United States Government Accountability Office

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Report to Congressional Committees

March 2012

CAPITAL PURCHASE PROGRAM

Revenues Have Exceeded Investments, but Concerns about Outstanding Investments Remain

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Highlights

Highlights of GAO-12-301, a report to congressional committees

March 2012

CAPITAL PURCHASE PROGRAM

Revenues Have Exceeded Investments, but Concerns about Outstanding Investments Remain

Why GAO Did This Study

The Capital Purchase Program (CPP) was established as the primary means of restoring liquidity and stability to the financial system under the Troubled Asset Relief Program (TARP). Under CPP, the Department of the Treasury (Treasury) invested almost $205 billion in 707 eligible financial institutions between 2008 and December 2009. CPP recipients have made dividend and interest payments to Treasury on the investments. TARP's authorizing legislation requires GAO to report every 60 days on TARP activities, including those of CPP. This report examines (1) the status of CPP and (2) the financial condition of institutions receiving CPP investments.

GAO reviewed Treasury reports on the CPP program and participants and interviewed officials from Treasury and the financial regulators. Using financial and regulatory data, GAO compared the financial condition of institutions remaining in CPP with those that had exited the program and those that did not participate in CPP.

What GAO Recommends

To provide Congress and the public with more transparent and comprehensive information on institutions remaining in CPP and enhance its reporting, the Secretary of the Treasury should consider analyzing and reporting on remaining and former CPP participants separately. Treasury stated that it would carefully consider our recommendation.

View GAO-12-301. For more information, contact A. Nicole Clowers at (202) 512-8678 or clowersa@gao.gov.

What GAO Found

While repayments, dividends, and interest from institutions participating in the Capital Purchase Program (CPP) have exceeded the program's original investment disbursements, the number of missed payments has increased over the life of the program. As of January 31, 2012, the Department of the Treasury (Treasury) had received $211.5 billion from its CPP investments, exceeding the $204.9 billion it had disbursed. Of that amount, $16.7 billion remains outstanding, and most of these investments were concentrated in a relatively small number of institutions. In particular, as of January 31, 2012, 25 institutions accounted for $11.2 billion, or 67 percent, of outstanding investments. As of November 30, 2011, Treasury estimated that CPP would have a lifetime income of $13.5 billion after all institutions exited the program. As of January 31, 2012, 341 institutions had exited CPP, almost half by repaying CPP with funds from other federal programs. Institutions continue to exit CPP, but the number of institutions missing scheduled dividend or interest payments has increased. For example, as of November 30, 2011, the number of institutions that had missed their quarterly payments rose to 158, a marked increase from 8 in February 2009, even though CPP had fewer participants. The number of CPP institutions designated as problem banks—that is, demonstrating financial, operational, or managerial weaknesses that threatened their continued financial viability—also rose from 47 in December 2009 to 130 in December 2011. Institutions that continue to miss payments and problem institutions may have difficulty ever fully repaying their CPP investments.

GAO's analysis showed that the remaining CPP institutions were financially weaker than institutions that had exited the program and institutions that did not receive CPP capital. In particular, the remaining CPP institutions tended to be less profitable and hold riskier assets than other institutions of similar asset size. Among other things, they had significantly lower returns on average assets and higher percentages of noncurrent loans than former CPP and non-CPP institutions. They also held less regulatory capital and reserves for covering losses. Although GAO's analysis found differences in the financial health of remaining and former CPP institutions, Treasury's quarterly financial analysis of CPP institutions did not distinguish between them. In prior work, GAO has noted the importance of providing clear information to Congress and the public about the performance of the assistance provided through the various programs within the Troubled Asset Relief Program. By distinguishing between remaining and former CPP participants, Treasury could provide greater transparency about the financial health of institutions remaining in CPP.

Contents

Abbreviations

CDCI	Community Development Capital Initiative
CPP	Capital Purchase Program
EESA	Emergency Economic Stabilization Act of 2008
FDIC	Federal Deposit Insurance Corporation
Federal Reserve	Board of Governors of the Federal Reserve System
OCC	Office of the Comptroller of the Currency
OFS	Office of Financial Stability
OTS	Office of Thrift Supervision
SBLF	Small Business Lending Fund
TARP	Troubled Asset Relief Program
Treasury	U.S. Department of the Treasury

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United States Government Accountability Office
Washington, DC 20548

March 8, 2012

Congressional Committees

From October 2008 through December 2009, the U.S. Department of the Treasury (Treasury) invested almost $205 billion in 707 financial institutions as part of the government's efforts to help stabilize U.S. financial markets and the economy. These investments were made through the Capital Purchase Program (CPP), which was the first and largest initiative under the Troubled Asset Relief Program (TARP).[1] Specifically, Treasury's authority under TARP enabled it to buy or guarantee up to almost $700 billion of the "troubled assets" that it deemed to be at the heart of the crisis, including mortgages, mortgage-backed securities, and any other financial instruments, such as equity investments.[2] Treasury created CPP in October 2008 to provide capital to viable financial institutions by using its authority to purchase preferred shares and subordinated debt. In return for its investments, Treasury received dividend or interest payments and warrants.[3] The program was closed to new investments on December 31, 2009, and since then Treasury has continued to oversee its CPP investments and collect dividend and interest payments and sell warrants. Some participants have repurchased their preferred shares or subordinated debt and exited the program with the approval of their primary bank regulators.

[1]As authorized by 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. EESA was signed into law on October 3, 2008, to help stem the worst financial crisis since the 1930s. EESA established the Office of Financial Stability within Treasury and provided it with broad, flexible authorities to buy or guarantee troubled mortgage-related assets or any other financial instruments necessary to stabilize the financial markets.

[2]Section 3(9) of the Emergency Economic Stabilization Act of 2008 (EESA), 12 U.S.C. § 5202(9). EESA required that the appropriate committees of Congress be notified in writing that the Secretary of the Treasury, after consultation with the Chairman of the Board of Governors of the Federal Reserve System, had determined that it was necessary to purchase other financial instruments to promote financial market stability. EESA originally authorized Treasury to purchase or guarantee up to $700 billion in troubled assets. The Helping Families Save Their Homes Act of 2009, Pub. L. No. 111-22, Div. A, 123 Stat. 1632 (2009), amended EESA to reduce the maximum allowable amount of outstanding troubled assets under EESA by almost $1.3 billion, from $700 billion to $698.7 billion.

[3]A warrant is an option to buy shares of common stock or preferred stock at a predetermined price on or before a specified date.

Rather than purchasing troubled mortgage-backed securities and whole loans, as initially envisioned under TARP, Treasury used CPP investments to strengthen financial institutions' capital levels. Treasury determined that strengthening capital levels was the more effective mechanism to help stabilize financial markets, encourage interbank lending, and increase confidence in lenders and investors. Treasury believed that strengthening the capital positions of viable financial institutions would enhance confidence in the institutions themselves and the financial system overall and increase the institutions' capacity to undertake new lending and support the economy. Financial institutions interested in receiving CPP investments sent their applications directly to their primary federal banking regulators, which performed the initial evaluations. Institutions were evaluated to determine their long-term strength and viability, and weaker institutions were encouraged by their regulators to withdraw their applications. Treasury's Office of Financial Stability (OFS), established to implement TARP, made the final decisions, although the regulators provided recommendations for approving or denying applications. In October 2010, we reported that while Treasury's processes included multiple reviews of CPP applicants, certain operational control weaknesses offered "lessons learned" for similarly designed programs, such as the Small Business Lending Fund (SBLF).[4]

This report is based upon our continuing analysis and monitoring of Treasury's activities in implementing the Emergency Economic Stabilization Act of 2008 (EESA), which provided us with broad oversight authorities for actions taken under TARP and required that we report at least every 60 days on TARP activities and performance.[5] To fulfill our statutorily mandated responsibilities, we have been monitoring and providing updates on TARP programs, including CPP, and this report

[4]SBLF was a $30 billion fund separate from TARP that provided capital to qualified community banks and community development loan funds with assets of less than $10 billion in an effort to encourage small business lending. SBLF provided an option for eligible institutions to refinance preferred stock issued to Treasury through CPP or the Community Development Capital Initiative under certain conditions. See GAO, *Small Business Lending Fund: Additional Actions Needed to Improve Transparency and Accountability*, GAO-12-183 (Washington, D.C.: Dec. 14, 2011).

[5]Section 116 of EESA, 122 Stat. at 3783 (codified at 12 U.S.C. § 5226).

expands on that work.[6] This report examines (1) the status of CPP, including repayments and other proceeds, restructuring of investments, and timeliness of dividend payments, and (2) the financial condition of institutions that received investments under CPP compared with institutions that have exited CPP and those that did not participate in the program.

