud, waste and abuse in TARP programs, while trying to promote transparency in TARP programs.

SIGTARP must report to Congress each quarter certain information about TARP over the preceding quarter. As of September 30, 2009, SIGTARP has issued three quarterly reports in February 2009, April 2009 and July 2009. SIGTARP also has a duty under EESA to conduct audits and investigations of the purchase, management, and sale of assets under any TARP program, and with certain limitations, any other action under EESA. As of September 30, 2009, SIGTARP has completed four audits and is currently conducting eleven audits that are at various stages.

Treasury-OFS has worked closely with SIGTARP and maintains regular lines of communications with the personnel conducting audits and investigations of TARP programs. Treasury-OFS staff also regularly provides updates to SIGTARP about program design and implementation issues. Treasury-OFS has benefited from their involvement in the development of TARP programs and policies as we pursue our common goal of carrying out the objectives of EESA, which are to promote financial stability and protect the interests of the taxpayers.

As of September 30, 2009, SIGTARP has issued 41 individual recommendations in their reports. General topics covered by SIGTARP's recommendations include reporting on use of TARP funds, valuation of the TARP portfolio, and potential fraud vulnerabilities associated with PPIP, TALF and HAMP. Treasury-OFS has given careful consideration to the recommendations in SIGTARP's prior reports, and has submitted responses detailing what actions that Treasury-OFS has taken or will take to address SIGTARP's recommendations. Treasury-OFS' policies and programs currently address many of the issues raised by SIGTARP in their recommendations, and in other cases Treasury-OFS took specific action to implement SIGTARP's recommendations. Treasury-OFS also has or will execute alternative approaches that we believe address some of the issues raised by SIGTARP in their recommendations. SIGTARP has closed 29 of its recommendations based on Treasury-OFS' response to the SIGTARP recommendations.

Congressional Oversight Panel

The Congressional Oversight Panel (COP)'s mandate includes assessing the impact of Treasury-OFS' spending to stabilize the economy, evaluating market transparency, ensuring effective foreclosure mitigation efforts, and guaranteeing that Treasury-OFS' actions are in the best interest of the American people.

The COP consists of five panel members appointed as follows: 1 member appointed by the Speaker of the House of Representatives; 1 member appointed by the minority leader of the House of Representatives; 1 member appointed by the majority leader of the Senate; 1 member appointed by the minority leader of the Senate; and 1 member appointed by the Speaker of the House of Representatives and the majority leader of the Senate, after consultation with the minority leader of the Senate and the minority leader of the House of Representatives. The COP also employs a professional staff, numbering approximately 27, who are responsible for carrying out the day-to-day work of the Panel. The COP also reaches out to experts, primarily academics, to conduct analysis in support of their work.

EESA requires the COP to produce a report every 30 days examining Treasury's efforts and the impact on the economy of those efforts. The statute grants the COP the authority to hold hearings, review official data, and write reports on actions taken by Treasury and financial institutions and their effect on the economy. Generally, the COP focuses on one program or topic each month and produces a report that describes the program, assesses its design and implementation and presents recommendations. Many of their recommendations have focused on issues of transparency and what they see as the need to operate the programs in a way that the public can understand exactly how their taxpayer dollars are being used.

The COP staff work in a fairly independent fashion, using publically available documents and information to develop the outlines of their reports. They also request information, documents, and data from Treasury-OFS. Treasury-OFS regularly briefs COP staff on the topic of their current focus, as well as any new initiatives or changes in Treasury-OFS programs.

The COP also convenes regular hearings on Capitol Hill, usually timed to coincide with the issuance of their reports. Treasury makes its senior staff available to appear before the COP as witnesses; the Secretary appears before the COP on a quarterly basis, and Assistant Secretary for Financial Stability Herb Allison is made available as requested for other hearings. Other Treasury officials have also appeared before the COP as requested.

To date, the COP has issued the following reports:

- Questions About the $700 Billion Emergency Economic Stabilization Funds
- Accountability for the Troubled Asset Relief Program
- Special Report on Regulatory Reform
- February Oversight Report: Valuing Treasury's Acquisitions
- Foreclosure Crisis: Working Toward a Solution
- Assessing Treasury's Strategy: Six Months of TARP

- Stress Testing and Shoring Up Bank Capital
- Lending to Small Businesses and Families and the Impact of the TALF
- TARP Repayments, Including the Repurchase of Stock Warrants
- Special Report on Farm Loan Restructuring
- The Continued Risk of Troubled Assets
- The Use of TARP Funds in Support and Reorganization of the Domestic Automotive Industry
- An Assessment of Foreclosure Mitigation Efforts After Six Months
- Guarantees and Contingent Payments in TARP and Related Programs

Section Ten: Other Management Information

Over the past year, Treasury-OFS has grown into an organization of 198 full-time employees (101 career civil servants, 85 term appointments, and 12 detailees) who support the TARP. These employees include 18 employees who report through the Department of the Treasury's Office of General Counsel and approximately 40 others outside of Treasury-OFS who continue to provide support to the office on an as-needed basis. Treasury-OFS continues to use direct-hire and other appointments to expedite hiring of highly-qualified candidates, which has enabled the Treasury-OFS to reduce the number of temporary and contract staff and strengthen the continuity and institutional knowledge of the workforce. The FY 2009 Administrative budget obligations totaled $248 million split between salaries and benefits of approximately $14 million and non-personnel services, generally contracts, of approximately $234 million.

As noted in Section One, Treasury-OFS is made up of seven divisions.

The Chief Investment Office (CIO) is responsible for program development and the execution and management of all investments made pursuant to EESA. Investments can be made by either purchasing or insuring "troubled assets" (as defined in EESA). The CIO relies on contracted asset managers and a custodian to assist in the management of acquired or insured assets. The CIO also manages a contract with an investment advisor who provides guidance on the selection of asset managers.

The Office of the Chief Financial Officer (CFO) has lead responsibility within Treasury-OFS for budget formulation and execution, cash management, accounting, financial systems, financial reporting, and internal controls. In each of these areas the CFO works closely with the appropriate offices within main Treasury. The CFO manages Treasury-OFS budget, cash flow requirements and accounting support activities for all of Treasury-OFS concentrating on accounting and reporting activities required by the Federal Credit Reform Act to include modeling of cash flow and all required re-estimates. The Office serves as liaison with Government Accountability Office (GAO) staff for financial statement reporting and internal controls. For the FY 2009 reporting cycle, the OCFO led the implementation of the OMB Circular A-123 internal controls requirements for Treasury-OFS.

The Office of the Chief of Homeownership Preservation is responsible for identifying opportunities to help homeowners while also protecting taxpayers. The key policy goals of the Office are to reduce the number of principal residences lost to foreclosure and to stabilize the value of homeownership in surrounding communities through polices which impact homeowners, home mortgage loans, lenders, servicers and their communities. The priorities of the Office are to: implement the Administration's loss mitigation program; develop and implement a robust outreach program targeted to at-risk homeowners; outline and implement strategies to regularly update the Administration, Congress, the public, and other key stakeholders, on results; and monitor, analyze and report on the results of the loan modification program.

The Office of the Chief Administrative Officer (OCAO) is responsible for developing an office infrastructure and managing internal operations in Treasury-OFS. The OCAO works to integrate Treasury-OFS investments, program, compliance, risk, finance, and legal functions and facilitates communication across the organization. The OCAO supports the execution of TARP programs and the management of the Treasury-OFS employees and contractual resources. The OCAO works with the Assistant Secretary for Financial Stability to set and execute goals and objectives. The OCAO works with each Treasury-OFS organizational entity to effectively manage the budget, facilities, information technology (IT), acquisition management oversight, document flows, physical security and privacy, and workforce planning.

The Office of the Chief Counsel provides legal advice to the Assistant Secretary. The Chief Counsel reports to the Assistant General Counsel (Banking and Finance) in Treasury's Legal Division. The Office of the Chief Counsel is responsible for the legal affairs of Treasury-OFS. The Office is involved in the structuring of Treasury-OFS programs and activities to ensure compliance with EESA and with other laws and regulations and to insure the programs and activities are well designed from a legal point of view. The Office assists in responding to FOIA requests, the inquiries of oversight bodies such as the GAO and the Congressional Oversight Panel (COP) and any litigation concerning EESA or Treasury-OFS activities. The Office also works on a variety of other legal matters pertaining to Treasury-OFS operations.

The Office of Reporting is responsible for coordinating Treasury-OFS' work with the external oversight entities including the GAO, Special Inspector General for TARP, Financial Stability Oversight Board and the Congressional Oversight Panel. The Office also prepares periodic reports to the Congress under EESA.

The Office of Internal Review (OIR) was recently established within Treasury-OFS to ensure that proper management controls are developed, in place, and operating as intended. Management controls include organization, policies, and procedures, all of which are designed to help program and financial managers achieve results and safeguard the integrity of their programs. The OIR also works with the other program offices to identify the most significant risks that the TARP faces including operational risk, credit risk, market risk, and reputational risk. The office assesses those risks (either quantitatively or qualitatively) and works to ensure that the assessments are integrated into the decision making processes of each business line of the TARP and that risks are managed in a consistent fashion across business lines. The OIR scope of responsibilities also covers the compliance oversight area including developing and implementing, in conjunction with the relevant program offices, processes and procedures to provide for overall program compliance with EESA. These include the HAMP program requirements, executive compensation, statutory reporting, and conflict of interest requirements.

Treasury-OFS is not envisioned as a permanent organization, so to the maximum extent possible and appropriate, Treasury-OFS utilizes private sector expertise in support of the execution of TARP programs. Fannie Mae and Freddie Mac accounted for almost thirty percent of the non-personnel services to assist in the administration and compliance, respectively, of the Home Affordable Modification Program. Additionally, asset managers were hired to serve as financial agents in managing the portfolio of assets associated with several TARP programs. The balance of the non-personnel private sector firms were engaged to assist with the significant volume of work associated with the TARP in the areas of accounting and internal controls, administrative support, facilities, legal advisory, financial advisory, and information technology.

Section Eleven: Limitations of the Financial Statements

The principal financial statements have been prepared to report the financial position and results of operations of the Treasury-OFS' Troubled Asset Relief Program, consistent with the requirements of 31 U.S.C. 3515(b). While the statements have been prepared from the books and records of the Office of Financial Stability and the Department of the Treasury in accordance with section 116 of EESA and GAAP for Federal entities and the formats prescribed by OMB, the statements are in addition to the financial reports used to monitor and control budgetary resources which are prepared from the same books and records.

The statements should be read with the realization that they are for a component of the U.S. Government, a sovereign entity.

Financial Statements

Message from the Chief Financial Officer

I am very pleased to submit the Office of Financial Stability's (OFS) Annual Financial Report for FY 2009. This report provides our stakeholders with meaningful financial results and program performance as required by the Emergency Economic Stabilization Act (EESA) and the Reports Consolidation Act. The unqualified audit opinion provided by our auditor, the Government Accountability Office (GAO), on these financial statements represents an extraordinary achievement by OFS and Treasury staff. The support of our contractors, staff at the Office of Management and Budget and the GAO audit team was invaluable to this success. I am exceptionally proud and appreciative of the effort and commitment made by everyone involved.

Under the EESA authority as described throughout this report, the government made unprecedented investments in private entities through the Troubled Asset Relief Program (TARP). The unique features of the EESA programs, as well as the statutory requirement that the budgetary cost of the programs be determined under the standards of the Federal Credit Reform Act (FCRA), adjusted for market risk, meant that OFS had to navigate unchartered ground in Federal budget and accounting concepts. For these and related reasons, creating the accounting and reporting infrastructure and internal control environment to support the development of the first year financial statements for the TARP, was an extraordinary challenge.

As a start up organization with an unprecedented emergency mission to stabilize the nation's financial system, OFS moved swiftly to develop and implement eight new programs. The face value of the amounts obligated for these programs in FY 2009 totaled $454 billion, nearly as much as the entire combined FY 2008 Federal non-defense discretionary outlays. OFS's budget, accounting, and financial reporting policies and operations had to be designed and executed simultaneously with the establishment of the new programs. OFS was able to leverage a number of Treasury's existing financial management systems and resources, but also had to develop procedures, reports, models, and methodologies from scratch.

All of the TARP initiatives except for the housing program are loans, guarantees or investments and are accounted for using FCRA methods of net present value for budgeting and financial reporting. Cost models (or "subsidy" models as they are called under FCRA) had to be developed for all of the programs and unique transactions. Never before has a Federal entity created as many subsidy cost models in such a short period made even more difficult by the vastness and complexity of TARP's programs. While we and GAO identified some non-material errors and opportunities for improvements in the models and processes, overall the results were outstanding, given the magnitude of the effort required this year. Because the credit and investment programs constitute the vast majority of OFS's financial activity, continuing to build a very strong internal control process and high quality, state of the art subsidy cost models is a top priority for us.

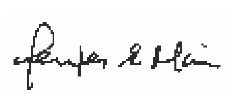
A consistent focus on internal control was a mainstay of OFS's efforts. From the first transactions in October, 2008, 23 days after passage of EESA, OFS instituted comprehensive controls around the highest risk elements of the transaction lifecycle – for example the disbursement and receipt of funds and receipt of appropriate consideration such as preferred shares and warrants associated with a transaction. OFS aggressively used prototyping to establish an effective process design, cross-functional meetings to ensure cohesion across areas, and real time control monitoring of all transactions to improve accuracy in execution. We focused on core controls such as appropriate levels of authorization and reconciliation of critical transaction information. Over the course of the year, we were able to maturate much of our internal control capacity from heavily monitored, individual transactions, to documented, repeated processes with embedded control monitoring, automated control evidence collection, and ongoing control testing.

Finally, OFS implemented the internal control requirements for financial reporting under Appendix A of OMB Circular A-123. OFS staff within the Office of the Chief Financial Officer worked closely with the program and other support offices to develop a comprehensive sub-certification and review process supporting management's interim and final assurance statements.

