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Highlights

Highlights of GAO-10-719, a report to congressional committees

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FINANCIAL ASSISTANCE

Ongoing Challenges and Guiding Principles Related to Government Assistance For Private Sector Companies

Why GAO Did This Study

The recent financial crisis resulted in a wide-ranging federal response that included providing extraordinary assistance to several major corporations. As a result of actions under the Troubled Asset Relief Program (TARP) and others, the government was a shareholder in the American International Group Inc. (AIG); Bank of America; Citigroup, Inc. (Citigroup); Chrysler Group LLC (Chrysler); General Motors Company (GM); Ally Financial/GMAC, Inc. (GMAC); and Fannie Mae and Freddie Mac (Enterprises). The government ownership interest in these companies resulted from financial assistance that was aimed at stabilizing the financial markets, housing finance, or specific market segments. This report (1) describes the government's ownership interest and evaluates the extent of government involvement in these companies, (2) discusses the government's management and monitoring of its investments and exit strategies, and (3) identifies lessons learned from the federal actions.

This work was done in part with the Special Inspector General for the Troubled Asset Relief Program (SIGTARP) and involved reviewing relevant documentation related to these companies and the federal assistance provided. GAO interviewed officials at Treasury, Federal Reserve, Federal Housing Finance Agency (FHFA), and the banking regulators, as well as the senior executives and relevant officials at the companies that received exceptional assistance.

View GAO-10-719 or key components.
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What GAO Found

The extent of government equity interest in companies receiving exceptional assistance varied and ranged from owning preferred shares with no voting rights except in limited circumstances (Bank of America until it repurchased its shares in 2009) to owning common shares with voting rights (Chrysler, Citigroup, GM, and GMAC) to acting as a conservator (the Enterprises). In each case, the government required changes to the companies' corporate governance structures and executive compensation. For example, of the 92 directors currently serving on boards of these companies, 73 were elected since November 2008 (see table 1). Many of these new directors were nominated by their respective boards, while others were designated by the government and other significant shareholders as a result of their common share ownership. The level of involvement in the companies varied depending on whether the government served as an investor, creditor, or conservator. For example, as an investor in Bank of America, Citigroup, and GMAC, the Department of the Treasury (Treasury) had minimal or no involvement in their activities. As both an investor in and a creditor of AIG, Chrysler, and GM—as a condition of receiving assistance—the government has required some combination of the restructuring of their companies, the submission of periodic financial reports, and greater interaction with company personnel. FHFA—using its broad authority as a conservator—has instituted a number of requirements and practices that involve them in the Enterprises.

Table 1: Changes in Boards of Directors since November 2008

Company	Current number of directors	New directors since November 2008	Government-designated directors
AIG	13	8	2
Bank of America	13	10	none
Citigroup	15	8	none
GM	13	13	10
Chrysler	9	9	3
GMAC	9	8	3
Fannie Mae	10	8	10
Freddie Mac	10	9	10
Total	**92**	**73**	**38**

Source: SIGTARP and GAO analysis of government's agreements and company-provided data.

The government has taken a variety of steps to manage its investments and consider exit strategies. It developed guidance outlining its approach and hired asset managers to help manage some of its investments. Treasury's staff manage the investments of Chrysler, GM, and GMAC, including others. Also, the Federal Reserve and Treasury collaborate in monitoring the government's debt and preferred equity investments in AIG, while the AIG trustees appointed by the Federal Reserve are responsible for divesting the government's beneficial interest. Conversely, although FHFA is responsible for monitoring the Enterprises and Treasury holds the preferred equity investment, congressional action will be needed to determine the long-term structures and exit strategies for the Enterprises.

While the debate about whether the government should intervene in private markets to avert a systemic crisis continues, only the future will reveal whether the government is again faced with the prospect of having to intervene in private markets to avert a systemic crisis. As with other past crises, experience from the most recent crisis offers additional insights to guide government action, should it ever be warranted. -–

Specifically, the government could protect the taxpayer's interest in any crisis by not only continuing to follow the principles previously identified by GAO (i.e., identifying and defining the problem, determining a national interest and setting clear goals, and protecting the government's and taxpayer's interests) but also by adhering to five additional principles based on the federal government's experience with the current crisis. First, it is essential to develop a strategic and coordinated approach when comprehensive and global governmental action is required. Second, taking actions to ensure the government has a strategy for managing any investments resulting from its intervention is necessary to help mitigate perceived or potential conflicts and manage external influences. Third, the federal government's intervention in private markets requires that those efforts be transparent and effectively communicated. Fourth, establishing an adequate oversight structure to help ensure accountability is essential. And finally, taking steps to mitigate moral hazard will be necessary to not only ensure that regulatory and market-based structures limit risk taking before a crisis occurs, but to also create strong disincentives to seeking federal assistance through utilization of stringent requirements.

Table 2: GAO Framework for the Federal Government When Providing Financial Assistance to Private Market Participants

Principles	Description
Established guiding principles	
Identify and define the problem	Separating out those issues that require an immediate response from the structural challenges that will take longer to resolve.
Determine national interests and set clear goals and objectives	Choosing whether a legislative solution or other government intervention best serves the national interest.
Protect government's Interests	Ensure not only that financial markets continue to function effectively, but also that any investment provides the highest possible return. For example, requiring concessions from all parties, placing controls over management, obtaining collateral when feasible, and being compensated for risk.
New guiding principles	
Coordinate actions on a global and comprehensive basis	Financial crises that are international in scope require comprehensive, global actions, and government interventions must be closely coordinated by the parties providing assistance—including U.S. and foreign governments—to help ensure that limited resources are used effectively.
Mitigate perceived or potential conflicts	Any action that results in the government having an ownership interest in private sector companies requires that the government's strategy for managing its investments include plans to mitigate perceived or potential conflicts that may arise from its newly acquired role as shareholder or creditor and its existing role as regulator, supervisor, or policymaker.
Ensure adequate transparency by establishing an effective communication strategy	Federal intervention into the private markets requires a strategy to help ensure open and effective communication with Congress and taxpayers. An effective communication strategy is important during changing market events and could help the public understand the policy goals that the government is trying to achieve and its rationale for spending public funds.
Establish a strong system for accountability	A system of accountability helps ensure that the interest of the government and taxpayers are adequately protected and the programs' objectives are achieved efficiently and effectively. Monitoring and other internal controls can help prevent and detect fraud.
Take steps to mitigate moral hazard	Federal government's financial assistance may create moral hazard or encourage market participants to expect similar emergency actions—the too big to fail perception. The government should ensure that financial assistance to private market participants include terms that make it a last resort and specify when the assistance will end.

Source: GAO.