To assess the status of CPP, we analyzed Treasury's reports, which included the amount of investments outstanding, the number of institutions that had repaid their investments, and the amount of dividends paid, among other things. We also interviewed Treasury officials responsible for the program. To assess the financial condition of institutions that received investments under CPP, we used financial and regulatory data to compare the financial condition of institutions that received CPP investments with those that did not. We determined that the financial information we used was sufficiently reliable to assess the condition and status of CPP and institutions that participated in the program. We also leveraged our past reporting on TARP, as well as that of the Special Inspector General for TARP, as appropriate. Appendix I has more information on our scope and methodology.

We conducted this performance audit from August 2011 to March 2012 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

Created in 2008, CPP was the primary initiative under TARP to help stabilize the financial markets and banking system by providing capital to qualifying regulated financial institutions through the purchase of senior

[6]See, for example, GAO, *Troubled Asset Relief Program: Opportunities Exist to Apply Lessons Learned from the Capital Purchase Program to Similarly Designed Programs and to Improve the Repayment Process*, GAO-11-47 (Washington, D.C.: Oct. 4, 2010), and *Troubled Asset Relief Program: As Treasury Continues to Exit Programs, Opportunities to Enhance Communication on Costs Exist*, GAO-12-229 (Washington, D.C.: Jan. 9, 2012).

preferred shares and subordinated debt.[7] On October 14, 2008, Treasury allocated $250 billion of the original $700 billion in overall TARP funds for CPP. The allocation was subsequently reduced in March 2009 to reflect lower estimated funding needs, as evidenced by actual participation rates. The program was closed to new investments on December 31, 2009.

Under CPP, qualified financial institutions were eligible to receive an investment of between 1 and 3 percent of their risk-weighted assets, up to a maximum of $25 billion.[8] In exchange for the investment, Treasury generally received senior preferred shares that would pay dividends at a rate of 5 percent annually for the first 5 years and 9 percent annually thereafter.[9] EESA required that Treasury also receive warrants to purchase shares of common or preferred stock or a senior debt instrument to further protect taxpayers and help ensure returns on the investments. Institutions are allowed to repay CPP investments with the approval of their primary federal bank regulator and afterward to repurchase warrants at fair market value.

While CPP was Treasury's program, federal banking regulators played a key role in the application and approval process, receiving and reviewing CPP applications, and recommending approval or denial. The banking regulators that participated in CPP included:

- *Board of Governors of the Federal Reserve System* (Federal Reserve), which supervised and regulated banks that were authorized to do business under state charters and that were members of the

[7]For purposes of CPP, qualifying financial institutions generally include stand-alone U.S.-controlled banks and savings associations, as well as bank holding companies and most savings and loan holding companies.

[8]Risk-weighted assets are all assets and off-balance-sheet items held by an institution, weighted for risk according to the federal banking agencies' regulatory capital standards. In May 2009, Treasury increased the maximum amount of CPP funding that small financial institutions (qualifying financial institutions with total assets of less than $500 million) could receive from 3 to 5 percent of risk-weighted assets.

[9]For S corporations, a federal business type that provides certain tax and other benefits, Treasury received subordinated debt rather than preferred shares in order to preserve these institutions' special tax status. The U.S. Internal Revenue Code prohibits S corporations from having more than one class of stock outstanding. Interest rates for this debt are 7.7 percent for the first 5 years and 13.8 percent for the remaining years.

Federal Reserve System, as well as bank and financial holding companies;[10]

- *Federal Deposit Insurance Corporation* (FDIC), which provided primary federal oversight of any state-chartered banks that were not members of the Federal Reserve System;

- *Office of the Comptroller of the Currency* (OCC), which was responsible for chartering, regulating, and supervising commercial banks with national charters; and

- *Office of Thrift Supervision* (OTS), which chartered federal savings associations (thrifts) and regulated and supervised federal and state thrifts and savings and loan holding companies. OTS has since been eliminated.[11]

Treasury, in consultation with the federal banking regulators, developed a standardized framework for processing applications and disbursing CPP funds (see fig. 1). Treasury encouraged financial institutions that were considering applying to CPP to consult with their primary federal bank regulators.[12] Eligibility was based on the regulator's assessment of applicants' strength and viability—as measured by examination ratings, financial performance ratios, and other mitigating factors—without taking into account the potential impact of TARP funds. Institutions deemed to be the strongest, such as those with the highest examination ratings, received presumptive approval from the banking regulators, and their applications were forwarded to Treasury. Institutions with lower examination ratings or other concerns that required further review were

[10]Bank holding companies are entities that own or control one or more U.S. commercial banks. Financial holding companies are a subset of bank holding companies that may engage in a wider range of activities.

[11]The Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, Title III, 124 Stat. 1376, 1520 (2010), eliminated OTS. Rulemaking authority previously vested in OTS was transferred to OCC for savings associations and to the Federal Reserve for savings and loan holding companies. Supervisory authority was transferred to OCC for federal savings associations, to FDIC for state savings associations, and to the Federal Reserve for savings and loan holding companies and their subsidiaries, other than depository institutions. The transfer of these powers was completed on July 21, 2011, and OTS was officially dissolved on October 19, 2011.

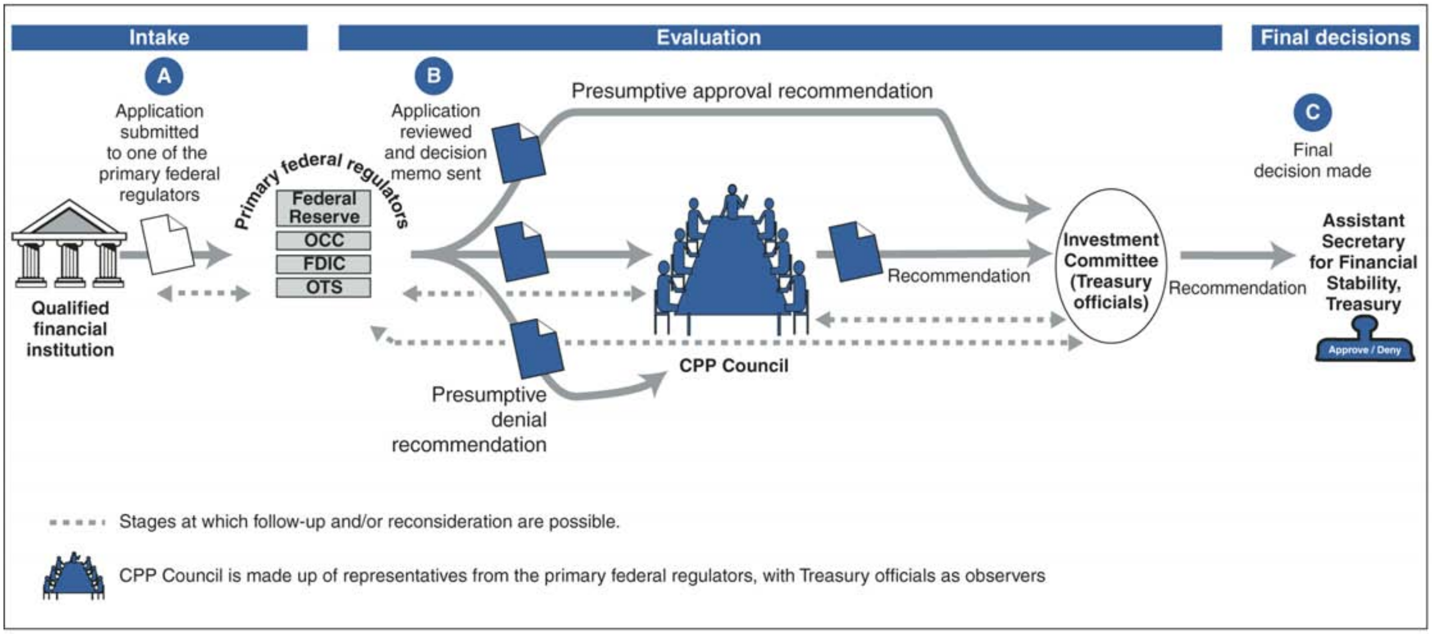
[12]The primary federal regulator is generally the regulator overseeing the lead bank. Primary federal regulators of bank holding companies also consult with the Federal Reserve.

referred to an interagency CPP Council composed of representatives from the four banking regulators, with Treasury officials as observers. The CPP Council evaluated and voted on the applicants, forwarding to Treasury applications that received "approval" recommendations from a majority of the council members. Treasury provided guidance to regulators and the CPP Council to use in assessing applicants that permitted consideration of factors such as signed merger agreements or confirmed investments of private capital, among other things, to offset low examination ratings or other attributes of weaknesses. Finally, institutions that the banking regulators determined to be the weakest and thus ineligible for a CPP investment, such as those with the lowest examination ratings, received a presumptive denial recommendation.[13]

The banking regulators or the CPP Council sent recommendations for approval to Treasury's Investment Committee, which was composed of three to five senior Treasury officials, including OFS's Chief Investment Officer (who served as the committee chair) and the assistant secretaries for financial markets, economic policy, financial institutions, and financial stability at Treasury. The Investment Committee could also request additional analysis or information in order to clear up any concerns before deciding on an applicant's eligibility. After completing its review, the Investment Committee made recommendations to the Assistant Secretary for Financial Stability for final approval. Once the Investment Committee recommended preliminary approval, Treasury and the approved institution initiated the closing process to complete the investment and disburse the CPP funds.