Looking ahead, we plan to continue improving our financial management capacity, including strengthening our financial reporting processes, developing additional or enhancing existing documentation supporting our policies, and formalizing our financial data management approach. We will be actively addressing GAO's audit findings and look forward to building on our successes this year to resolve the outstanding issues identified in this audit.

Successfully preparing the first year financial statements for the programs developed under the EESA required extraordinary dedication and commitment. It has been a privilege to lead this effort and I want to extend my thanks to the many people who contributed to making this endeavor successful.

Thank you for your interest in our FY 2009 Annual Financial Report.



Jennifer E. Main
Chief Financial Officer

Financial Statements and Notes

The OFS prepares financial statements for the Troubled Asset Relief Program as a critical aspect of ensuring the accountability and stewardship for the public resources entrusted to it and as required by Section 116 of EESA. Preparation of these statements is also an important part of the OFS' financial management goal of providing accurate and reliable information that may be used to assess performance and allocate resources. The OFS management is responsible for the accuracy and propriety of the information contained in the financial statements and the quality of internal controls. The statements are, in addition to other financial reports, used to monitor and control budgetary resources. The OFS prepares these financial statements from its books and records in conformity with the accounting principles generally accepted in the United States for federal entities and the formats prescribed by the Office of Management and Budget.

While these financial statements reflect activity of the OFS in executing its programs, including providing resources to various entities to help stabilize the financial markets, they do not include, as more fully discussed in Note 1, the assets, liabilities, or results of operations of commercial entities in which the OFS has a significant equity interest. In addition, comparative information is not available because OFS began operations on October 3, 2008.

The Balance Sheet summarizes the OFS assets, liabilities and net position as of the reporting date. Intragovernmental assets and liabilities resulting from transactions between federal agencies are presented separately from assets and liabilities from transactions with the public.

The Statement of Net Cost shows the net cost of operations for the reporting period.

The Statement of Changes in Net Position presents the OFS ending net position by two components - Cumulative Results of Operations and Unexpended Appropriations. It summarizes the change in net position. The ending balances of both components of net position are also reported on the Balance Sheet.

The Statement of Budgetary Resources provides information about funding and availability of budgetary resources and the status of those resources at the end of the reporting period.

Balance Sheet

Office of Financial Stability (Troubled Asset Relief Program)
BALANCE SHEET
As of September 30, 2009

Dollars in Millions		
ASSETS		
Intragovernmental Assets:		
Fund Balance with Treasury (Note 4)	$	97,733
Troubled Asset Relief Program:		
Direct Loans and Equity Investments, Net (Note 6)		237,892
Asset Guarantee Program (Note 6)		1,765
Total Assets	$	337,390
LIABILITIES		
Intragovernmental Liabilities:		
Accounts Payable and Other Liabilities	$	5
Principal Payable to the Bureau of the Public Debt (Note 8)		143,335
Due to the General Fund (Note 3)		109,748
Total Intragovernmental Liabilities	$	253,088
Accounts Payable and Other Liabilities		73
Liability for Home Affordable Modification Program (Note 5)		1
Total Liabilities	$	253,162
Commitments and Contingencies (Note 7)		
NET POSITION		
Unexpended Appropriations	$	84,229
Cumulative Results of Operations		(1)
Total Net Position	$	84,228
Total Liabilities and Net Position	$	337,390

The accompanying notes are an integral part of these financial statements.

Statement of Net Cost

Office of Financial Stability (Troubled Asset Relief Program)
STATEMENT OF NET COST
For the Period Ended September 30, 2009

Dollars in Millions

Gross Cost:		
Subsidy Cost (Note 6)		
Direct Loan and Equity Investment Programs	$	43,605
Asset Guarantee Program		(2,201)
Total Program Subsidy Cost		41,404
Interest Expense on Borrowings from the Bureau of the Public Debt (Note 8)		6,436
Home Affordable Modification Program (Note 5)		2
Administrative Cost		167
Total Gross Cost	**$**	**48,009**
Less Earned Revenue:		
Dividend and Interest Income - Programs (Note 6)		(9,503)
Interest Income on Financing Account		(3,649)
Subsidy Allowance Amortized (Note 9)		6,716
Net Earned Revenue	**$**	**(6,436)**
Total Net Cost of Operations	**$**	**41,573**

The accompanying notes are an integral part of these financial statements.

Statement of Changes in Net Position

Office of Financial Stability (Troubled Asset Relief Program)
STATEMENT OF CHANGES IN NET POSITION
For the Period Ended September 30, 2009

Dollars in Millions	Unexpended Appropriations	Cumulative Results of Operations
Beginning Balances, at Inception	$ -	$ -
Budgetary Financing Sources		
Appropriations Received	238,268	-
Appropriations Used	(154,039)	154,039
Other Financing Sources	-	(112,467)
Total Financing Sources	84,229	41,572
Net Cost of Operations	-	(41,573)
Ending Balances	$ 84,229	$ (1)

The accompanying notes are an integral part of these financial statements.

Statement of Budgetary Resources

Office of Financial Stability (Troubled Asset Relief Program)
STATEMENT OF BUDGETARY RESOURCES
For the Period Ended September 30, 2009

Dollars in Millions	Budgetary Accounts	Nonbudgetary Financing Accounts
BUDGETARY RESOURCES		
Unobligated Balances Brought Forward, Inception	$ -	$ -
Budget Authority:		
Appropriations	238,268	-
Borrowing Authority	-	309,971
Spending Authority from Offsetting Collections		
Earned: Collected	-	243,072
Change in Unfilled Orders Without Advance	-	28,927
Total Budget Authority	238,268	581,970
Permanently Not Available	-	(120,841)
TOTAL BUDGETARY RESOURCES (Note 10)	$ 238,268	$ 461,129
STATUS OF BUDGETARY RESOURCES		
Obligations Incurred:		
Direct	$ 210,112	$ 452,184
Unobligated Balance:		
Apportioned and Available	28,156	7,009
Not Available	-	1,936
TOTAL STATUS OF BUDGETARY RESOURCES	$ 238,268	$ 461,129
CHANGE IN OBLIGATED BALANCES		
Obligated Balance Brought Forward, Inception	$ -	$ -
Obligations Incurred	210,112	452,184
Gross Outlays	(153,961)	(372,982)
Change in Uncollected Customer Payments from Federal Sources	-	(28,927)
Obligated Balance, Net, End of Period:		
Unpaid Obligations	56,151	79,202
Uncollected Customer Payments from Federal Sources	-	(28,927)
Obligated Balance, Net, End of Period	$ 56,151	$ 50,275
NET OUTLAYS		
Gross Outlays	$ 153,961	$ 372,982
Offsetting Collections	-	(243,072)
Distributed Offsetting Receipts	(2,720)	-
NET OUTLAYS	$ 151,241	$ 129,910

The accompanying notes are an integral part of these financial statements.

Notes to the Financial Statements

Note 1. Reporting Entity

The Troubled Asset Relief Program (TARP) was authorized by the Emergency Economic Stabilization Act of 2008 (EESA or "The Act"). The Act gave the Secretary of the Treasury (the Secretary) broad and flexible authority to establish the TARP to purchase and insure mortgages and other troubled assets, which permits the Secretary to inject capital into banks and other commercial companies by taking equity positions in those entities, if needed, to stabilize the financial markets.

The EESA established certain criteria under which the TARP would operate, including provisions that impact the budgeting, accounting, and reporting of troubled assets acquired under the Act. Section 101(a) of the EESA provided the authority for the Secretary to purchase troubled assets, and Section 101(a)(3) of the EESA established the Office of Financial Stability (OFS) to implement the TARP. Section 102 of the EESA required the Secretary to establish a program to guarantee troubled assets originated or issued prior to March 14, 2008, including mortgage-backed securities. Section 115 of the EESA limits the authority of the Secretary to purchase troubled assets up to $700 billion[1] outstanding at any one time, calculated at the aggregate purchase prices of all troubled assets held. There was approximately $381.3 billion outstanding against the Section 115 authority as of September 30, 2009. Section 120 of the EESA established that the authorities under Sections 101(a), excluding Section 101(a)(3) and Section 102 of the EESA, shall terminate on December 31, 2009. Section 120 of the EESA further established that the Secretary, upon submission of a written certification to Congress, may extend the authority provided under the Act to expire no later than 2 years from the date of the enactment of the Act (October 3, 2008).

Under the provisions of the EESA, the OFS implemented the TARP which resulted in the development of the following programs: the Capital Purchase Program; the Targeted Investment Program; the Asset Guarantee Program; the Consumer and Business Lending Initiative; the Public-Private Investment Program; the American International Group, Inc. Investment Program (formerly known as the Systemically Significant Failing Institutions Program); and the Automotive Industry Financing Program (see Note 6); as well as the Home Affordable Modification Program (see Note 5).

While these financial statements reflect the activity of the OFS in executing its programs, including providing resources to various entities to help stabilize the financial markets, they do not include the assets, liabilities, or results of operations of commercial entities in which the OFS has a significant equity interest. Through the purchase of troubled assets, the OFS has entered into several different types of direct loan, equity investment, and asset guarantee arrangements with private entities. These direct loans, equity investments, and asset guarantees were made with the intent of helping to

[1] The Helping Families Save Their Homes Act of 2009 (PubL.No. 111-22, Div. A, 123 Stat., 1632 (2009) amended the act to reduce the maximum allowable amount of outstanding troubled assets under the act by almost $1.3 billion, from $700 billion to $698.7 billion. As required under section 102 of EESA, the $381.3 billion does not include a subtraction from the outstanding guarantee amount to reflect the balance in the Troubled Assets Insurance Financing Fund.

stabilize the financial markets and mitigating, as best as possible, any adverse impact on the economy. These direct loans, equity investments, and asset guarantees were not made to engage in the business activities of the respective private entities. Based on this intent, the OFS has concluded that such direct loans, equity investments, and asset guarantees are considered "bail outs", under the provisions of paragraph 50 of Statement of Federal Financial Accounting Concepts (SFFAC) No. 2, *Entity and Display*. In addition, these entities do not meet the conclusive criteria in SFFAC No. 2. As such, OFS determined that none of these entities meet the criteria to be classified as a federal entity. Consequently, their assets, liabilities, and results of operations are not consolidated in these OFS financial statements.

In addition, the OFS has made investments in certain Special Purpose Vehicles[2] (SPV). SFFAC No. 2, paragraphs 43 and 44, reference indicative criteria such as ownership and control over an SPV to carry out government powers and missions, as criteria in the determination of consolidation. The OFS has concluded that the lack of control over the SPVs is the primary basis for determining that none of the SPVs meet the criteria to be classified as a federal entity. As a result, the assets, liabilities and results of operations of the SPVs are not included in these OFS financial statements. The OFS has recorded the investments in private entities and investments in SPVs in accordance with Credit Reform Accounting, as discussed below. Additional disclosures regarding these SPV investments are included in these Notes.

The EESA established the OFS within the Office of Domestic Finance of the Department of the Treasury (Treasury). The OFS prepares stand-alone financial statements to satisfy EESA's requirement for the TARP to prepare annual financial statements. Additionally, as an office of the Treasury, its financial statements are consolidated into Treasury's department-wide financial statements and Agency Financial Report.

Note 2. Summary of Significant Accounting Policies

Basis of Accounting and Presentation

The accompanying financial statements include the operations of the OFS and have been prepared from the accounting records of the OFS in conformity with accounting principles generally accepted in the United States for federal entities (Federal GAAP), and the Office of Management and Budget (OMB) Circular A-136, *Financial Reporting Requirements*, as amended. Federal GAAP includes the standards issued by the Federal Accounting Standards Advisory Board (FASAB). The FASAB is recognized by the American Institute of Certified Public Accountants (AICPA) as the official accounting standards-setting body for the U.S. Government. As such, the FASAB is responsible for establishing Federal GAAP for Federal reporting entities.

In July 2009, the FASAB issued the Statement of Federal Financial Accounting Standards (SFFAS) No. 34, *The Hierarchy of Generally Accepted Accounting Principles, Including the Application of Standards Issued by the Financial Accounting Standards*

[2] The OFS has invested in SPV's under the Consumer and Business Lending Initiative and the Automotive Industry Financing Program.

Board. SFFAS No. 34 identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of general purpose financial reports of federal reporting entities that are presented in conformity with Federal GAAP.

In addition to the above, Section 123(a) of the EESA requires that the budgetary cost of purchases of troubled assets and guarantees of troubled assets, and any cash flows associated with authorized activities, be determined in accordance with the Federal Credit Reform Act of 1990 (FCRA). Section 123(b) (1) of the EESA requires that the budgetary costs of troubled assets and guarantees of troubled assets be calculated by adjusting the discount rate for market risks. As a result of this requirement, the OFS considered market risk in its calculation and determination of the estimated net present value of its direct loans, asset guarantees, and equity investments for budgetary purposes. Similarly, market risk is considered in valuations for financial reporting purposes (see Note 6 for further discussion).

Consistent with the accounting policy for equity investments made by Treasury in private entities, the OFS accounts for its equity investments at fair value, defined as the estimated amount of proceeds the OFS would receive if the equity investments were sold to a market participant. The OFS uses the present value accounting concepts embedded in SFFAS No. 2, *Accounting for Direct Loans and Loan Guarantees*, to derive fair value measurements. The OFS concluded that the equity investments were similar to direct loans in that there is a stated rate and a redemption feature which, if elected, requires repayment of the amount invested. Furthermore, consideration of market risk provides a basis to arrive at a fair value measurement. Therefore, the OFS uses SFFAS No. 2 (as more fully discussed below) for reporting and disclosure requirements of it equity investments.

Federal loans and loan guarantees are governed by FCRA for budgetary accounting and the associated FASAB accounting standard SFFAS No. 2, as amended for financial reporting. The OFS applies the provisions of the SFFAS No. 2, as amended, when accounting for direct loans, equity investments, and asset guarantees. Direct loans and equity investments disbursed and outstanding are recognized as assets at the net present value of their estimated future cash flows and outstanding asset guarantees are recognized as liabilities or assets at the net present value of their estimated future cash flows. The subsidy allowance account represents the difference between the face value of the outstanding direct loan and equity investment balance and the net present value of the expected future cash flows, and is reported as an adjustment to the face value of the direct loan or equity investment. Consequently, direct loans, asset guarantees, and equity investments, including investments in preferred and common stock and warrants of public companies, are accounted for and reported by the OFS using credit reform accounting in accordance with SFFAS No. 2, as amended.

The OFS recognizes dividend revenue associated with equity investments when declared by the entity in which OFS has invested and when received in relation to any repurchases and restructuring. The OFS reflects changes in the value of direct loans, equity investments, and asset guarantees in the subsidy cost on the Statement of Net Cost annually. The OFS has received common stock warrants, additional preferred stock (referred to as warrant preferred stock) or additional notes, as additional consideration for direct loans and equity investments made and asset guarantees entered into. The OFS accounts for the warrants and warrant preferred stock received under Section 113 of EESA as fees under SFFAS No. 2, and, as such, the value of the warrants and warrant preferred stock is a reduction of the subsidy allowance.

Use of Estimates

The OFS has made certain estimates and assumptions relating to the reporting of assets, liabilities, revenues, and cost to prepare these financial statements. Actual results could significantly differ from these estimates. Major financial statement line items subject to estimates include Troubled Asset Relief Program Direct Loans and Equity Investments, Net, Asset Guarantee Program, and related subsidy cost (see Note 6).

The most significant differences between actual results and estimates may occur in the valuation of direct loans, equity investments, and asset guarantees. The forecasted future cash flows used to determine these amounts as of September 30, 2009, are sensitive to slight changes in model assumptions, such as general economic conditions, specific stock price volatility of the entities which the OFS has an equity interest, estimates of expected default, and prepayment rates. Forecasts of future financial results have inherent uncertainty and the OFS's Troubled Asset Relief Program Direct Loans and Equity Investments, Net and Asset Guarantee Program line items as of September 30, 2009, are reflective of relatively illiquid, troubled assets whose values are particularly sensitive to future economic conditions and other assumptions. Additional discussion related to sensitivity analysis can be found in the Management Discussion and Analysis section of the Agency Financial Report.

Credit Reform Accounting

The FCRA provided for the use of program, financing, and general fund receipt accounts to separately account for activity related to loans and guarantees. These accounts are classified as either budgetary or non-budgetary in the Statement of Budgetary Resources. The budgetary accounts include the program and general fund receipt accounts, and the non-budgetary accounts consist of the credit reform financing accounts.

As discussed previously, the OFS accounts for the cost of purchases of troubled assets and guarantees of troubled assets, and any cash flows associated with authorized activities, including direct loans, in accordance with Section 123(a) of the EESA and the FCRA for budgetary accounting and SFFAS No. 2 for financial reporting, except for the Home Affordable Modification Program (HAMP) (see Note 5).

The authoritative guidance for financial reporting is primarily contained in the SFFAS No. 2, as amended by the SFFAS No. 18, *Amendments to Accounting Standards for Direct Loans and Loan Guarantees*, and the SFFAS No. 19, *Technical Amendments to Accounting Standards for Direct Loans and Loan Guarantees*.

In accordance with SFFAS No. 2, the OFS maintains program accounts which receive appropriations and obligate funds to cover the subsidy cost of direct loans, equity investments and asset guarantees, and disburses the subsidy cost to the OFS financing accounts. The financing accounts are non-budgetary accounts that are used to record all of the cash flows resulting from the OFS direct loans, equity investments and asset guarantees.[3] Cash flows include disbursements, repayments, repurchases, fees, recoveries, borrowings from the Treasury, interest, negative subsidy and the subsidy cost received from the program accounts.

The financing arrangements specifically for the TARP activities are provided for in the EESA as follows: (1) Borrowing for program funds under Section 118 that constitute appropriations when obligated or spent, which are reported as "appropriations" in these financial statements; (2) borrowing by financing accounts for non-subsidy cost under the FCRA and Section 123; and (3) the Troubled Assets Insurance Financing Fund (TAIFF) under Section 102(d).

The OFS has general fund receipt accounts which are used to record the receipt of amounts paid from the financing accounts when there is a negative subsidy or negative modification from the original estimate or a downward reestimate. Amounts in the general fund receipt accounts are available for appropriations only in the sense that all general fund receipts are available for appropriations. Any assets in these accounts are non-entity assets and are offset by intragovernmental liabilities. At the end of the fiscal year, the fund balance transferred to the U.S. Treasury through the general fund receipt account is no longer included in the OFS's fund balance reporting.

The SFFAS No. 2 requires that the actual and expected costs of federal credit programs be fully recognized in financial reporting. The OFS calculated and recorded an initial estimate of the future performance of direct loans, equity investments, and asset guarantees. The data used for these estimates were reestimated at the fiscal year-end to reflect adjustments for market risk, asset performance, and other key variables and economic factors. The reestimate data was then used to estimate and report the "Subsidy Cost" in the Statement of Net Cost. A detailed discussion of the OFS subsidy calculation and reestimate assumptions, process and results is provided in Note 6.

Fund Balance with Treasury

The Fund Balance with Treasury includes general, financing and other funds available to pay current liabilities and finance authorized purchases. Cash receipts and disbursements are processed by the Treasury, and the OFS's records are reconciled with those of the Treasury on a regular basis.

Available unobligated balances represent amounts that are apportioned for obligation in the current fiscal year. Unavailable unobligated balances represent unanticipated collections in excess of the amounts apportioned which are unavailable. Obligated balances not yet disbursed include undelivered orders and unpaid expended authority.

[3] For the Asset Guarantee Program, OFS has established the Troubled Assets Insurance Financing Fund, as required by section 102(d) of the EESA which is the financing account under FCRA for the Asset Guarantee Program.

Troubled Asset Relief Program Direct Loans and Equity Investments, Net

Troubled Asset Relief Program Direct Loans and Equity Investments, Net represents the estimated net outstanding amount of the OFS direct loans and equity investments, exclusive of the HAMP. The direct loan and equity investment balances have been determined in accordance with the provisions of SFFAS No. 2 (see Note 6).

Asset Guarantee Program

The Asset Guarantee Program represents the asset resulting from the net present value of the estimated cash inflows that are in excess of the estimated future claim payments (see Note 6).

Liabilities for Home Affordable Modification Program

Liabilities for Home Affordable Modification Program (HAMP) represent the liability for payments to servicers and investors, and principal balance reduction payments for the account of borrowers under the HAMP are accounted for in accordance with SFFAS No. 5, *Accounting for Liabilities of the Federal Government*. Under SFFAS No. 5, a liability is recognized for any unpaid amounts due as of the reporting date. This liability includes amounts due from the OFS to pay for benefits and services provided under the terms of the HAMP as of the OFS's reporting date regardless of whether such payments have been reported to the OFS. The liability estimate is calculated based on information reported by participating servicers.

The OFS has determined that credit reform accounting, is not applicable to HAMP since there are no incoming cash flows to be valued.

General Property and Equipment

Equipment with a cost of $50 thousand or more per unit and a useful life of two years or more is capitalized at full cost and depreciated using the straight-line method over the equipment's useful life. Other equipment not meeting the capitalization criteria is expensed when purchased. Under this policy, the OFS had no capitalized general property and equipment at September 30, 2009.

Accounts Payable and Other Liabilities

Accounts Payable and Other Liabilities are amounts due to intragovernmental or public entities that will generally be liquidated during the next operating cycle (within one year from the balance sheet date).

Principal Payable to the Bureau of the Public Debt

Principal Payable to the Bureau of the Public Debt (BPD) represents the net amount due to the BPD for equity investments, direct loans, and asset guarantees funded by borrowings from the BPD as of September 30, 2009 (see Note 8).

Due to the General Fund

Due to the General Fund represents the amount of downward reestimates as of September 30, 2009, related to direct loans, equity investments, and asset guarantees as of September 30, 2009 (see Notes 3 and 6).

Unexpended Appropriations

Unexpended Appropriations represents the OFS undelivered orders and unobligated balances as of September 30, 2009.

Cumulative Results of Operations

Cumulative Results of Operations, presented on the Balance Sheet and on the Statement of Changes in Net Position, represents the net results of the OFS operations since inception, through September 30, 2009. The Other Financing Sources in the Statement of Changes in Net Position consist primarily of transfers due to the Treasury General Fund as of September 30, 2009, relating to the downward reestimates.

Leave

A liability for OFS employees' annual leave is accrued as it is earned and reduced as leave is taken. Each year the balance of accrued annual leave is adjusted to reflect current pay rates as well as forfeited "use or lose" leave. Amounts are unfunded to the extent current or prior year appropriations are not available to fund annual leave earned but not taken. Sick leave and other types of non-vested leave are expensed as taken.

Employee Health and Life Insurance and Workers' Compensation Benefits

The OFS employees may choose to participate in the contributory Federal Employees Health Benefit and the Federal Employees Group Life Insurance Programs. The OFS matches a portion of the employee contributions to each program. Matching contributions are recognized as current operating expenses.

The Federal Employees' Compensation Act (FECA) provides income and medical cost protection to covered Federal civilian employees injured on the job, and employees who have incurred a work-related injury or occupational disease. Future workers' compensation estimates are generated from an application of actuarial procedures developed to estimate the liability for FECA benefits. The actuarial liability estimates for FECA benefits include the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases.

Employee Pension Benefits

The OFS employees participate in either the Civil Service Retirement System (CSRS) or the Federal Employees' Retirement System (FERS) and Social Security. These systems provide benefits upon retirement and in the event of death, disability or other termination of employment and may also provide pre-retirement benefits. They may also include benefits to survivors and their dependents, and may contain early retirement or other special features. The OFS contributions to both retirement plans and Social Security, as well as imputed costs for pension and other retirement benefit costs administered by the Office of Personnel Management, are recognized on the Statement of Net Cost as Administrative Costs. Federal employee benefits also include the Thrift Savings Plan (TSP). For FERS employees, a TSP account is automatically established and the OFS matches employee contributions to the plan, subject to limitations. The matching contributions are also recognized as Administrative Costs on the Statement of Net Cost.

Note 3. Non-Entity Liabilities

The OFS had approximately $109.7 billion in downward reestimates related to its Troubled Asset Relief Program Direct Loans and Equity Investments, Net and Asset Guarantee program which is a non-entity liability payable due to the Treasury General Fund as of September 30, 2009 (see Note 6).

Note 4. Fund Balances with Treasury

As of September 30, 2009, Fund Balances with Treasury, by fund type and status, consisted of the following:

Fund Balances:	(Dollars in Millions)
General Funds	$ 45,650
Program Funds	38,658
Financing Funds	13,425
Total Fund Balances	$ 97,733
Status of Fund Balances:	
Unobligated Balances	
Available	$ 35,165
Unavailable	1,936
Obligated Balances Not Yet Disbursed	60,632
Total Status of Fund Balances	$ 97,733

Included in the OFS Financing Funds is the premium collections of approximately $174.8 million related to the Asset Guarantee Program (AGP) that are required by the EESA Section 102(d) to be maintained in the TAIFF (see Note 6).

Note 5. The Home Affordable Modification Program

The Home Affordable Modification Program (HAMP) is designed to assist eligible homeowners who are experiencing financial hardships to remain in their homes by providing reductions in their monthly mortgage payments for up to five years. The HAMP provides for one-time, monthly, and annual incentives to servicers, borrowers, and investors who participate in the program. On an ongoing basis, beyond such incentives, the OFS shares equally in the cost of the reductions with the mortgage investors. Lastly, investors are paid a Home Price Decline Protection payment to partially offset losses from home price declines.

For the HAMP, Fannie Mae provides direct programmatic support as a third party agent on behalf of the OFS, Freddie Mac provides compliance oversight as a third party agent on behalf of the OFS, and the servicers work directly with the borrowers to modify and service the borrowers' loans.

As of September 30, 2009, the OFS had entered into agreements with 63 servicers to provide up to approximately $27.1 billion in payments and incentives to borrowers, servicers and investors. As of September 30, 2009, this $27.1 billion was included in Obligations Incurred in the Statement of Budgetary Resources. All HAMP payments are made to servicers either for themselves or for the benefit of borrowers and investors. Furthermore, all payments are contingent on borrowers remaining current on their mortgage payments. As of September 30, 2009, approximately $946.5 thousand in incentive payments had been paid to three servicers in incentive payments for 743 borrowers who had completed official loan modifications.

Servicers have until December 31, 2012, to enter into mortgage modifications with borrowers.

As of September 30, 2009, the OFS had accrued approximately $1.4 million of first lien incentive for modifications under the HAMP program.

Note 6. Troubled Asset Relief Program Direct Loans and Equity Investments, Net and Asset Guarantee Program

The OFS applies the provisions of SFFAS No. 2 to account for direct loans, equity investments and asset guarantees. This standard requires measurement of the asset or liability at the net present value of the estimated future cash flows. The cash-flow estimates for each transaction reflect the actual structure of the instruments. For each of these instruments, analytical cash flow models generate estimated cash flows to and from the OFS over the estimated term of the instrument. Further, each cash-flow model reflects the specific terms and conditions of the program, technical assumptions regarding the underlying assets, risk of default or other losses, and other factors as appropriate. The models also incorporate an adjustment for market risk to reflect the additional return required by the market to compensate for variability around the expected losses reflected in the cash flows (the "unexpected loss"). The basic methods for each of these models are outlined below.