[13]For a discussion of our assessment of the CPP approval process, see GAO-11-47.

Figure 1: Process for Accepting and Approving CPP Applications



Sources: GAO analysis; Treasury; Art Explosion (images).

Note: If the applicant was a bank holding company, an application was submitted to both the applicant's holding company regulator and the regulator of the largest insured depository institution controlled by the applicant.

Nine major financial institutions were initially included in CPP.[14] These institutions did not follow the application process that was ultimately developed but were included because Treasury and the federal banking regulators considered them essential to the operation of the financial system. At the time, these nine institutions held about 55 percent of U.S. banking assets and provided a variety of services, including retail, wholesale, and investment banking and custodial and processing services. According to Treasury officials, the nine financial institutions agreed to participate in CPP in part to signal the program's importance to the stability of the financial system. Initially, Treasury approved $125 billion in capital purchases for these institutions and completed the

[14]The nine major financial institutions were Bank of America Corporation; Citigroup, Inc.; JPMorgan Chase & Co.; Wells Fargo & Company; Morgan Stanley; The Goldman Sachs Group, Inc.; The Bank of New York Mellon Corporation; State Street Corporation; and Merrill Lynch & Co., Inc.

transactions with eight of them on October 28, 2008, for a total of $115 billion. The remaining $10 billion was disbursed after the merger of Bank of America Corporation and Merrill Lynch & Co., Inc. was completed in January 2009.

Treasury Estimates a Lifetime Gain for CPP, but Concerns about Some Investments Remain

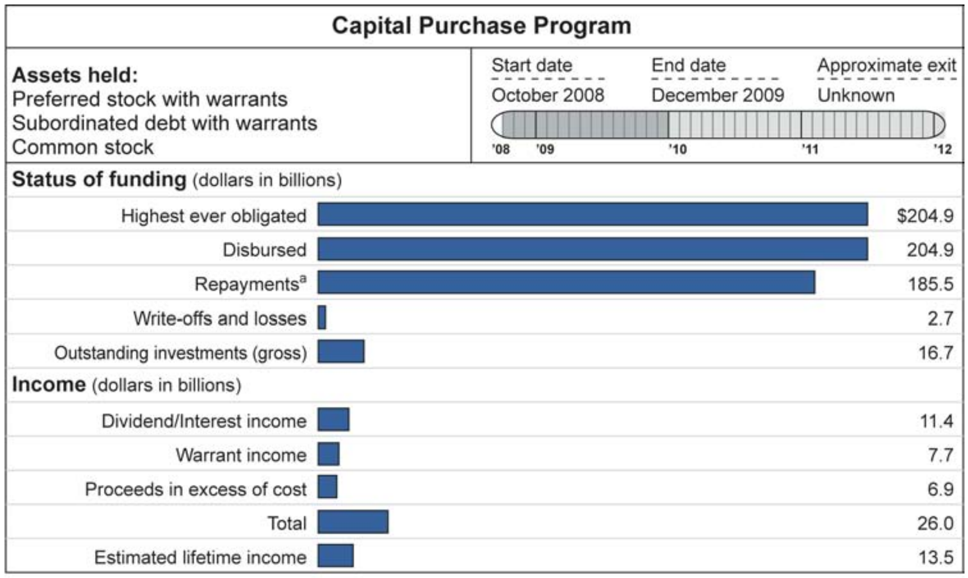
Repayments and income from dividends, interest, and warrants from CPP investments have exceeded the amounts originally disbursed, but concerns remain about the financial strength of the remaining institutions and their ability to repay and exit the program. As we have reported, Treasury disbursed $204.9 billion to 707 financial institutions nationwide from October 2008 through December 2009.[15] As of January 31, 2012, Treasury had received $211.5 billion in repayments and income from its CPP investments, exceeding the amount originally disbursed by $6.6 billion (see fig. 2).[16] The repayments and income amount included $185.5 billion in repayments of original CPP investments as well as $11.4 billion in dividends, interest, and fees; $7.7 billion in warrants sold; and $6.9 billion in gains from the sale of Citigroup common stock. After accounting for write-offs and realized losses totaling $2.7 billion, CPP had $16.7 billion in outstanding investments as of January 31, 2012. Although this $16.7 billion is still potentially at risk, Treasury estimated a lifetime gain of $13.5 billion for CPP as of November 30, 2011.[17]

[15] See GAO-12-229.

[16] Treasury, *Troubled Asset Relief Program (TARP) Monthly 105(a) Report – January 2012* (Feb. 10, 2012).

[17] Treasury estimates lifetime costs on a quarterly basis in conjunction with the Office of Management and Budget and publishes them in its monthly 105(a) reports.

Figure 2: Status of CPP, as of January 31, 2012

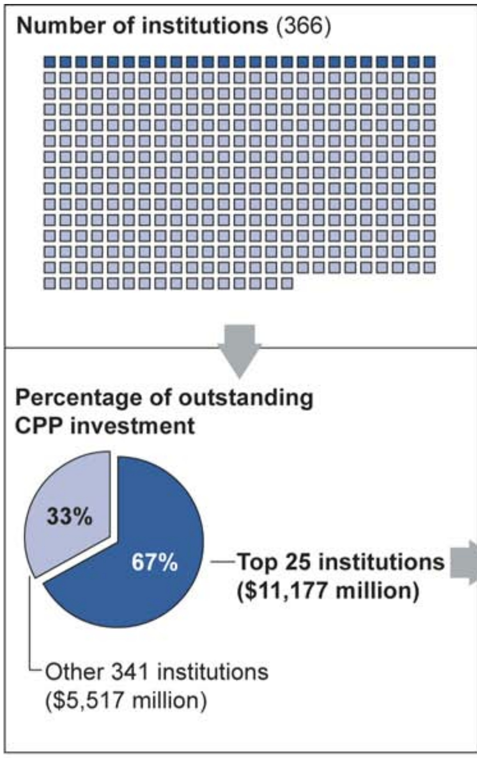


Source: GAO analysis of Treasury data.

[a]The total amount of repayments includes $336 million from institutions that transferred to the Community Development Capital Initiative and $2.2 billion from institutions that transferred to the Small Business Lending Fund.

As of January 31, 2012, 52 percent (366) of the original 707 institutions remained in CPP. These institutions accounted for $16.7 billion in outstanding investments, or 8 percent of the original amount disbursed. About two-thirds of the outstanding investments were concentrated in a relatively small number of institutions (see fig. 3). Specifically, 25 remaining CPP investments accounted for $11.2 billion, or 67 percent of outstanding investments. In contrast, the remaining $5.5 billion (33 percent) was spread among 341 institutions.