Direct Loans

The estimated future cash flows for direct loans are derived using analytical models that estimate the cash flows to and from the OFS over the life of the loan. These cash flows include the scheduled principal, interest, and other payments to the OFS, including estimated proceeds from equity interest obtained or additional notes. These models also include estimates of default and recoveries, incorporating the value of any collateral provided by the contract. The probability and timing of default and losses relating to a default are estimated by using applicable historical data when available, or publicly available proxy data, including credit rating agency historical performance data.

In the case of the Term Asset-backed Securities Loan Facility (TALF), the OFS uses an analytical model to project cash flows to and from the OFS based on the estimated loan collateral performance, the estimated mix of collateral funded through the TALF and the terms of the contracts.

The models include an adjustment for market risk which is intended to capture the risk of unexpected losses, but are not intended to represent fair value, i.e. the proceeds that would be expected to be received if the loans were sold to a market participant.

Equity Investments

Preferred stock cash flows are projected using an analytical model developed to incorporate the risk of losses associated with adverse events, such as failure of the institution or increases in market interest rates. The model estimates how cash flows vary depending on: 1) current interest rates, which may affect the decision whether to repay the preferred stock; and 2) the strength of a financial institution's assets. Inputs to the model include institution specific accounting data obtained from regulatory filings, an institution's stock price volatility, historical bank failure information, as well as market prices of comparable securities trading in the market. OFS estimates the values and projects the cash flows of warrants using an option-pricing approach based on the current stock price and its volatility. Investments in common stock which are exchange traded are valued at the market price. The result of using market prices, either quoted prices for the identical asset or quoted prices for comparable assets, is that the equity investments are recorded at estimated fair value.

Asset Guarantees

The value of the asset guarantee reflects the net present value of estimated default-claim payments by the OFS, net of income from recoveries on defaults, fees, or other income. Guarantee fees to date have been paid in the form of preferred stock, subsequently converted to trust preferred stock, and a warrant to purchase common stock of the financial institution, whose value is modeled using the same methodology for other equity purchase programs, discussed above. Default-claim payments are based on estimated losses on the guaranteed assets. Key inputs into these estimates are forecasted gross domestic product, unemployment rates and home price depreciation, in a base scenario and a stress scenario.

Subsidy Cost

The recorded subsidy cost of a direct loan, equity investment or asset guarantee is based on a set of estimated future cash flows. OFS actions that change these estimated future cash flows change subsidy costs and are recorded as a modification. The cost of a modification is recognized as a modification expense, included in subsidy cost, when the direct loan, equity investment, or asset guarantee is modified. During fiscal year 2009, modifications occurred within the Capital Purchase Program, Consumer and Business Lending Initiative, the American International Group, Inc. Investment Program, and the Automotive Industry Financing Program. See detailed discussion related to each program and related modifications below. Total net modification costs for the period ended September 30, 2009, approximated $412.1 million.

Equity Investments, Direct Loan and Asset Guarantee Programs

The OFS administers a number of programs designed to help stabilize the financial system and restore the flow of credit to consumers and businesses. The OFS has purchased direct loans and made equity investments and entered into asset guarantees. The table below is a list and type of the OFS programs:

Program	Program Type
Capital Purchase Program	Equity Investment/ Subordinated Debentures
Targeted Investment Program	Equity Investment
Asset Guarantee Program	Guarantee
Consumer and Business Lending Initiative	Direct Loan
Public-Private Investment Program	Equity Investment and Direct Loan
American International Group, Inc. Investment Program (*)	Equity Investment
Automotive Industry Financing Program	Equity Investment and Direct Loan

(*) Formerly known as the Systemically Significant Failing Institutions Program

A description of each of these programs is provided below, and certain financial data by program is provided in the table at the end of this footnote.

Capital Purchase Program

In October 2008, the OFS began implementation of the TARP with the Capital Purchase Program (CPP), designed to help stabilize the financial system by assisting in building the capital base of certain viable U.S. financial institutions to increase the capacity of those institutions to lend to businesses and consumers and support the economy. Under this program, the OFS purchases senior perpetual preferred stock from qualifying U.S. controlled banks, savings associations, and certain bank and savings and loan holding companies (Qualified Financial Institution or QFI). The senior preferred stock has a stated dividend rate of 5.0% through year five, increasing to 9.0% in subsequent years. The dividends are cumulative for bank holding companies and subsidiaries of bank holding companies and non-cumulative for others and payable when and if declared by the institution's board of directors. Under the original terms of the senior preferred stock the QFI may not redeem the shares within the first three years of the date of the investment, unless it has received the proceeds of one or more Qualified Equity Offerings (QEO)[4] which results in aggregate gross proceeds to the QFI of not less than 25.0% of the issue price of the senior preferred stock. QFIs that are Sub-chapter S

[4] A Qualified Equity Offering is defined as the sale by the QFI after the date of the senior preferred stock investment of Tier 1 perpetual preferred stock or common stock for cash.

corporations issued subordinated debentures in order to maintain compliance with the Internal Revenue Code. The maturity of the subordinated debentures is 30 years and interest rates are 7.7% for the first 5 years and 13.8% for the remaining years.

In February 2009 and May 2009, the United States Congress passed the American Recovery and Reinvestment Act of 2009 and the Helping Families Save Their Homes Act of 2009, respectively. These acts contained amendments to the EESA (EESA Amendments) which require the Secretary to allow QFIs to repay at any time, subject to regulatory approval, regardless of whether the 25.0% or greater QEO was accomplished. The ability of a QFI to repay the OFS investment prior to year 3 or a 25.0% QEO was not considered in the original subsidy cost estimate. Therefore, a modification cost of $77.7 million was recorded as a result of these amendments.

In addition to the senior preferred stock, the OFS received warrants, as required by section 113(d) of EESA, from public QFIs to purchase a number of shares of common stock. The warrants have an aggregate market price equal to 15.0% of the total senior preferred stock investment. The exercise price and market value used to determine the number of shares of common stock subject to the warrant was calculated based on the average of closing prices of the common stock on the 20 trading days ending on the last day prior to the date the QFIs application was preliminarily approved for participation in the program. The warrants include customary anti-dilution provisions. In the event that a public QFI completes, prior to December 31, 2009, one or more QEOs with aggregate gross proceeds of not less than 100.0% (100.0% QEO) of the senior perpetual preferred stock investment, the number of shares subject to the warrants will be reduced by 50.0%. As of September 30, 2009, 19 QFIs reduced the number of shares available under the warrants as a result of this provision. The warrants have a 10 year term. The OFS may exercise one half of the warrants prior to the earlier of a 100.0% QEO, or December 31, 2009. Subsequent to December 31, 2009, OFS may exercise any warrants held in whole or in part. The OFS considers the impact of potential future QEOs in the valuation process.

The OFS received warrants from non-public QFIs for the purchase of additional senior preferred stock (or subordinated debentures if appropriate) with a stated dividend rate of 9.0% (13.8% interest rate for subordinate debentures) and a liquidation value equal to 5.0% of the total senior preferred stock (additional subordinate debenture) investment. These warrants were immediately exercised and resulted in the OFS holding additional senior preferred stock (subordinated debentures) (collectively referred to as “warrant preferred stock”) of non-public QFIs. The OFS did not receive warrants from banks considered Community Development Financial Institutions (CDFIs). As of September 30, 2009, the OFS has invested in 20 institutions considered CDFIs.

The EESA Amendments previously discussed also allow the Secretary to liquidate warrants associated with repurchased senior preferred stock at the market price. In addition, a QFI, upon the repurchase of its senior preferred stock, also has the contractual right to repurchase the common stock warrants at the market price.

In June 2009, the OFS entered into an exchange agreement with Citigroup. Under the terms of the agreement the OFS exchanged $25.0 billion of its investment in senior preferred stock for a new series (Series M) of mandatorily convertible preferred stock.

The initial conversion price was $3.25 per share. In July 2009, the OFS received the Series M shares, which were subsequently converted in September 2009 to approximately 7.7 billion common shares of Citigroup. This exchange transaction was not considered in the original subsidy cost estimate for CPP. As a result, the OFS recorded a modification cost of approximately $1.8 billion for the fiscal year ended 2009. The OFS also has investments in Citigroup through the TIP and AGP.

During the period ended September 30, 2009, the OFS invested approximately $204.6 billion in 685 institutions, including small, community, regional, and national banks, as well as CDFIs, in 48 states, the District of Columbia, and Puerto Rico. Approximately $70.7 billion of the OFS investments have been repurchased or redeemed bringing the total gross investment balance as of September 30, 2009 to approximately $133.9 billion. In addition, during the period ended September 30, 2009, the OFS received under CPP approximately $6.8 billion in dividends on senior preferred and warrant preferred stock and approximately $2.9 billion in proceeds from the repurchase of warrants and warrant preferred stock. 38 QFIs have not declared and paid one or more dividends to OFS under CPP as of September 30, 2009.

On November 1, 2009, a CPP participant, CIT Group, filed for Chapter 11 Bankruptcy. The OFS had invested $2.3 billion in senior preferred stock of CIT Group and received a warrant for the purchase of common stock. The OFS does not expect a significant recovery of its preferred stock investment. As such, this investment has been reduced to zero in these financial statements. The ultimate amount received, if any, from this investment will depend on the outcome of the bankruptcy proceedings.

On November 6, 2009, a subsidiary of UCBH Holdings, Inc. (a CPP participant), United Commercial Bank, was closed by its regulators. The OFS had invested approximately $298.7 million in senior preferred stock and received a warrant for the purchase of common shares. The value of these shares, including the warrant, reflected in these financial statements is approximately $22.5 million as of September 30, 2009. The ultimate amount received, if any, from this investment will depend on the outcome of the receivership.

On November 13, 2009, a subsidiary of Pacific Coast National Bancorp. (a CPP participant), Pacific Coast National Bank, was closed by its regulators. The OFS had invested approximately $4.1 million in senior preferred stock and received warrant preferred stock in the amount of $206 thousand. The value of the shares, including the warrant preferred stock, reflected in these financial statements is approximately $154 thousand as of September 30, 2009. The ultimate amount received, if any, from this investment will depend on the outcome of the receivership.

Further details on the outstanding senior preferred share investments and subordinated debentures under CPP and the net investment amount including estimated cash flows associated with the sale or exercise of the warrants, as of September 30, 2009, are presented in the table at the end of this section.

Targeted Investment Program

The Targeted Investment Program (TIP) was designed to prevent a loss of confidence in financial institutions that could result in significant market disruptions, threatening the financial strength of similarly situated financial institutions, impairing broader financial markets, and undermining the overall economy. The OFS considers institutions as candidates for the TIP on a case-by-case basis, based on a number of factors described in the program guidelines. These factors include the threats posed by destabilization of the institution, the risks caused by a loss of confidence in the institution, and the institution's importance to the nation's economy.

The OFS completed the first transaction under the TIP in December 2008, when it invested $20.0 billion in Citigroup cumulative perpetual preferred stock and received a warrant for the purchase of Citigroup common stock. Under the agreement with Citigroup, the OFS receives an 8.0% annual dividend, payable quarterly, if and when declared by Citigroups' Board of Directors. As part of this agreement, Citigroup must implement rigorous compensation standards and other restrictions on corporate expenditures. In June 2009, the OFS and Citigroup agreed to an exchange of the cumulative perpetual preferred stock issued under the TIP for a new series of trust preferred securities. Citigroup issued subordinated debentures to a trust established by Citigroup, and the trust issued trust preferred securities to OFS. Interest and principal payments on the subordinated debentures are passed-through to the trust preferred security holders. The trust preferred securities pay a quarterly distribution at an annual rate of 8.0% to OFS. The subordinated debentures contain an interest deferral provision allowing Citigroup to defer payment of interest for up to 5 years. The OFS will not receive distributions from the trust preferred securities during a deferral period. Deferred interest is required to be paid upon termination of the deferral period. As of September 30, 2009, Citigroup has not exercised its option to defer interest payments. The subordinated debentures mature in 2039. As a result, the trust is scheduled to pay out the proceeds to the holders of the trust preferred securities. In addition, the subordinated debentures can be prepaid by Citigroup at any time prior to maturity, subject to consultation with the Federal Reserve, as long as the U.S. Government holds the trust preferred securities. The terms of the new securities are substantially the same as the preferred stock originally received by the OFS and therefore the exchange transaction did not result in a modification. The OFS also has investments in Citigroup through the CPP and the AGP.

In January 2009, the OFS completed its second transaction under the TIP, investing $20.0 billion in Bank of America. Under the agreement with Bank of America, the OFS purchased $20.0 billion of cumulative perpetual preferred stock and received a warrant for the purchase of Bank of America common stock. The preferred stock purchased from Bank of America contains a stated annual dividend rate of 8.0%, payable quarterly, if declared. Bank of America's agreement under the TIP stipulated that the institution must implement rigorous executive compensation standards and other restrictions on corporate expenditures. The OFS also has investments in Bank of America through the CPP.

During the period ended September 30, 2009, OFS received approximately $1.9 billion in dividends under the TIP. See the table presented at the end of this section for further details.

Asset Guarantee Program

The Asset Guarantee Program (AGP) provides guarantees for assets held by systemically significant financial institutions that face a risk of losing market confidence due in large part to a portfolio of distressed or illiquid assets. The AGP is applied with extreme discretion in order to improve market confidence in the systemically significant institution and in financial markets broadly.

Section 102 of the EESA established the AGP to guarantee troubled assets originated or issued prior to March 14, 2008, including mortgage-backed securities, and established the Troubled Assets Insurance Financing Fund (TAIFF). In accordance with Section 102(c) and (d) of the EESA, premiums from financial institutions, are collected and all fees are recorded by the OFS in the TAIFF. In addition, Section 102(c)(3) of the EESA requires that the original premiums assessed are "set" at a minimum level necessary to create reserves sufficient to meet anticipated claims. In the event there are insufficient funds within the TAIFF for the payment of claims, amounts are borrowed from the Treasury until sufficient funds are received into the TAIFF. In the event that the estimate of claims exceeds the estimated future cash inflows, an upward reestimate would be recorded and amounts would be transferred to the TAIFF as a subsidy expense.