Figure 3: Remaining CPP Investments, as of January 31, 2012



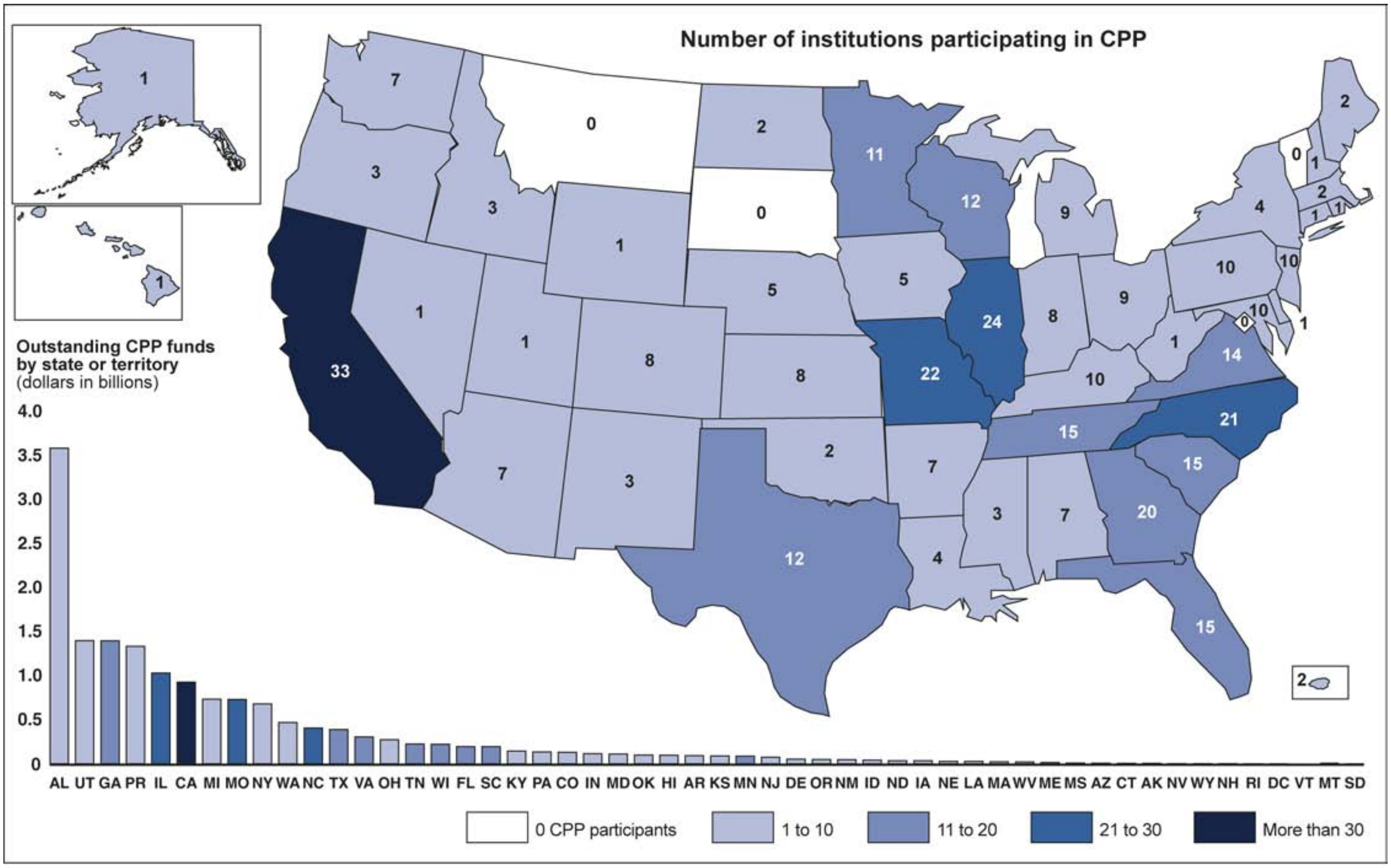
Outstanding CPP investment by top 25 institutions

	Institution	Location	Investment amount (in millions)	Percentage of total outsanding investment	
1	Regions Financial Corp.	Birmingham, AL	$3,500.0	21.0%	
2	Zions Bancorporation	Salt Lake City, UT	1,400.0	8.4	
3	Synovus Financial Corp.	Columbus, GA	967.9	5.8	
4	Popular, Inc.	Hato Rey, PR	935.0	5.6	
5	First Bancorp	San Juan, PR	400.0	2.4	
6	M&T Bank Corporation	Buffalo, NY	381.5	2.3	45.4%
7	Sterling Financial Corporation	Spokane, WA	303.0	1.8	
8	Citizens Republic Bancorp, Inc.	Flint, MI	300.0	1.8	
9	First Banks, Inc.	Clayton, MO	295.4	1.8	
10	New York Private Bank & Trust Corp.	New York, NY	267.3	1.6	
11	Flagstar Bancorp, Inc.	Troy, MI	266.7	1.6	
12	Cathay General Bancorp	El Monte, CA	258.0	1.5	
13	PrivateBancorp, Inc.	Chicago, IL	243.8	1.5	
14	International Bancshares Corporation	Laredo, TX	216.0	1.3	
15	MB Financial Inc.	Chicago, IL	196.0	1.2	
16	Pacific Capital Bancorp	Santa Barbara, CA	180.6	1.1	
17	United Community Banks, Inc.	Blairsville, GA	180.0	1.1	
18	Dickinson Financial Corporation II	Kansas City, MO	146.1	0.9	
19	Banner Corporation	Walla Walla, WA	124.0	0.5	
20	BBCN Bancorp, Inc.	Los Angeles, CA	122.0	0.7	
21	Anchor BanCorp Wisconsin, Inc.	Madison, WI	110.0	0.7	
22	Taylor Capital Group	Rosemont, IL	104.8	0.7	
23	Park National Corporation	Newark, OH	100.0	0.6	
24	Central Pacific Financial Corp.	Honolulu, HI	98.7	0.6	
25	Hampton Roads Bankshares, Inc.	Norfolk, VA	80.3	0.6	21.5%
	Total top 25		**$11,177.1**	**67.0%**	**67.0%**
	All other CPP outstanding		$5,516.7	33.0%	
	All CPP outstanding		$16,693.8	100.0%	

Source: GAO analysis of Treasury data.

On a geographical basis, outstanding CPP investments were relatively widely disbursed throughout the United States as of January 31, 2012. All but 3 states and the District of Columbia had at least 1 institution with CPP investments outstanding, and 25 states had at least 5 such institutions (see fig. 4). California had the highest number of remaining CPP institutions with 33, followed by Illinois with 24. These states also had the highest number of original CPP recipients (72 and 45, respectively). In terms of total CPP investments outstanding, however, Alabama had the largest amount ($3.6 billion), followed by Utah ($1.4 billion), Georgia ($1.4 billion), and Puerto Rico ($1.3 billion).

Figure 4: Remaining Participation in CPP by State, as of January 31, 2012



Sources: GAO analysis of Treasury data: Map Resources (map).

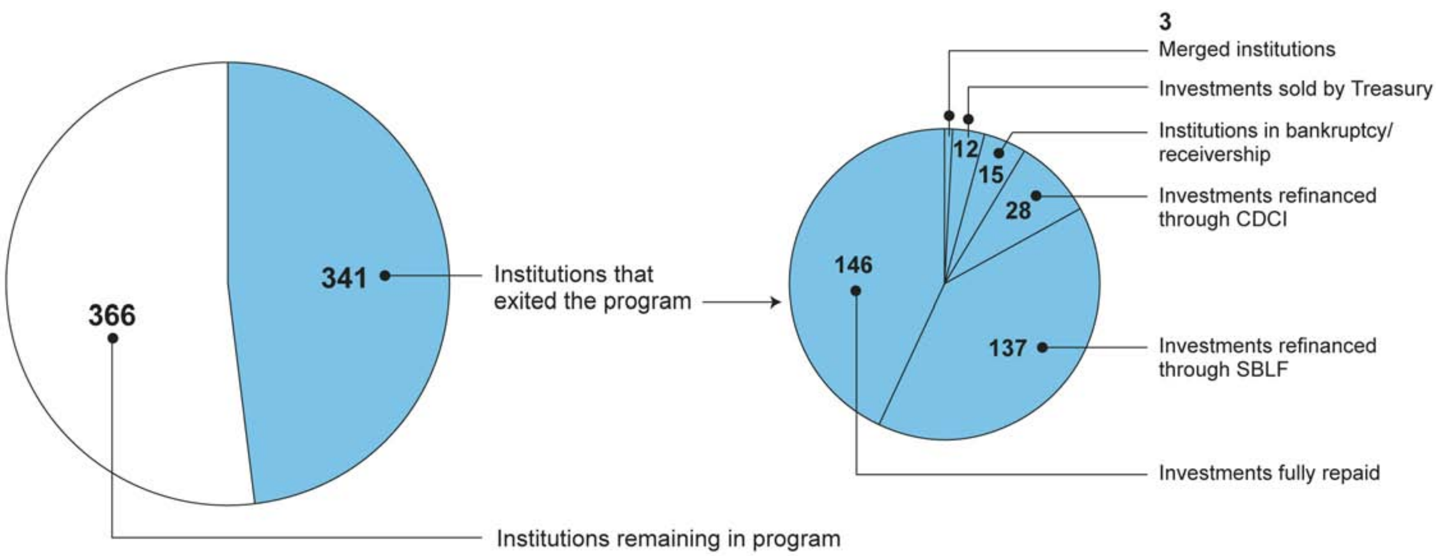
Institutions Continue to Exit CPP, with Many Using SBLF

Nearly half (341) of the 707 institutions that originally participated in CPP had exited the program as of January 31, 2012. Of the 341 institutions that exited CPP, 43 percent, or 146 institutions, exited by fully repaying their investments.[18] Another 48 percent, or 165 institutions, exited CPP by exchanging their investments under other federal programs: 28 through the Community Development Capital Initiative (CDCI) and 137 through

[18]Additionally, 11 institutions have made partial repayments but remain in the program.

the SBLF program (see fig. 5).[19] Finally, of the remaining 9 percent of CPP recipients that exited the program, 15 went into bankruptcy or receivership, 12 had investments sold by Treasury, and 3 merged with another institution.

Figure 5: Institutions That Received CPP Investments, as of January 31, 2012



Source: GAO analysis of Treasury data.