The OFS completed its first transaction under the AGP in January 2009, when it finalized the terms of a guarantee agreement with Citigroup. Under the agreement, the OFS, the Federal Deposit Insurance Corporation (FDIC), and the Federal Reserve Bank of New York (FRBNY) provided protection against the possibility of large losses on an asset pool of approximately $301.0 billion of loans and securities backed by residential and commercial real estate and other such assets, which remain on Citigroup's balance sheet. The following loss-sharing terms apply to the transaction: Citigroup absorbs the first $39.5 billion in losses, and losses over the $39.5 billion are shared by the U. S. government (90.0 %) and Citigroup (10.0 %) (the "second loss"). For the second loss, the OFS absorbs up to $5.0 billion, then the FDIC absorbs up to $10.0 billion, and lastly the FRBNY funds any U.S. government losses above the OFS and the FDIC commitments through a non-recourse loan. The guarantee is in place for ten years for residential assets and five years for non-residential assets.

As a premium for the guarantee, Citigroup issued $7.0 billion of cumulative perpetual preferred stock with an 8.0 % stated dividend rate and a warrant for the purchase of common stock; approximately $4.0 billion and the warrant were issued to the OFS, and approximately $3.0 billion was issued to the FDIC. As part of the agreement, Citigroup submitted an executive compensation plan to the OFS and the FDIC for approval and must comply with certain common stock dividend restrictions. The OFS has received approximately $174.8 million in dividends on the preferred stock received as compensation for this arrangement. These dividends have been deposited into the TAIFF. The preferred stock originally issued to the OFS and the FDIC were exchanged for the trust preferred securities discussed above under the TIP. The OFS has also invested in Citigroup through the CPP and the TIP.

The net present value of the estimated cash inflows from the preferred stock and warrant received by the OFS from Citigroup as a premium is greater than the estimated net present value of future claim payments, resulting in an asset of approximately $1.8 billion, after reestimates, as of September 30, 2009.

In January 2009, the OFS, FDIC, FRBNY (together the USG Parties) and Bank of America signed a Summary of Terms (Term Sheet) pursuant to which the USG Parties agreed to guarantee or lend against a pool of up to $118.0 billion of financial instruments consisting of securities backed by residential and commercial real estate loans and corporate debt and related derivatives. In May 2009, prior to completing definitive documentation, Bank of America notified the USG Parties of its desire to terminate negotiations with respect to the guarantee contemplated in the Term Sheet. All parties agreed that Bank of America received value for entering into the Term Sheet with the USG Parties and that the USG Parties should be compensated for out-of-pocket expenses and a fee equal to the amount Bank of America would have paid for the guarantee from the date of the signing of the Term Sheet through the termination date. Under the terms of the settlement, the U.S. Treasury received $276.0 million for its role in the guarantee agreement through the OFS, the FRBNY received $57.0 million, and the FDIC received $92.0 million. All the OFS funds received for the settlement were deposited in the TAIFF and subsequently paid to the Treasury General Fund. The $276 million received by OFS pursuant to the settlement is reflected in the OFS Statement of Net Cost as a reduction of the AGP subsidy cost.

Consumer and Business Lending Initiative (CBLI)

Term Asset-Backed Securities Loan Facility

The Term Asset-Backed Securities Loan Facility (TALF) was created by the Federal Reserve Board (FRB) to provide low cost funding to investors in certain classes of Asset Backed Securities (ABS). The OFS agreed to participate in the program by providing liquidity and credit protection to the FRB.

Under the TALF, the FRBNY, as implementer of the TALF program, originated loans on a non-recourse basis to holders of certain AAA rated ABS secured by recently originated consumer and commercial loans and commercial mortgage backed securities (New Issue CMBS). In addition to securities secured by recently originated loans, CMBS issued prior to January 2009 and originally AAA rated (Legacy CMBS) are eligible collateral. TALF loans have a term of 3 or 5 years and are secured solely by eligible collateral. Haircuts (a percentage reduction used for collateral valuation) are determined based on the riskiness of each type of eligible collateral and the maturity of the eligible collateral pledged to the FRBNY. The “haircuts” provide additional protection to OFS by exposing the TALF borrowers to some risk of loss. Interest rates charged on the TALF loans depend on the weighted average maturity of the pledged collateral, the collateral type and whether the collateral pays a fixed or variable coupon.

As part of the program, the FRBNY has entered into a put agreement with the TALF, LLC, a special purpose vehicle created by the FRBNY. In the event of a TALF borrower default, the FRBNY will seize the collateral and sell it to the TALF, LLC under this agreement. The TALF, LLC receives a monthly fee equal to the difference between the TALF loan rate and the FRBNY’s fee (spread) as compensation for entering into the put agreement. The accumulation of this fee will be used to fund purchases. In the event there are insufficient funds to purchase the collateral, the OFS has committed to invest up to $20.0 billion in non-recourse subordinate notes issued by the TALF, LLC. The subordinate notes bear interest at 1 Month LIBOR plus 3.0% and mature 10 years from the closing date, subject to extension. The OFS disbursed $100.0 million upon creation of the TALF, LLC and the remainder can be drawn to purchase collateral in the event the spread is not sufficient to cover purchases. Any amounts needed in excess of the OFS commitment and the fee would be provided through a loan from the FRBNY. Upon wind-down of the TALF, LLC (collateral defaults, reaches final maturity or is sold), the cash balance will be disbursed according to the following payment priority:

1. FRBNY principal balance
2. OFS principal balance
3. FRBNY interest
4. OFS interest
5. Remaining cash balance – 90.0% to the OFS, 10.0% to the FRBNY

Subsequent to the initial cost estimates prepared for the TALF, certain changes were made to the terms of the program, including increasing the term to 5 years and the addition of different types of acceptable collateral. These program changes resulted in a modification, increasing the original cost estimate by $8.0 million.

The TALF, LLC is owned and controlled by the FRBNY. The credit agreement between the OFS and the TALF, LLC provides the OFS with certain rights consistent with a creditor but would not constitute control. As such TALF, LLC is not a federal entity and the assets, liabilities, revenue and cost of TALF, LLC are not included in the OFS financial statements. The discussion below provides information on 1) the amount of TALF loans issued by the FRBNY, by collateral class, and 2) the assets, liabilities, income and expense of the TALF, LLC.

The FRBNY has originated $50.9 billion in TALF loans[5], of which about $42.7 billion is outstanding as of September 30, 2009. The average "haircut" was approximately 9.92% of the originated balance. As of September 30, 2009, all of the TALF loans performed as agreed. The table below shows the outstanding balance of the FRBNY TALF loans as of September 30, 2009, by collateral type:

Collateral Type	Loan Amount (Dollars in Billions)	% of Total
Auto	$ 7.43	17.3%
Credit Cards	$ 21.61	50.6 %
Equipment	$ 0.89	2.1 %
Floor Plan	$ 1.01	2.4 %
Premium Finance	$ 0.99	2.3 %
Servicing Advances	$ 0.58	1.4 %
Small Business	$ 0.46	1.1 %
Student Loan	$ 5.63	13.1 %
New Issue CMBS	$ 0.0	0.0 %
Legacy CMBS	$ 4.13	9.7 %
Total	$ 42.73	100.0 %

As of September 30, 2009, the TALF, LLC has assets of approximately $198.9 million consisting primarily of investments in U.S. Treasury and Agency securities[6]. Total liabilities of the TALF, LLC are $101.8 million consisting of the OFS subordinated note plus accrued interest. During the period ended September 30, 2009, the TALF, LLC collected $99.1 million in fees and investment income and incurred $2.3 million in expenses, $1.8 million of which is accrued interest on the OFS subordinated note. As of September 30, 2009 there were no TALF borrower defaults and consequently no purchases of collateral by the TALF, LLC.

American International Group, Inc. Investment Program (AIG)

The OFS provides assistance to certain systemically significant financial institutions on a case by case basis in order to provide stability to institutions that are critical to a functioning financial system and are at substantial risk of failure as well as to prevent broader disruption to financial markets.

In November 2008, the OFS invested $40.0 billion in AIG's cumulative Series D perpetual cumulative preferred stock with a dividend rate of 10.0% compounded quarterly. On April 17, 2009, AIG and the OFS restructured their November 2008 agreement. Under the restructuring, the OFS exchanged $40.0 billion of cumulative Series D preferred stock for $41.6 billion of non-cumulative 10.0% Series E preferred stock. The amount of Series E preferred stock is equal to the original $40.0 billion, plus approximately $733.0 million in undeclared dividends as of the February 1, 2009, scheduled quarterly dividend payment date, $15.0 million in dividends compounded on

[5] These represent loans originated by the FRBNY and not the OFS. The intention of this disclosure is to show the activity in the program and the types of collateral that could eventually be purchased by the TALF, LLC with funding provided by the OFS.

[6] Agency securities refer to securities issued by either Ginnie Mae, Fannie Mae, Freddie Mac, or the Federal Home Loan Banks.

the undeclared dividends, and an additional $855.0 million in dividends from February 1, 2009, but not paid as of April 17, 2009. AIG's restructured agreement kept the quarterly dividend payment dates of May 1, August 1, November 1, and February 1, as established by the original November 2008 agreement. The original subsidy cost estimate did not consider this restructuring which resulted in a modification cost of $127.2 million.

In addition to the exchange, the OFS agreed to make available an additional $29.8 billion capital facility to allow AIG to draw additional funds if needed to assist in AIG's restructuring. The OFS investment consists of Series F non-cumulative perpetual preferred stock with an initial liquidation amount of $0.0. This liquidation amount increases with any draw down by AIG on the facility. The dividend rate applicable to these shares is 10.0% and is payable quarterly, if declared, on the outstanding liquidation amount. As of September 30, 2009, approximately $3.2 billion has been funded by the OFS to AIG under this additional capital facility. Consistent with SSFAS No.2, the unused portion of the AIG capital facility is not recognized as an asset as of September 30, 2009.

As of September 30, 2009, AIG has not made any dividend payments on any of the perpetual preferred stock. Subsequently, AIG failed to make a dividend payment on November 2, 2009. Per the terms of the preferred stock, if AIG misses 4 dividend payments, the OFS may appoint to the AIG board of directors, the greater of two members or 20.0% of the total number of directors of the Company.

Automotive Industry Financing Program

The objective of the Automotive Industry Financing Program (AIFP) was to help prevent a significant disruption of the American automotive industry, which could have a negative effect on the economy of the United States. The discussion below details the various investments and loans made by the OFS in the automotive industry, generally provided in chronological order.

The table below illustrates amounts originally disbursed and collected under AIFP. These amounts are shown before conversions, exchanges, or valuation. For a detailed discussion on the current status of the loans see the narrative below the table.

	Amounts Disbursed as of September 30, 2009	Collection of Interest, Dividends, and Additional Notes	Principal Repayments	Amount Outstanding before Conversions, Exchanges, and Valuation
	(dollars in millions)			
GM General Purpose Loan including Working Capital Advances	$ 19,400	$ 134	$ -	$ 19,400
GMAC LLC Rights Offering	884	9	-	884
Chrysler Holding LLC General Purpose	4,000	53	-	4,000
Chrysler Financial	1,500	22	1,500	-
Auto Supplier Support Program	413	6	-	413
Auto Warranty Program	640	4	640	-
Chrysler Debtor-In-Possession	1,888	-	-	1,888
Chrysler Exit	4,577	-	-	4,577
GM Debtor-In-Possession	30,100	34	-	30,100
GMAC Preferred stock	5,000	265	-	5,000
GMAC Mandatorily Convertible Preferred stock	7,500	165	-	7,500
Total	$ 75,902	$ 692	$ 2,140	$ 73,762

General Motors (GM or old GM) General Purpose Loan including Working Capital Advances

The OFS provided GM with a total of $13.4 billion in a three-year direct loan bearing interest at 3 Month LIBOR (subject to a 2.0% floor), plus 3.0% and secured by various types of collateral. $4.0 billion of this loan was funded in December 2008, an additional $5.4 billion in January, 2009, and an additional $4.0 billion in February 2009. In April 2009, the OFS and GM amended this loan agreement to increase the maximum loan amount from $13.4 billion to $15.4 billion, and on May 20, 2009 to increase the maximum loan amount from $15.4 billion to $19.4 billion (these amendments are referred to as the Working Capital Advances) to provide GM with adequate working capital to assist in the restructuring effort. The additional amounts were funded upon amendment, bringing the total funded under this loan to $19.4 billion. The agreement required GM to develop and implement a restructuring plan to achieve long-term financial viability and required compliance with certain enhanced executive compensation and expense control requirements.

Furthermore, the OFS received warrants for shares of GM common stock and an additional senior unsecured note in the principal amount of $748.6 million. The purpose of this loan was to enhance the ability of GM and its subsidiaries to pursue timely and aggressive production of energy-efficient advanced technology vehicles; preserve and promote the jobs of American workers employed directly by GM and its subsidiaries; safeguard the ability of GM and its subsidiaries to provide retirement and health care benefits for retirees and their dependents; and stimulate manufacturing and sales of automobiles produced by GM. On June 1, 2009, GM filed for Chapter 11 bankruptcy. All rights under this loan were transferred to a newly created entity (GM NewCo) and subsequently extinguished in connection with a successful credit bid for the assets of old GM. In addition, the OFS received $134.4 million in interest while the loan was outstanding. See further discussion below under GM Debtor-In-Possession.

GMAC LLC Rights Offering

In December 2008, the OFS agreed, in principal, to lend up to $1.0 billion to GM for participation in a rights offering by GMAC in support of GMAC's reorganization as a bank holding company. The loan was secured by the GMAC common interest acquired in the rights offering. The loan agreement specified that at any time, at the option of the lender (OFS), the unpaid principal and accrued interest was exchangeable for the membership interest purchased, by GM, during the rights offering. The note was funded for $884.0 million. In May 2009, the OFS exercised its exchange option under the loan and received 190,921 membership interests, representing approximately 35.36% of the voting interest, in GMAC in full satisfaction of the loan. In addition, OFS received $9.1 million in interest while the loan was outstanding. The conversion to GMAC shares was not considered in the original subsidy cost. As a result, a modification was recorded reducing the estimated subsidy cost by approximately $1.6 billion.

Chrysler Holding LLC General Purpose

The OFS provided a three-year, $4.0 billion loan to Chrysler in January 2009, bearing interest at 3 Month LIBOR (subject to a 2.0% floor) plus 3.0%. The loan was secured by various collateral including parts inventory, real estate, and certain equity interests held by Chrysler. This agreement required Chrysler to submit a restructuring plan to achieve long-term viability and required compliance with certain enhanced executive compensation and expense-control requirements. Furthermore, the OFS received a senior unsecured note from Chrysler in the principal amount of approximately $266.8 million, containing the same terms as the General Purpose loan. The purpose of this loan was to: enhance the ability of Chrysler and its subsidiaries to pursue timely and aggressive production of energy-efficient advanced technology vehicles; preserve and promote the jobs of American workers employed directly by Chrysler and its subsidiaries; safeguard the ability of Chrysler and its subsidiaries to provide retirement and health care benefits for retirees and their dependents; and stimulate manufacturing and sales of automobiles produced by Chrysler.

On April 30, 2009, Chrysler filed for Chapter 11 bankruptcy. Upon entering bankruptcy, a portion of Chrysler was sold to a newly created entity (New Chrysler). Under the terms of the bankruptcy agreement, $500.0 million of this loan was assumed by New Chrysler (see discussion under Chrysler Exit for discussion of note terms). The balance remains outstanding and is in default. Any recovery of the remainder of this loan will depend on: (a) Chrysler Holding's obligation to pay the greater of $1.375 billion or 40.0% of the equity value of Chrysler Financial to OFS should Chrysler Holding receive certain distributions from Chrysler Financial and, (b) proceeds received from the sale of assets remaining in the bankrupt company. In addition, OFS received $52.1 million in interest payments on this note.

Chrysler Financial

In January, 2009, the OFS loaned $1.5 billion to Chrysler LB Receivables Trust (Chrysler Trust), a special purpose entity created by Chrysler Financial, to finance the extension of new consumer auto loans. The five-year loan bore interest at 1 Month LIBOR plus 1.0% for the first year, 1.5% for the remaining term and was secured by a senior secured interest in a pool of newly originated consumer automotive loans, and Chrysler served as a guarantor for certain covenants of Chrysler Financial. Under the agreement, Chrysler Financial was required to comply with the executive compensation and corporate governance requirements of Section 111(b) of the EESA, as well as enhanced restrictions on executive compensation including the need to reduce by 40.0% its bonus pool for Senior Executive Officers and Senior Employees. In lieu of warrants, the OFS received additional notes in an amount equal to 5.0% of the maximum loan amount. The additional notes would vest 20.0% on the closing date and 20.0% on each anniversary of the closing date and had other terms similar to the loan. The purpose of this loan was to assist Chrysler Financial in providing retail financing to purchasers of automobiles, light duty trucks and recreational vehicles; to stimulate manufacturing and sales of automobiles produced by Chrysler's affiliates; preserve and promote the jobs of American workers employed directly by Chrysler's affiliates and in related industries; and safeguard the ability of Chrysler to provide retirement and health care benefits for their retirees and their dependents. On July 14, 2009, the loan and additional note of $15.0 million were paid in full. In addition, the OFS received $7.4 million in interest payments while this loan was outstanding.

Auto Supplier Support Program

In April 2009, the OFS committed $5.0 billion in financing for the Auto Supplier Support Program, as follows: $3.5 billion for GM suppliers and $1.5 billion for Chrysler suppliers. These commitments were subsequently reduced to $2.5 billion for GM suppliers and $1.0 billion for Chrysler suppliers per the loan agreement. Under the program, suppliers are able to sell their receivable to a SPV, created by the respective automaker, at a discount. The purchases of the receivables are funded by equity investments made by the automaker, cash payments made by the automaker on previously purchased receivables or from draws on the OFS funding commitment. The duration of the program is 12 months, extendable at the option of the OFS. Interest is charged on advances under the facility at a rate of 3 Month LIBOR (subject to a 2.0% floor) plus 3.5%. In addition, the OFS received a contingent payment note comprised of an exit fee equal to 4.0% of the adjusted commitment amount and 50.0% of the residual equity in the SPV after the program's end date. This program provides suppliers with access to government backed protection ensuring that money owed to them for the products they ship will be paid regardless of what happens to the recipient car company. This provided suppliers with needed funding to operate their businesses and help unlock credit more broadly in the supplier industry. Purchases of receivables and collection of amounts due from GM and Chrysler is performed by a third party service provider. Suppliers must maintain qualifying commercial terms with the automakers to participate in the program. The OFS has provided approximately $413.1 million of funding to this program. The bankruptcy of Chrysler and GM did not impact this program, as both companies were allowed to continue paying suppliers while in bankruptcy. As of September 30, 2009, the OFS had received $5.9 million in interest under the Auto Supplier Support Program.

Auto Warranty Program

In April 2009 and May 2009, the OFS loaned approximately $280.0 million to Chrysler and $360.6 million to GM , respectively, to capitalize SPVs created by Chrysler and GM to finance participation in the Warranty Commitment Program (warranty program). The OFS also received additional notes as consideration for its loans in an amount equal to 6.67% of the funded amounts. The warranty program covered all warranties on new vehicles purchased from Chrysler and GM during the period in which Chrysler and GM were restructuring. The program was run by a third party program administrator with the backing of financial resources allocated by the OFS, Chrysler and GM. Chrysler and GM contributed 15.0% of the projected cost for warranty service on each covered vehicle, with the OFS providing additional funds to cover 110.0% of the projected cost. The SPVs holding the funds operated separately from Chrysler and GM and would transfer the necessary funds to a third-party to handle all warranty claims even if Chrysler and GM entered into bankruptcy or went out of business. Both Chrysler and GM have completed the Section 363[7] sales in June 2009 and July 2009, respectively. Upon completion of the sale, the OFS received principal amounts due from both GM and Chrysler and terminated the warranty program. Interest in the amount of $3.1 million was received by the OFS from Chrysler. No interest was received in connection with the GM repayment. The GM additional note was assigned to the New GM as part of the bankruptcy proceedings and extinguished as part of the credit bid for the assets of old GM. The Chrysler additional note is still outstanding.

Chrysler Debtor-In-Possession

In May 2009, the OFS and the Canadian government jointly agreed to make a loan in the total amount of $4.1 billion ($3.0 billion by the OFS and $1.1 billion by Canada) to Chrysler LLC in its capacity as debtor-in-possession (DIP) in its bankruptcy case. In May 2009, the OFS increased its loan commitment in the DIP credit agreement to $3.8 billion, and the Canadian government increased its commitment to $1.2 billion, bringing the maximum loan amount to $5.0 billion. The loan interest rate was the 3 Month Eurodollar rate plus 3.0%. The stated maturity was September 2009, with earlier maturity depending on the bankruptcy proceedings. Of the $3.8 billion committed by the OFS, approximately $1.9 billion was funded during the bankruptcy. This DIP loan provided the necessary liquidity to sustain Chrysler during the bankruptcy period. Upon the Section 363 sale of the Chrysler assets, the funding commitment was reduced to amounts previously drawn. As such, no additional amounts were drawn from this facility. Recovery of the DIP loan is subject to the bankruptcy process associated with the Chrysler assets remaining after the sale to New Chrysler.

Chrysler Exit

In May 2009, the OFS committed to make a loan to New CarCo Acquisition LLC (New Chrysler or Chrysler Group LLC), the company that purchased the assets of Chrysler.

[7] Section 363 refers to Section 363 of the Federal Bankruptcy Code, which allows companies in bankruptcy to sell assets in reorganization.

The final terms of the credit agreement resulted in a loan to New Chrysler for approximately $7.1 billion. This amount consists of $6.6 billion of new funding and $500.0 million of assumed debt[8] from the OFS January 2, 2009 credit agreement with Chrysler Holding LLC. The loan was secured by a first priority lien on the assets of Chrysler Group LLC. Funding of the loan was available in two installments or tranches (B and C), each with varying availability and terms. The following describes the terms of Tranches B and C.

The maximum funding under Tranche B was $2.0 billion and was funded on the closing date of the agreement. Interest on Tranche B is 3 Month Eurodollar plus 5.0% margin (in certain situations, defined in the agreement, a rate other than the 3 Month Eurodollar rate will be applied. This rate, referred to as the Alternative Base Rate, will be the greater of the Prime Rate, the Federal Funds Effective rate plus 0.5% or the 3 Month Eurodollar rate plus 1.0%. If this Alternative Base Rate is applied, the margin will be 4.0% versus the 5.0% if the 3 Month Eurodollar Rate is used). Tranche B is due and payable on December 10, 2011, provided that the Chrysler Group LLC may elect to extend the maturity of up to $400.0 million of Tranche B to the Tranche C maturity date. If so elected, the applicable margin will increase to 6.5% for Eurodollar and 5.5% for ABR loans, respectively.

The maximum funding under Tranche C is approximately $4.64 billion, of which approximately $2.58 billion was funded on the closing date. Interest on Tranche B is 3 Month Eurodollar plus 7.91% margin (in certain situations, defined in the agreement, a rate other than the 3 Month Eurodollar rate will be applied. This rate, referred to as the Alternative Base Rate, will be the greater of the Prime Rate, the Federal Funds Effective rate plus 0.5% or the 3 Month Eurodollar rate plus 1.0%. If this Alternative Base Rate is applied, the margin will be 6.91% versus the 7.91% if the 3 Month Eurodollar Rate is used). On June 10, 2016, the Tranche C loan shall be prepaid to the extent the funded amount is greater than 50.0% of the closing date commitment amount, taking into consideration amounts previously prepaid as a voluntary prepayment. The remaining balance of the Tranche C loan is due and payable on June 10, 2017.

Interest on both the Tranche B and Tranche C will be payable in-kind through December 2009 and will be added to the principal balance of the respective Tranche. In addition, additional in-kind interest will accrue in the amount of $17.0 million per quarter. Such amount will be added to the Tranche C loan balance subject to interest at the appropriate rate.

The OFS also obtained other consideration, including a 9.85% equity interest in Chrysler Group LLC and additional notes[9] with principal balances of $288.0 million and $100.0 million[10]. As of September 30, 2009, the OFS has funded approximately $4.6 billion under this facility.

[8] The assumed debt contains the same terms as the Tranche C loan with respect to mandatory prepayment, interest and maturity.
[9] The additional notes bear the same interest rate and maturity as the Tranche C loan.
[10] Interest begins to accrue on this note after certain events, defined in the credit agreement, have taken place.

GM Debtor-In-Possession

On June 1, 2009, GM filed for Chapter 11 bankruptcy. As part of the filing the OFS and the Canadian government agreed to lend up to $33.3 billion under the terms of the DIP credit agreement; the OFS's commitment amount was $30.1 billion. The OFS funded the $30.1 billion of which approximately $986.0 million remains outstanding as of September 30, 2009. In July 2009, the DIP credit agreement was amended to reflect the fact that the amounts there under (other than approximately $986.0million that remained with GM for wind-down in bankruptcy and $7.1 billion that was assumed by GM NewCo) were extinguished in connection with a successful credit bid for the assets of old GM.

The OFS has assigned its rights in this loan as well as the General Purpose and Working Capital loans and previously received common stock warrants to a newly created entity (GM NewCo or General Motors Company). The purpose of this GM NewCo was to obtain sufficient assets of GM out of bankruptcy to satisfy the original loans disbursed to GM and discussed above, which it accomplished through a successful credit bid for the assets in a sale pursuant to Section 363 of the Bankruptcy Code. Upon closing of the Section 363 sale, the General Motors Company has assumed $7.1 billion of the DIP loan, simultaneously paying $0.4 billion (return of warranty program funds), resulting in a balance of $6.7 billion. The loan has a term of 6 years and bears interest at 3 Month Eurodollar (subject to a 2.0% floor) plus 5.0% and has a first lien security interest in the assets of General Motors Company. The OFS also received $2.1 billion in 9.0% cumulative perpetual preferred stock and 60.8% of the common equity interest in General Motors Company. The assets received by the OFS as a result of the assignment and Section 363 sale are considered recoveries of the original loans for subsidy cost estimation purposes. As of September 30, 2009, the OFS had received $34.1 million in dividends on GM preferred stock.

GMAC Preferred Stock

In December 2008, the OFS purchased preferred membership interests for $5.0 billion which were converted to senior preferred stock with an 8.0% annual distribution right (dividends) from GMAC. Under the agreement, GMAC issued warrants to the OFS to purchase, for a nominal price, additional preferred equity in an amount equal to 5.0% of the preferred equity purchased. These warrants were exercised at closing of the investment transaction. The additional preferred stock provided for a 9.0% annual distribution right. The purpose of this investment was to enable GMAC to restore liquidity to its finance businesses and restore stability to the domestic automobile industry in the United States. As of September 30, 2009, the OFS has received $265.2 million in dividends associated with these preferred and warrant preferred stock.