[19] CDCI is a TARP program that provides capital to Community Development Financial Institutions that have a federal depository institution supervisor. The program is structured like CPP but expands to credit unions and provides more favorable capital terms. SBLF was created by the Small Business Jobs Act of 2010, Pub. L. No. 111-240, 124 Stat. 2504 (2010), enacted on September 27, 2010. SBLF is a $30 billion capital support program, separate from TARP, that encourages small and midsize banks and community development loan funds to lend to small businesses. When SBLF closed on September 27, 2011, the program had approved $4 billion in disbursements to 332 institutions. Of the 332 institutions participating in SBLF, 137 institutions were originally TARP participants with combined investments of $2.2 billion.

An Increasing Number of Remaining CPP Participants Have Missed Dividend or Interest Payments and Appeared on FDIC's Problem Bank List

The number of institutions remaining in the program continues to decrease as CPP investments are repaid. However, a growing number of the remaining institutions have missed scheduled dividend or interest payments or appeared on FDIC's problem bank list. As a result, there is increased concern regarding the speed at which institutions will be able to repay remaining funds and how much of these funds Treasury will ultimately recover.

The Number of Remaining CPP Participants That Have Missed Dividend or Interest Payments Has Increased

The cumulative number of financial institutions that had missed at least one scheduled dividend or interest payment by the end of the month in which the payments were due rose from 164 as of November 30, 2010, to 226 as of November 30, 2011.[20] Dividend or interest payments are due on a quarterly basis, but institutions can elect whether to pay dividends and may choose not to pay for a variety of reasons. For example, the institution or its federal and state regulators may decide not to pay dividends to conserve cash and maintain (or increase) capital levels. Further, institutions are required to pay dividends only if they declare dividends, although unpaid cumulative dividends generally accrue and the institution must pay them before making payments to other types of shareholders, such as holders of common stock. However, investors view a company's ability to pay dividends as an indicator of its financial strength and may see failure to pay full dividends as a sign of financial weakening.

The 226 institutions that had missed at least one payment had missed a cumulative total of 1,170 payments.[21] As of November 30, 2011, 184 institutions had missed 3 or more payments, and 97 of these institutions had missed 6 or more. The total amount of missed dividend and interest payments was $429 million, although some of these payments were later made prior to the end of the reporting month. On a quarterly basis, the

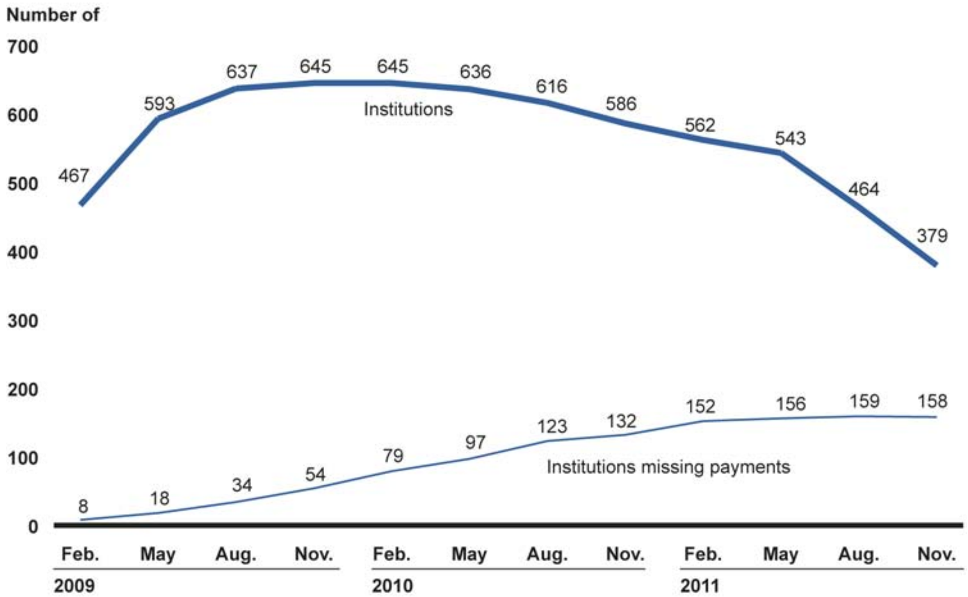
[20]Under CPP terms, institutions pay cumulative dividends on their preferred shares, except for banks that are not subsidiaries of holding companies, which pay noncumulative dividends. Some other types of institutions, such as S corporations, received their CPP investments in the form of subordinated debt and pay Treasury interest rather than dividends.

[21]CPP dividend and interest payments are due on February 15, May 15, August 15, and November 15 of each year, or the first business day subsequent to those dates. The reporting period ends on the last day of the calendar month in which the dividend or interest payment is due.

number of institutions missing dividend or interest payments due on their CPP investments increased steadily from 8 in February 2009 to 158 in November 2011, or about 42 percent of institutions still in the program (see fig. 6).[22] This increase has occurred while program participation has declined, and the proportion of those missing scheduled payments has risen accordingly. The number of institutions missing payments has stabilized since February 2011, but most of these institutions continued to miss them. In particular, 119 of the 158 institutions that missed payments in November 2011 had also missed payments in each of the previous three quarters. Moreover, only 7 of the 158 institutions had never missed a previous payment.

[22] In its dividend and interest reports, Treasury no longer considers a payment to be missed or unpaid once the institution (1) repays its investment amount and exits CPP, (2) repays dividends by way of capitalization at the time of exchange, or (3) enters bankruptcy or has its bank subsidiary placed into receivership; however, we included such institutions in our counts.

Figure 6: Number of Institutions Missing Scheduled Dividend or Interest Payments and Number of Institutions Participating in CPP, by Quarter, February 2009 through November 2011



Source: GAO analysis of Treasury data.

Note: Dividend and interest payments are due on a quarterly basis. The number of participating institutions in any given quarter did not reach 707 (that is, the total number of institutions that participated in CPP) because institutions entered and exited the programs at different times. Also, 379 institutions remained in CPP as of November 30, 2011, but as of January 31, 2012, that number had decreased to 366.

On July 19, 2011, Treasury announced that it had, for the first time, exercised its right to elect members to the boards of directors of two of the remaining CPP institutions.[23] In considering whether to nominate directors, Treasury said that it proceeds in two steps. First, after an institution misses five dividend or interest payments, Treasury sends OFS staff members to observe board meetings. Second, once an institution has missed six dividend payments, Treasury decides whether to nominate a board member based on a variety of considerations, including what it learns from the board meetings, the institution's financial condition,

[23]According to the standard terms of CPP, after participants have missed six dividend payments—consecutive or not—Treasury can exercise its right to appoint two members to the board of directors for that institution.

the function of its board of directors, and the size of its investment.[24] As of January 31, 2012, Treasury had elected 12 board members to 7 CPP institutions.

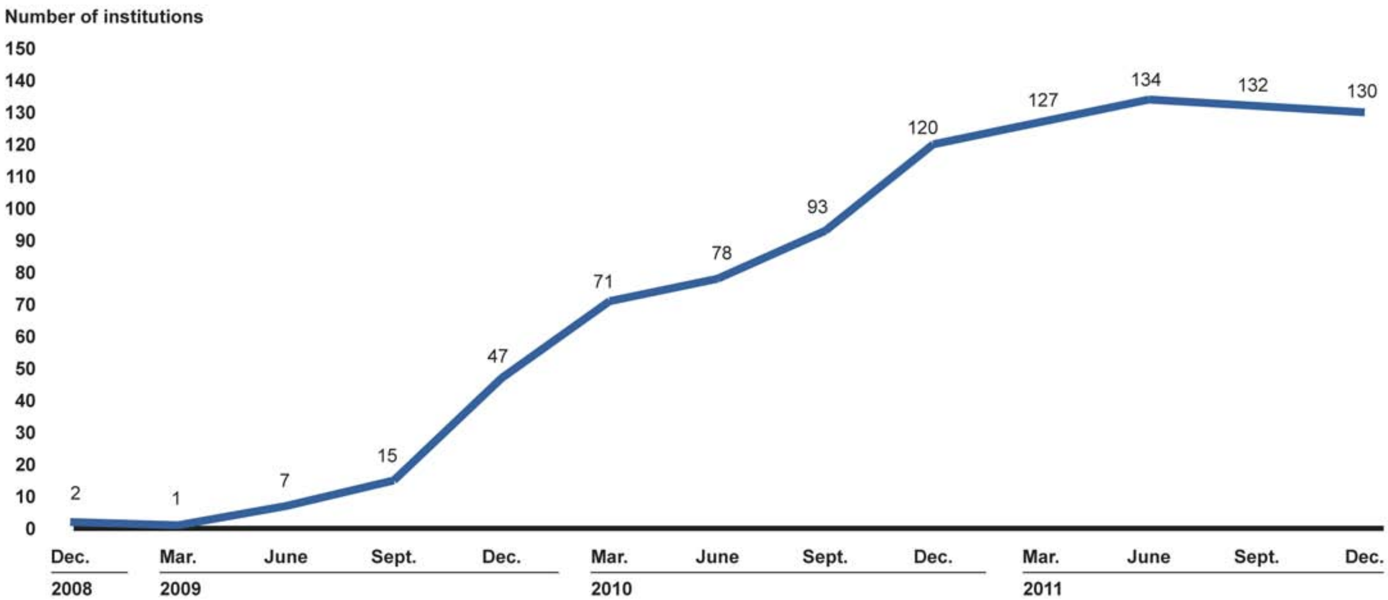
The Number of Remaining CPP Institutions on FDIC's Problem Bank List Has Also Increased