GMAC Mandatorily Convertible Preferred Stock

In May 2009, the OFS published a non-binding term sheet to invest $13.1 billion to support GMAC, subject to definitive documentation and GMAC's capital needs. The OFS has invested $7.5 billion (of the $13.1 billion) in 9.0% Mandatorily Convertible Preferred Stock in GMAC to support its ability to originate new loans to Chrysler dealers and consumers, and help address GMAC's capital needs. The preferred stock have a liquidation amount of $50 per share and are convertible in whole or in part, at any time, at the option of GMAC, subject to the approval of the Federal Reserve. Furthermore, GMAC shall not convert any of the stock to the extent such conversion would result in the OFS owning in excess of 49% of GMAC's common equity except (1) with the prior written consent of the OFS, (2) pursuant to GMAC's Capital Plan, or (3) pursuant to an order of the Federal Reserve compelling such a conversion. The determination of the percentage of common equity owned by the OFS would take into account the common stock currently owned by the OFS as a result of the conversion of the GMAC Rights Offering, previously discussed. Absent a previous conversion, the preferred stock will automatically convert after 7 years. The conversion rate is 0.00432 units of common stock per unit of convertible preferred stock. The remaining $5.6 billion (per the non-binding term sheet) is subject to the FRB's review of GMAC's capital plan assessment of whether additional capital is needed. As of September 30, 2009, the remaining $5.6 billion has not been funded. The OFS had received approximately $165.4 million in dividends associated with these preferred and warrant preferred stock.

Public-Private Investment Program

The Public-Private Investment Program (PPIP) is part of the OFS's efforts to help restart the market and provide liquidity for legacy assets. Under this program, the OFS will make equity and debt investments in investment vehicles (referred to as Public Private Investment Funds or "PPIFs") established by private investment managers. The equity investment will be used to match private capital and will equal not more than 50.0% of the total equity invested. The debt investment will be, at the option of the investment manager, equal to 50.0% or 100.0% of the total equity (including private equity). The PPIFs are only allowed to purchase commercial mortgage-backed securities and non-agency residential mortgage-backed securities issued prior to January 1, 2009 that were originally rated AAA or an equivalent rating by two or more nationally recognized statistical rating organizations without external credit enhancement and that are secured directly by the actual mortgage loans, leases or other assets and not other securities. The PPIFs are also permitted to invest in certain temporary securities, including bank deposits, U.S. Treasury securities, and certain money market mutual funds. At least 90 percent of the assets underlying any eligible asset must be situated in the United States. On September 30, 2009, the OFS signed definitive limited partnership and loan agreements with two investment managers, committing to potentially disburse up to $6.7 billion. As of September 30, 2009, no private fund managers had made any investments and the OFS had not disbursed any funds.

Subsidy Reestimates

The purpose of reestimates is to update original program subsidy cost estimates to reflect actual cash flow experience as well as changes in forecasts of future cash flows. Forecasts of future cash flows are updated based on actual program performance to date, additional publicly available relevant historical market data on securities performance, revised expectations for future economic conditions, and enhancements to cash flow projection methods. Financial statement reestimates for all programs were performed using actual financial transaction data through September 30, 2009. In accordance with credit reform guidance and to ensure the timely completion of the credit reform reestimate process, market and security specific data publicly available as of September 30, 2009, was used for the CPP, AGP, TIP and direct loan AIFP and data through August 31, 2009 was used for the equity portion of AIFP, AIG and TALF in the reestimate calculations. The OFS assessed the key inputs of the reestimates using data publically available as of September 30, 2009, and in its determination, there were no significant changes to the key inputs for the three programs for which August 31, 2009, data was used that would require a revision to the reestimates.

Downward Reestimates for the fiscal year ended September 30, 2009, are as follows:

Downward Reestimate Amounts
(*Dollars in Millions*)

Program	Subsidy	Interest	Total
AGP	$(1,097)	$(77)	$(1,174)
Direct Loan			
AIFP	$(9,039)	$(1,571)	$(10,610)
CBLI/TALF	(222)	(21)	(243)
Subtotal Direct	$(9,261)	$(1,592)	$(10,853)
Equity Investment			
CPP	$(68,558)	$(3,861)	$(72,419)
TIP	(20,366)	(1,101)	(21,467)
AIG	(845)	(280)	(1,125)
AIFP	(2,331)	(379)	(2,710)
Subtotal Equity	$(92,100)	$(5,621)	$(97,721)
Total	$(102,458)	$(7,290)	$(109,748)

Descriptions of the reestimates, by OFS Program, are as follows:

The approximately $1.2 billion in downward reestimates for the AGP is primarily due to improvements in market conditions from when the guarantee was committed in January 2009. The improved market conditions resulted in an increase in the projected AGP asset due to the net present value of the estimated cash inflows from the preferred stock and warrants received by OFS from Citigroup as a premium being greater than the estimated value of future claim payments associated with the $5.0 billion asset guarantee.

The approximately $10.6 billion in downward reestimates for the direct loans-AIFP is primarily the result of the post bankruptcy improved financial position of one of the major companies participating in the program. The $0.2 billion in downward reestimates for the TALF is entirely due to projected improved performance of the securities within the program versus the original estimate.

The $70.7 billion in repurchases during fiscal year 2009 accounts for $9.7 billion of the $72.4 billion in downward reestimates in the CPP. Projected repurchases of $30.0 billion in the next 12 months accounts for approximately $5.4 billion, with the $57.3 billion balance in downward reestimates in the CPP primarily due to improved market conditions from when the original estimate was made in December 2008.

The $21.5 billion in downward reestimates in the TIP is mostly due to improved market conditions from when the original estimates were made in December 2008 and January 2009. Approximately $2.3 billion is due to a $20.0 billion repurchase forecast within 12 months following September 30, 2009.

The $1.1 billion in downward reestimates for the AIG Investment Program and $2.7 billion in downward reestimates for the AIFP equity programs are primarily due to improvements in market conditions from when the equities were purchased resulting in a reduction in the projected costs of the programs.

Key financial data for the Troubled Asset Relief Program Loans and Equity Investments and Asset Guarantee Program are included in the following two tables:

1. Direct Loans and Equity Investments Outstanding, Gross, represent amounts paid by OFS to acquire the loans and equity investments. Repurchases, redemptions, and repayments have been deducted from these balances.
2. Net Direct Loans and Equity Investments represent the present value of net cash flows that OFS estimates it will receive from the loans and equity investments. For equity securities, this amount represents fair value.
3. Subsidy Expense by component, subsidy cost allowance and a reconciliation of the subsidy cost allowance illustrate the relationship between subsidy cost and asset value.
4. Reconciliation of subsidy cost by program is also incorporated in the tables.

Office of Financial Stability (Troubled Asset Relief Program)
NOTES TO THE FINANCIAL STATEMENTS
For the Period Ended September 30, 2009

CPP	Capital Purchase Program
AIG	American International Group, Inc. Investment Program
TIP	Targeted Investment Program
AIFP	Automotive Industry Financing Program
CBLI	Consumer and Business Lending Initiative

Dollars in Millions	TOTAL	CPP	AIG	TIP	AIFP	CBLI
Troubled Asset Relief Program Direct Loans and Equity Investments						
Direct Loans and Equity Investment Programs:						
Direct Loans and Equity Investments Outstanding, Gross	$ 290,969	$ 133,901	$ 43,206	$ 40,000	$ 73,762	$ 100
Subsidy Cost Allowance	(53,077)	7,770	(30,054)	341	(31,478)	344
Net Direct Loans and Equity Investments	$ 237,892	$ 141,671	$ 13,152	$ 40,341	$ 42,284	$ 444
New Loans or Investments Disbursed	$ 363,826	$ 204,618	$ 43,206	$ 40,000	$ 75,902	$ 100
Obligations for Loans and Investments not yet Disbursed	$ 51,681	$ -	$ 26,629	$ -	$ 5,152	$ 19,900
Budget Subsidy Rate, Excluding Modifications and Reestimates: (See Note 1 below)						
Interest Differential		5.97%	-45.52%	9.31%	6.97%	5.87%
Defaults		25.60%	123.56%	48.38%	54.21%	0.00%
Other		-4.58%	4.74%	-8.84%	-3.13%	-110.10%
Total Budget Subsidy Rate		26.99%	82.78%	48.85%	58.05%	-104.23%
Subsidy Cost by Component:						
Interest Differential	$ 4,175	$ 12,279	$ (17,280)	$ 3,724	$ 5,446	$ 6
Defaults	161,297	52,655	46,906	19,352	42,384	-
Other	(13,705)	(9,414)	1,799	(3,536)	(2,444)	(110)
Total Subsidy Cost, Excluding Modifications and Reestimates	$ 151,767	$ 55,520	$ 31,425	$ 19,540	$ 45,386	$ (104)
Reconciliation of Subsidy Cost Allowance:						
Balance, inception	$ -	$ -	$ -	$ -	$ -	$ -
Subsidy cost for disbursements	151,767	55,520	31,425	19,540	45,386	(104)
Subsidy cost for modifications	412	1,866	127	-	(1,589)	8
Interest and Dividend Collections	9,329	6,790	-	1,862	677	-
Warrants and additional notes	2,916	2,901	-	-	15	-
Net Interest (to) / from Treasury on Borrowings and Financing Account Balance	(2,773)	(2,428)	(373)	(276)	309	(5)
Balance, End of Period, Before Reestimates	$ 161,651	$ 64,649	$ 31,179	$ 21,126	$ 44,798	$ (101)
Subsidy Reestimates	(108,574)	(72,419)	(1,125)	(21,467)	(13,320)	(243)
Balance, End of Period	$ 53,077	$ (7,770)	$ 30,054	$ (341)	$ 31,478	$ (344)
Reestimates:						
Interest on Reestimate	$ (7,213)	$ (3,861)	$ (280)	$ (1,101)	$ (1,950)	$ (21)
Subsidy	(101,361)	(68,558)	(845)	(20,366)	(11,370)	(222)
Total Reestimates - (Decrease) in Subsidy Cost	$ (108,574)	$ (72,419)	$ (1,125)	$ (21,467)	$ (13,320)	$ (243)
Reconciliation of Subsidy Cost:						
Subsidy cost for disbursements	$ 151,767	$ 55,520	$ 31,425	$ 19,540	$ 45,386	$ (104)
Subsidy cost for modifications	412	1,866	127	-	(1,589)	8
Subsidy Reestimates	(108,574)	(72,419)	(1,125)	(21,467)	(13,320)	(243)
Total Direct Loan and Equity Investment Programs Subsidy Cost	$ 43,605	$ (15,033)	$ 30,427	$ (1,927)	$ 30,477	$ (339)

Note 1: The rates reflected in the "Budget Subsidy Rate" table above are weighted rates for the program. To compensate for the weighting of the various risk category subsidy rates, the "by component" dollar amounts reflected were computed as a ratio of the component rate to the total weighted subsidy rate multiplied by the subsidy expense for the program. Therefore, the *Total Subsidy Cost excluding modifications and reestimates* will not equal the *New Loans or Investments Disbursed* multiplied by the *Budget Subsidy Rate*.

Office of Financial Stability (Troubled Asset Relief Program)
NOTES TO THE FINANCIAL STATEMENTS
For the Period Ended September 30, 2009

Dollars in Millions	AGP
Asset Guarantee Program	
Asset Guarantees Outstanding:	
Oustanding Principal Amount of Guaranteed Assets, Face Value	$ 301,000
Amount of Outstanding Principal Guaranteed	$ 5,000
Asset for Asset Guarantee Program	$ 1,765
Budget Subsidy Rate, Excluding Modifications and Reestimates:	
Defaults	43.62%
Fees and Other Collections	-53.23%
Other	-5.37%
Total Budget Subsidy Rate	-14.98%
Subsidy Cost by Component:	
Defaults	2,181
Fees and Other Collections	(2,662)
Other	(270)
Total Subsidy Cost, Excluding Modifications and Reestimates	$ (751)
Reconciliation of Asset Guarantee Program:	
Balance, Inception	$ -
Subsidy Cost	(751)
Dividend Collections on Preferred Stock	175
Net Interest from Treasury on Borrowings and Financing Account Balance	(15)
Balance, End of Period, Before Reestimate	$ (591)
Subsidy Reestimate	(1,174)
Balance, End of Period	$ (1,765)
Reestimates:	
Interest on Reestimate	$ (77)
Subsidy	(1,097)
Total Reestimates - (Decrease) in Subsidy Cost	$ (1,174)
Reconciliation of Subsidy Cost:	
Subsidy cost	$ (751)
Subsidy reestimate	(1,174)
Cancellation fees collected	(276)
Total Asset Guarantee Program Subsidy Cost	$ (2,201)

Note 7. Commitments and Contingencies

The OFS is party to various legal actions and claims brought by or against it. In the opinion of management and General Counsel, the ultimate resolution of these legal actions and claims will not have a material effect on the OFS financial statements as of September 30, 2009. The OFS has not incurred any loss contingencies that would be considered probable or reasonably possible for these cases. Refer to Note 6 for additional commitments.

Note 8. Principal Payable to the Bureau of the Public Debt

Equity investments, direct loans, and asset guarantees accounted for under credit reform accounting are funded by subsidy appropriations and borrowings from the BPD. The OFS also borrows funds to pay the Treasury General Fund for negative subsidy costs and downward reestimates. The OFS makes periodic principal repayments to the BPD based on the analysis of its cash balances and future disbursement needs. All debt is intragovernmental and covered by budgetary resources. See additional details on borrowing authority in Note 10, Statement of Budgetary Resources.

Debt transactions for the period ending September 30, 2009, are:

	(*Dollars in Millions*)
Beginning Balance, Principal Payable to the BPD	$ -
New Borrowings	215,593
Repayments	(72,258)
Ending Balance, Principal Payable to the BPD	$ 143,335

Borrowings from the BPD by TARP Program that are outstanding as of September 30, 2009, are as follows:

	(*Dollars in Millions*)
Capital Purchase Program	$ 77,232
American International Group, Inc. Investment Program	12,531
Targeted Investment Program	20,460
Automotive Industry Financing Program	32,134
Consumer & Business Lending Initiative	204
Asset Guarantee Program	774
Total Borrowings Outstanding	$ 143,335

Borrowings are payable to the BPD as collections are available and carry terms ranging from 2 to 30 years. Interest rates on borrowings range from 1.0% to 4.5%. Interest expense for the period ended September 30, 2009, was $6.4 billion.

Note 9. Statement of Net Cost

The Statement of Net Cost (SNC) presents the net cost of operations for the OFS for the Department of the Treasury strategic goal of ensuring that U.S. and World economies perform at full economic potential. The OFS has determined that all initiatives and programs under the TARP fall within this strategic goal.

The OFS SNC reports the accumulated full cost of the TARP's output, including both direct and indirect costs of the program services and output identifiable to TARP, in accordance with SFFAS No. 4, *Managerial Cost Accounting Concepts and Standards*.

The OFS SNC includes approximately $6.4 billion of intragovernmental costs relating to interest expense on borrowings from the BPD and approximately $3.6 billion in intragovernmental revenues relating to interest income on financing account balances for the period ended September 30, 2009.

Subsidy Allowance Amortized on the SNC is the difference between interest income on financing fund account balances, dividends and interest income on direct loans, equity investments, and asset guarantees from TARP participants, and interest expense on borrowings from the BPD. Credit reform accounting requires all costs on the SNC for programs to be reflected only in the subsidy cost. The subsidy allowance account is used to present the loan or equity investment at the estimated net present value of future cash flows.

Note 10. Statement of Budgetary Resources

The Statement of Budgetary Resources (SBR) presents information about total budgetary resources available to the OFS and the status of those resources for the period ended September 30, 2009. The OFS's total budgetary resources were approximately $238.3 billion for the period ended September 30, 2009. Additionally, non-budgetary resources including borrowing authority and spending authority from collections of loan principal, liquidation of equity investments, interest and fees in financing funds were approximately $461.1 billion for the period ended September 30, 2009.

Permanent Indefinite Appropriations

The OFS receives permanent indefinite appropriations annually to fund increases in the projected subsidy costs of loans and the OFS investment programs as determined by the reestimation process required by the FCRA. The initial funding as a result of the reestimation process will occur in 2010.

Additionally, Section 118 of the EESA states that the Secretary may issue public debt securities and use the resulting funds to carry out the Act and that any such funds expended or obligated by the Secretary for actions authorized by this Act, including the payment of administrative expenses, shall be deemed appropriated at the time of such expenditure or obligation.

Borrowing Authority

The OFS is authorized to borrow from the BPD when funds needed to disburse direct loans and investments, and to enter into asset guarantee arrangements exceed subsidy costs and collections in the non-budgetary financing accounts. As of September 30, 2009, the OFS had available approximately $45.8 billion of borrowing authority.

The OFS uses dividends and interest received as well as principal repayments on direct loans and liquidation of equity investments to repay debt in the non-budgetary loan and investment financing accounts. These receipts are not available for any other use per credit reform accounting guidance.

Apportionment Categories of Obligations Incurred: Direct vs. Reimbursable Obligations

All of the OFS apportionments are Direct and are Category B. Category B apportionments typically distribute budgetary resources on a basis other than calendar quarters, such as by activities, projects, objects or a combination of these categories. The OFS obligations incurred are direct obligations (obligations not financed from reimbursements).

Undelivered Orders

Undelivered orders as of September 30, 2009, were approximately $56.1 billion in budgetary accounts, and approximately $79.2 billion in non-budgetary financing accounts.

Explanation of Differences Between the Statement of Budgetary Resources and the Budget of the United States Government

Federal agencies are required to explain material differences between amounts reported in the SBR and the actual amounts reported in the Budget of the U.S. Government (President's Budget). However, the President's Budget, which will include the FY 2009 actual amounts for OFS, has not yet been published. The President's Budget is expected to be published in February 2010 and will be made available from the U.S. Government Printing Office. Since the financial statements are published before the President's Budget, a reconciliation is to be performed between the prior year's SBR and the actual amounts for that year published in the prior year's President's Budget. Any significant differences identified from this reconciliation are to be explained in the federal agency's notes to its financial statements. Given that FY 2009 is the OFS's first year of operations, no prior year data was available to perform a comparison.

Note 11. Reconciliation of Obligations Incurred to Net Cost of Operations

The OFS presents the SNC using the accrual basis of accounting. This differs from the obligation-based measurement of total resources supplied, both budgetary and from other sources, on the SBR. The reconciliation of obligations incurred to net cost of operations shown below categorizes the differences between the two, and illustrates that the OFS maintains reconcilable consistency between the two types of reporting.

The Reconciliation of Obligations Incurred to Net Cost of Operations for the period ended September 30, 2009 is as follows:

	(Dollars in Millions)
Resources Used to Finance Activities:	
Obligations Incurred	$ 662,296
Spending Authority from Offsetting Collections	(271,999)
Offsetting Receipts	(2,720)
Total Resources Used to Finance Activities	387,577
Resources Used to Finance Items Not Part of Net Cost:	
Net Obligations in Loan and Investment Financing Funds	(180,185)
Increase in Resources Obligated for Items Ordered but not yet Provided	(56,073)
Total Resources Used to Finance Items Not Part of Net Cost	(236,258)
Resources Used to Finance Net Cost	151,319
Components of Net Cost That Will Not Require or Generate Resources in the Current Period:	
Downward Reestimate of Subsidy Cost	(109,748)
Other	2
Total Components of Net Cost Not Requiring or Generating Resources in the Current Period	(109,746)
Net Cost of Operations	$ 41,573

Required Supplementary Information

Office of Financial Stability (Troubled Asset Relief Program)
COMBINED STATEMENT OF BUDGETARY RESOURCES
For the Period Ended September 30, 2009

Dollars in Millions	Combined		TARP Programs		TARP Administrative Fund	
	Budgetary Accounts	Nonbudgetary Financing Accounts	Budgetary Accounts	Nonbudgetary Financing Accounts	Budgetary Accounts	Nonbudgetary Financing Accounts
BUDGETARY RESOURCES						
Unobligated Balances Brought Forward, Inception	$ -	$ -	$ -	$ -	$ -	$ -
Budget Authority:						
Appropriations	238,268	-	237,989	-	279	-
Borrowing Authority	-	309,971	-	309,971	-	-
Spending Authority from Offsetting Collections						
Earned: Collected	-	243,072	-	243,072	-	-
Change in Unfilled Orders Without Advance	-	28,927	-	28,927	-	-
Total Budget Authority	238,268	581,970	237,989	581,970	279	-
Permanently Not Available	-	(120,841)	-	(120,841)	-	-
TOTAL BUDGETARY RESOURCES	$ 238,268	$ 461,129	$ 237,989	$ 461,129	$ 279	$ -
STATUS OF BUDGETARY RESOURCES						
Obligations Incurred:						
Direct	$ 210,112	452,184	$ 209,863	452,184	$ 249	$ -
Unobligated Balance:						
Apportioned and Available	28,156	7,009	28,126	7,009	30	-
Not Available	-	1,936	-	1,936	-	-
TOTAL STATUS OF BUDGETARY RESOURCES	$ 238,268	$ 461,129	$ 237,989	$ 461,129	$ 279	$ -
CHANGE IN OBLIGATED BALANCES						
Obligated Balance Brought Forward, Inception	$ -	$ -	$ -	$ -	$ -	$ -
Obligations Incurred	210,112	452,184	209,863	452,184	249	-
Gross Outlays	(153,961)	(372,982)	(153,871)	(372,982)	(90)	-
Change in Uncollected Customer Payments from Federal Sources	-	(28,927)	-	(28,927)	-	-
Obligated Balance, Net, End of Period:						
Unpaid Obligations	56,151	79,202	55,992	79,202	159	-
Uncollected Customer Payments from Federal Sources	-	(28,927)	-	(28,927)	-	-
Obligated Balance, Net, End of Period	$ 56,151	$ 50,275	$ 55,992	$ 50,275	$ 159	$ -
NET OUTLAYS						
Gross Outlays	$ 153,961	$ 372,982	$ 153,871	$ 372,982	$ 90	$ -
Offsetting Collections	-	(243,072)	-	(243,072)	-	-
Distributed Offsetting Receipts	(2,720)	-	(2,720)	-	-	-
NET OUTLAYS	$ 151,241	$ 129,910	$ 151,151	$ 129,910	$ 90	$ -

Management's Report on Internal Control over Financial Reporting

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

Management's Report on Internal Control over Financial Reporting

The Office of Financial Stability's (OFS) internal control over financial reporting is a process effected by those charged with governance, management, and other personnel, the objectives of which are to provide reasonable assurance that (1) transactions are properly recorded, processed, and summarized to permit the preparation of financial statements in accordance with U.S. generally accepted accounting principles, and assets are safeguarded against loss from unauthorized acquisition, use, or disposition; and (2) transactions are executed in accordance with the laws governing the use of budget authority and other laws and regulations that could have a direct and material effect on the financial statements.

OFS management is responsible for establishing and maintaining effective internal control over financial reporting. OFS management evaluated the effectiveness of OFS' internal control over financial reporting as of September 30, 2009, based on the criteria established under 31 U.S.C. 3512(c), (d) (commonly known as the Federal Managers' Financial Integrity Act).

Based on that evaluation, we conclude that, as of September 30, 2009, OFS' internal control over financial reporting was effective.

Office of Financial Stability

Herbert M. Allison Jr.
Assistant Secretary for Financial Stability

Jennifer E. Main
Chief Financial Officer

December 4, 2009

Comments from the Office of Financial Stability

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

ASSISTANT SECRETARY

December 7, 2009

Mr. Gary T. Engel
Director, Financial Management and Assurance
U.S. Government Accountability Office

Dear Mr. Engel:

We have reviewed the draft Independent Auditor's Report concerning your audit of the Office of Financial Stability's fiscal year 2009 financial statements. As an organization in its first year executing complex programs unique in the Federal government, OFS is very proud to receive an unqualified opinion on our financial statements and an unqualified opinion on management's assertion that our internal controls were operating effectively. We are also proud that there were no reportable instances of noncompliance with laws or regulations.

Your audit report did identify two significant deficiencies in internal control in the areas of 1) accounting and financial reporting processes, and 2) verification procedures for data input into the credit subsidy models used for valuing loans, equity investments, and asset guarantees. We concur with these findings and are committed to pursuing remediation plans until the deficiencies are corrected.

We know that your audit team faced many of the same challenges we did in preparing these first year financial statements. We appreciated the professionalism and commitment demonstrated by your staff throughout the audit process. The audit process was valuable for us and resulted in concrete improvements in our operations and financial management efforts.

OFS is committed to maintaining the high standards and transparency reflected in these audit results as we carry out our responsibilities for managing the Troubled Asset Relief Program (TARP).

Sincerely,

Herb Allison
Assistant Secretary
Office of Financial Stability

GAO Contact and Staff Acknowledgments

GAO Contact

Gary T. Engel, (202) 512-3406 or engelg@gao.gov

Acknowledgments

The following individuals made key contributions to this report: Marcia L. Carlsen, Lynda E. Downing, Paul F. Foderaro, Joseph P. O'Neill (lead Assistant Directors); and Serena Agoro-Menyang, Cheryl E. Clark, Francis L. Dymond, Tony J. Eason, Lawrance L. Evans, Cynthia L. Grant, Natasha F. Guerra, Cole D. Haase, Brian S. Harechmak, Tyrone D. Hutchins, Arthur L. James, Jr., Charles E. Jones, Jason Scott Kirwan, Jeffrey L. Knott, Steven M. Koons, Damian Kudelka, Judy Lee, Robert E. Lee, John A. Long, Dragan Matic, Diane M. Monticchio, Tim Mooney, Mary V. Orsorno, Rebecca A. Riklin, Grant L. Simmons, Anne Y. Sit-Williams, John A. Spence, Monique B. Williams, Chris G. Yfantis, and Heneng Yu.

GAO's Mission

The Government Accountability Office, the audit, evaluation, and investigative arm of Congress, exists to support Congress in meeting its constitutional responsibilities and to help improve the performance and accountability of the federal government for the American people. GAO examines the use of public funds; evaluates federal programs and policies; and provides analyses, recommendations, and other assistance to help Congress make informed oversight, policy, and funding decisions. GAO's commitment to good government is reflected in its core values of accountability, integrity, and reliability.

Obtaining Copies of GAO Reports and Testimony

The fastest and easiest way to obtain copies of GAO documents at no cost is through GAO's Web site (www.gao.gov). Each weekday afternoon, GAO posts on its Web site newly released reports, testimony, and correspondence. To have GAO e mail you a list of newly posted products, go to www.gao.gov and select "E-mail Updates."

Order by Phone

The price of each GAO publication reflects GAO's actual cost of production and distribution and depends on the number of pages in the publication and whether the publication is printed in color or black and white. Pricing and ordering information is posted on GAO's Web site, http://www.gao.gov/ordering.htm.

Place orders by calling (202) 512-6000, toll free (866) 801-7077, or

TDD (202) 512-2537.

Orders may be paid for using American Express, Discover Card, MasterCard, Visa, check, or money order. Call for additional information.

To Report Fraud, Waste, and Abuse in Federal Programs

Contact:

Web site: www.gao.gov/fraudnet/fraudnet.htm
E-mail: fraudnet@gao.gov
Automated answering system: (800) 424-5454 or (202) 512-7470

Congressional Relations

Ralph Dawn, Managing Director, dawnr@gao.gov, (202) 512-4400
U.S. Government Accountability Office, 441 G Street NW, Room 7125
Washington, DC 20548

Public Affairs

Chuck Young, Managing Director, youngc1@gao.gov, (202) 512-4800
U.S. Government Accountability Office, 441 G Street NW, Room 7149
Washington, DC 20548