At the same time that the number of institutions missing dividend payments has risen, the number of CPP institutions on FDIC's problem bank list has generally increased. FDIC compiles a list of banks with demonstrated financial, operational, or managerial weaknesses that threaten their continued financial viability and publicly reports the number of such institutions on a quarterly basis. While some CPP funds were disbursed to bank holding companies, FDIC's problem bank list does not include them. FDIC accounted for bank holding companies participating in CPP when their subsidiary depositories were designated as problem banks. It is possible that a bank holding company CPP recipient downstreamed CPP funds to a subsidiary depository that appeared on the problem bank list. However, it is unclear the extent to which this downstreaming occurred and thus the extent to which subsidiaries on the list may have benefitted from CPP funds.[25] As of December 31, 2009, 47 CPP institutions were on the problem bank list (see fig. 7). This number had grown to 120 institutions by December 31, 2010, and to 130 by December 31, 2011. The number of these institutions increased every quarter from March 2009 to June 2011 and rose even as the number of institutions participating in CPP declined. As figure 7 shows, the number of problem banks fell slightly for the first time in the third quarter of 2011. Federal and state bank regulators may not allow such institutions to make dividend payments in an effort to preserve their capital and promote safety and soundness.

[24]Treasury reported that it might not nominate directors immediately after an institution missed six payments but would develop a pool of candidates screened by executive search firms it engaged. Board members whom Treasury nominates cannot be government employees and must have the same fiduciary duties and obligations to the institution's shareholders as any other member of the board and receive the same compensation from the institution.

[25]Multiple subsidiary depositories of the same CPP bank holding company that were designated as problem banks were counted separately.

Figure 7: Number of CPP Institutions on FDIC's Problem Bank List, December 2008 through December 2011



Source: FDIC.

Note: The numbers presented in figure 7 were compiled by FDIC in response to our request and are not otherwise maintained or published by FDIC. FDIC's problem bank list does not include bank holding companies. Bank holding company recipients of CPP funds were accounted for if one or more of their subsidiary depositories were designated as problem banks. Each subsidiary depository appearing on the list was counted separately.

The Financial Strength of CPP Participants is a Key Consideration in Exiting the Program

The financial strength of the participating institutions will largely determine the speed at which they repay their investments and exit CPP and thus is a key factor in the program's total lifetime income. Institutions will have to demonstrate that they are financially strong enough to repay their CPP investments in order to receive regulatory approval to exit the program. The institutions' financial strength will also be a primary factor in whether they make dividend payments, and institutions that continue to miss payments may have difficulty exiting CPP. Financial institutions that are on the problem bank list because of their financial weaknesses, as identified by their regulators, may also face challenges exiting the program. In late 2013, CPP dividend and interest rates will begin increasing (as described earlier), and the increase may prompt institutions to repay their investments more quickly. If broader interest rates are low, especially approaching the date that the dividend resets, banks could have a further incentive to redeem their preferred shares.

However, the increased dividend rate could make exiting even more difficult for problem banks and those that have missed payments.

As we have previously reported, in unwinding TARP programs, Treasury has stated that it strives to protect taxpayer investment and maximize overall investment returns with competing constraints, promote the stability of financial markets and the economy by preventing disruptions, bolster markets' confidence to increase private capital investment, and dispose of the investments as soon as it is practicable.[26] As we and others have noted, these goals at times conflict—that is, maximizing returns on investments may require Treasury to hold the assets until their value increases, creating a conflict with the goal of exiting as soon as practicable.[27] Treasury officials told us that Treasury's practice was generally to hold rather than sell its CPP investments.[28] As a result, Treasury's ability to exit the program would depend on the ability of institutions to repay their investments. However, Treasury officials noted that, if warranted, Treasury could change its practice in the future and sell more of its investments to third parties.

[26]See GAO-12-229.

[27]See GAO, *TARP: Treasury's Exit from GM and Chrysler Highlights Competing Goals, and Results of Support to Auto Communities Are Unclear*, GAO-11-471 (Washington, D.C.: May 10, 2011). The Congressional Oversight Panel also noted these competing goals. See Congressional Oversight Panel, *January Oversight Report: Exiting TARP and Unwinding Its Impact on the Financial Markets* (Washington, D.C.: Jan. 14, 2010).

[28]Treasury has already sold some CPP investments. According to its Section 105(a) reports, Treasury may sell its holdings or exchange CPP securities on a limited basis to protect taxpayers' interest and further EESA's objectives.

Remaining CPP Institutions Are Financially Weaker than Former CPP and Non-CPP Institutions, but Treasury's Analysis Does Not Show This Difference

Institutions that remain in CPP tend to be financially weaker than institutions that have exited the program and institutions that did not receive CPP capital. Our analysis considered various measures that describe banking institutions' profitability, asset quality, capital adequacy, and ability to cover losses. The analysis focused on institutions with under $10 billion in assets, a group that constituted nearly all of the remaining institutions.[29] We analyzed financial data on 352 remaining CPP institutions and 256 former CPP institutions that exited CPP through full repayments or conversion to CDCI or SBLF.[30] These two groups accounted for 608 of the 707 institutions that participated in CPP.[31] We compared these two groups to a non-CPP group (i.e., institutions that have not participated in CPP and have less than $10 billion in assets) of 8,040 active financial institutions for which financial information was available. All financial information generally reflects quarterly regulatory filings on December 31, 2011.[32]

Remaining CPP Institutions Are Generally Less Profitable and Hold Riskier Assets

Profitability measures for remaining CPP institutions were lower than those for former CPP participants and the non-CPP group. From March 2008 to December 2011, the remaining CPP institutions consistently had lower quarterly return on average assets values than the other groups (see fig. 8). This measure shows how profitable a company is relative to its total assets and how efficient management is at using its assets to generate earnings. For the quarter ending December 31, 2011, remaining CPP institutions had a median return on average assets of 0.25, compared with 0.74 for former CPP institutions and 0.69 for the non-CPP group.[33] The return on average equity measure, which shows the profit a

[29]We also compared institutions with less than $1 billion in assets to those with between $1 billion and $10 billion in assets. The relationships and trends were relatively similar, so we combined them for the purposes of our discussion.

[30]Financial data were available from SNL Financial for 427 of the 608 CPP institutions, and we accounted for the remaining 181 institutions using SNL Financial information for the holding company's largest subsidiary.

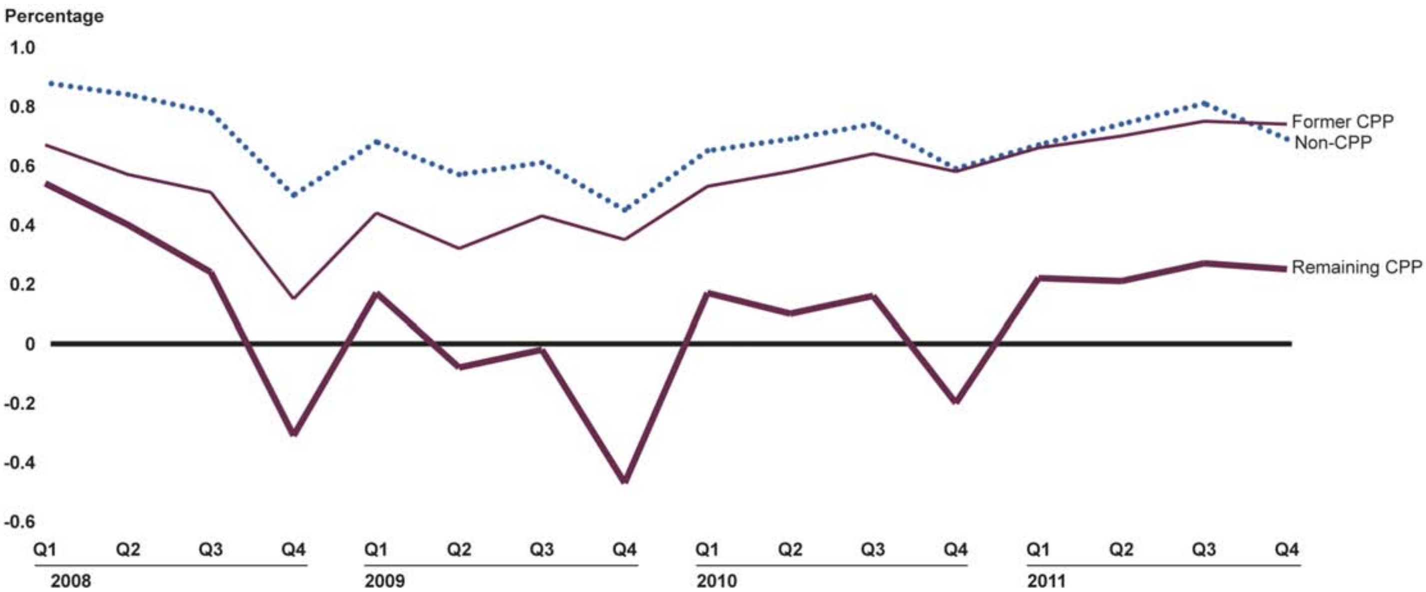
[31]Of the 99 CPP institutions our analysis excluded, 11 were active participants with more than $10 billion in assets, 37 were former participants with more than $10 billion in assets, and 51 had no data available in SNL Financial, had been acquired, or were defunct.

[32]We chose to present median values, but we also analyzed weighted averages and found the results to be similar.

[33]Return on average assets is net income divided by average total assets.

company generates with the money shareholders have invested, showed a similar but more pronounced relationship. The median return on average equity was 2.71 for remaining CPP institutions, compared with 7.15 for former CPP institutions and 6.22 for the non-CPP group.[34]

Figure 8: Quarterly Trend of Median Return on Average Assets by CPP Status, March 2008 through December 2011



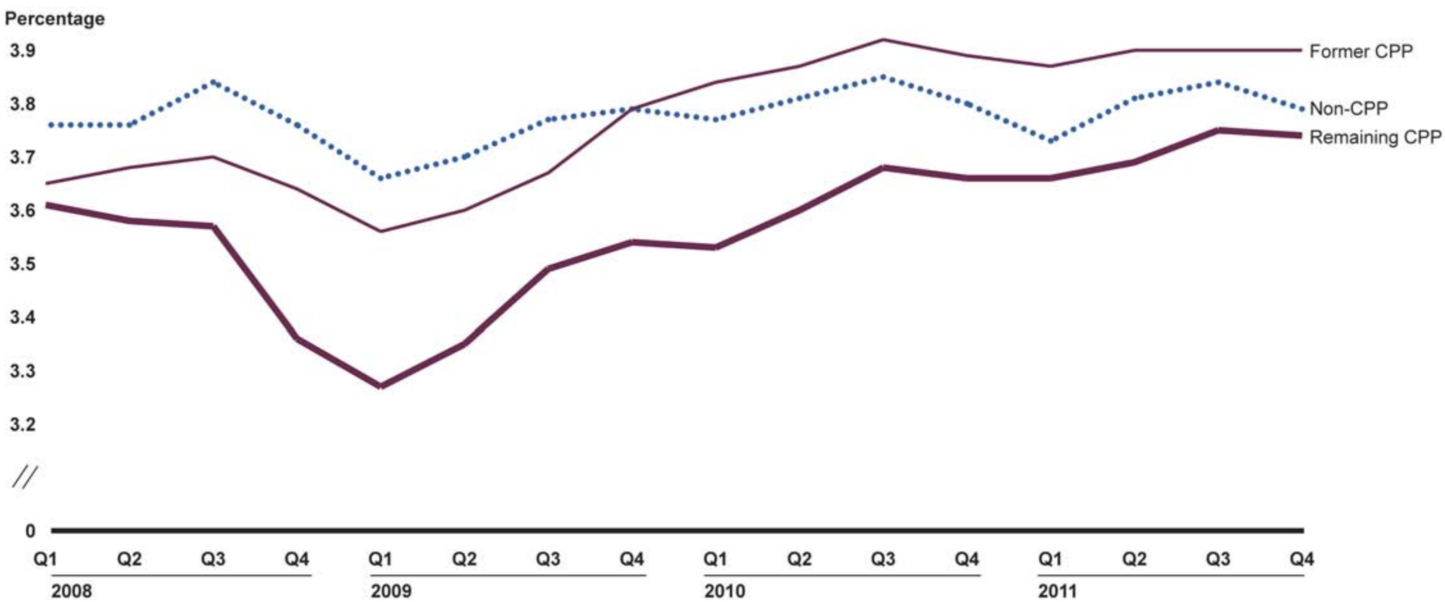
Source: GAO analysis of SNL Financial data.

Further, the median net interest margin—another important measure of profitability—was consistently lower for remaining CPP institutions than for the other groups, but the differences were less pronounced, particularly in recent quarters (see fig. 9).[35] The net interest margin measures a company's investment decisions by comparing its investment returns to its interest expenses. A higher margin indicates a more successful business strategy. For the quarter ending December 31, 2011, the median net interest margin was lowest (3.74) for the remaining CPP institutions. However the medians were not significantly higher for the other two groups—3.90 for former CPP institutions and 3.79 for the non-CPP group.

[34]Return on average equity is net income divided by average total equity.

[35]Net interest margin is net interest income divided by average earning assets.

Figure 9: Quarterly Trend of Median Net Interest Margin by CPP Status, March 2008 through December 2011



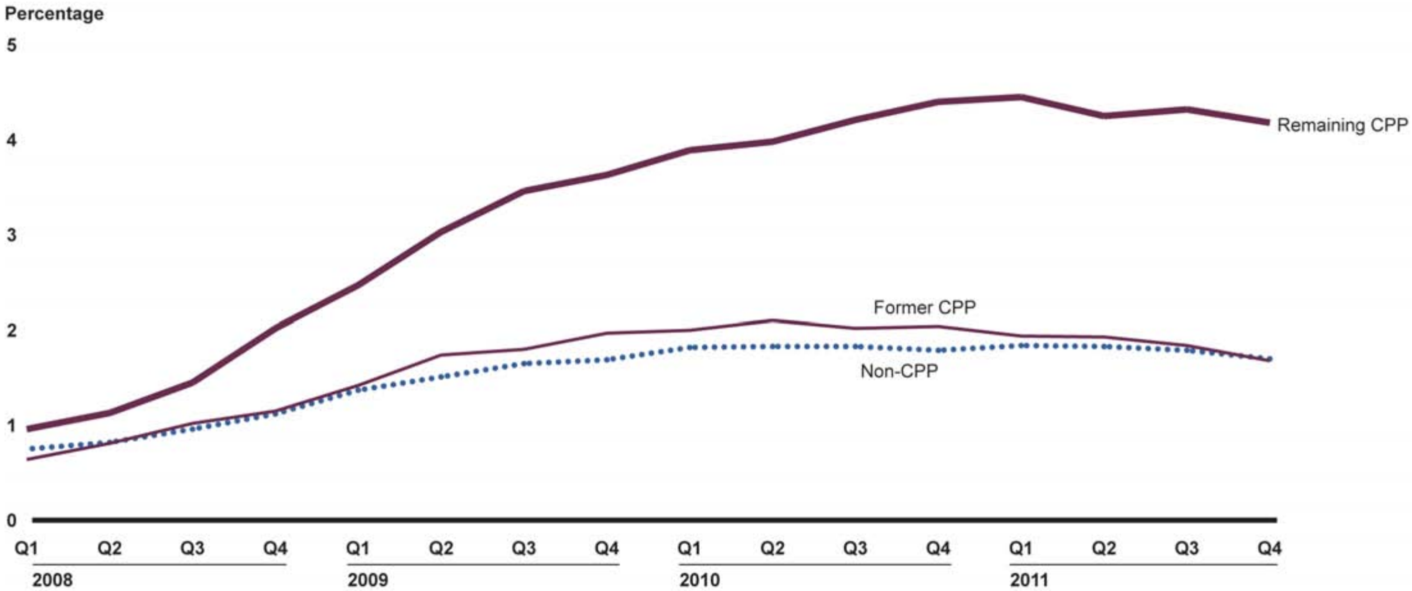
Source: GAO analysis of SNL Financial data.

Note: Since 2000, the net interest margin for all banks has generally ranged between 3 and 4 percent. We have adjusted the scale in figure 9 accordingly to more clearly show the differences between the three groups.

Not only were remaining CPP institutions less profitable than former CPP institutions and the non-CPP group, but they also held relatively more poorly performing assets, as measured by several financial indicators. First, remaining CPP institutions had a consistently higher percentage of noncurrent loans than former CPP institutions and the non-CPP group from March 2008 to December 2011 (see fig. 10). While the median noncurrent loan percentage increased over time for each group before leveling off, the rate of growth was steeper and the period of growth lasted longer for the remaining CPP institutions. As of December 31, 2011, a median of 4.18 percent of loans for remaining CPP institutions were noncurrent, compared with 1.68 percent for former CPP institutions and 1.70 percent for the non-CPP group. Second, remaining CPP institutions had a higher median ratio of net charge-offs to average loans

(1.22) than both former CPP institutions (0.47) and the non-CPP group (0.30), as of December 31, 2011.[36]

Figure 10: Quarterly Trend of Median Noncurrent Loan Percentage by CPP Status, March 2008 through December 2011



Source: GAO analysis of SNL Financial data.

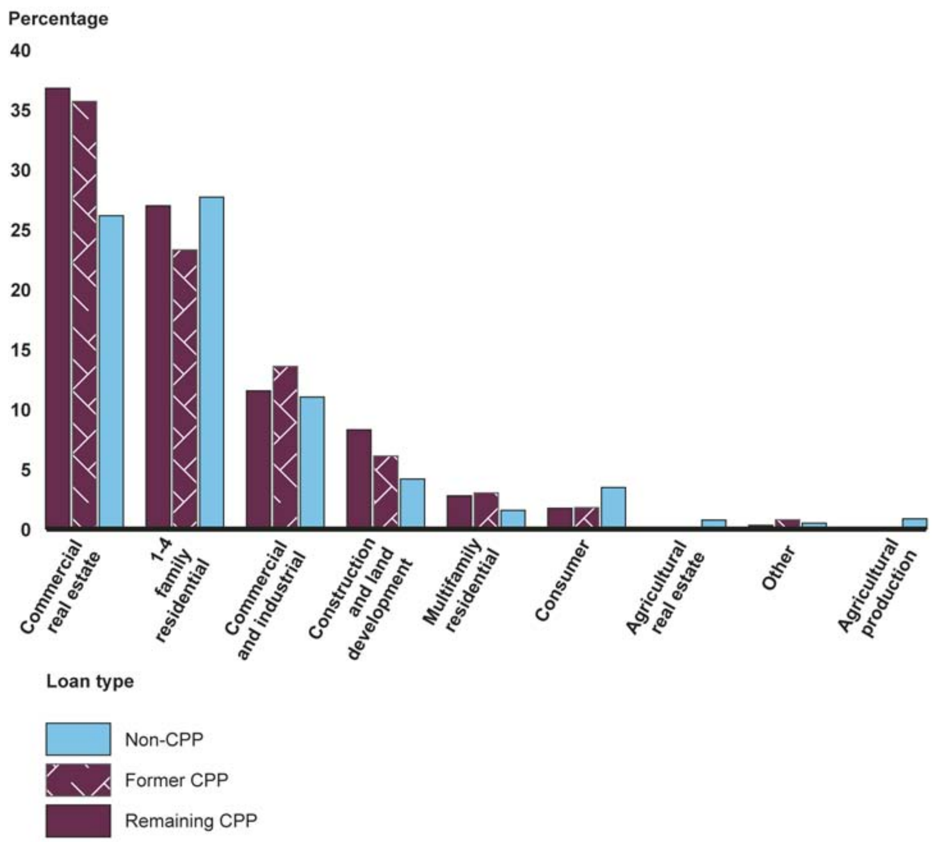
Finally, both remaining and former CPP institutions tended to hold loans that were more concentrated in risky business lines than those held by the non-CPP group, although the differences, and the overall percentages of these loans, were relatively small for one loan category. Both remaining and former CPP institutions had higher proportions of commercial real estate and construction and land development loans compared with the non-CPP group (see fig. 11). As we have reported, delinquencies on commercial real estate loans have more than doubled since the onset of the financial crisis in 2008, and such loans are prone to volatility because of high transaction costs, rigid and constrained supply, and a number of other factors.[37] While remaining CPP institutions had

[36]A charge-off occurs when a bank recognizes that a particular asset or loan will not be collectible and must be written off.

[37]See GAO, *Banking Regulation: Enhanced Guidance on Commercial Real Estate Risks Needed*, GAO-11-489 (Washington, D.C.: May 19, 2011).

about the same proportion of commercial real estate loans overall as the former CPP institutions (about 35 percent), they had a noticeably higher proportion of construction and land development loans compared to the non-CPP group. Although these loans made up only about 4 to 8 percent of the banks' overall portfolios, construction and land development loans are generally considered to be particularly risky. For example, they often have long development times and can include properties that are built without firm commitments from buyers or lessees.

Figure 11: Median Loan Composition by CPP Status, as of December 31, 2011



Source: GAO analysis of SNL Financial data.

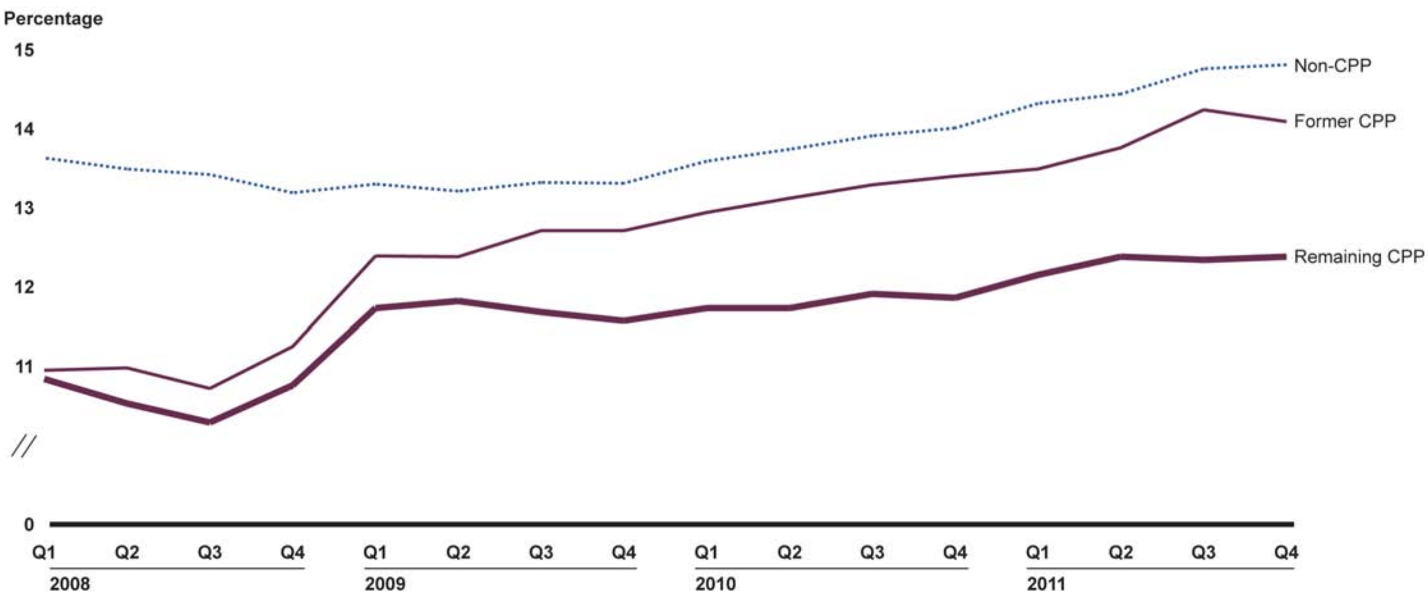
Remaining CPP Institutions Hold Less Regulatory Capital and Reserves for Covering Losses Compared to Institutions That Exited CPP or Never Participated

Compared with former CPP institutions and the non-CPP group, remaining CPP institutions held less regulatory capital as a percentage of assets. Regulators require minimum amounts of capital to lessen an institution's risk of default and improve its ability to sustain operating losses. Capital can be measured in several ways, but we focused on Tier 1 capital, which includes both risk-based and common risk-based measures, because it is the most stable form of regulatory capital.[38] The Tier 1 risk-based capital ratio measures Tier 1 capital as a share of risk-weighted assets, and the common equity Tier 1 ratio measures common equity Tier 1 as a share of risk-weighted assets.

Remaining CPP institutions had lower Tier 1 capital levels than former CPP institutions and the non-CPP group. On a quarterly basis, for example, the Tier 1 risk-based capital ratio for remaining CPP participants generally remained well below those for the former CPP institutions and the non-CPP group from March 2008 to December 2011 (see fig. 12). While Tier 1 capital levels of the remaining institutions have trended slightly upward since December 2009, levels for the other two groups rose at a slightly higher rate, increasing the gap between the groups. As of December 31, 2011, Tier 1 capital accounted for 12.38 percent of risk-weighted assets for remaining CPP institutions compared with 14.09 percent for former CPP institutions and 14.81 percent for the non-CPP group.

[38]Tier 1 capital includes the core capital elements that are considered the most reliable and stable such as common stock, noncumulative perpetual preferred stock, and minority interests in consolidated subsidiaries. Total capital includes Tier 1 capital and Tier 2 capital, or supplementary capital. Risk-weighted assets are on- and off-balance sheet assets adjusted for their risk characteristics.

Figure 12: Quarterly Trend of Median Tier 1 Risk-based Capital Ratio by CPP Status, March 2008 through December 2011



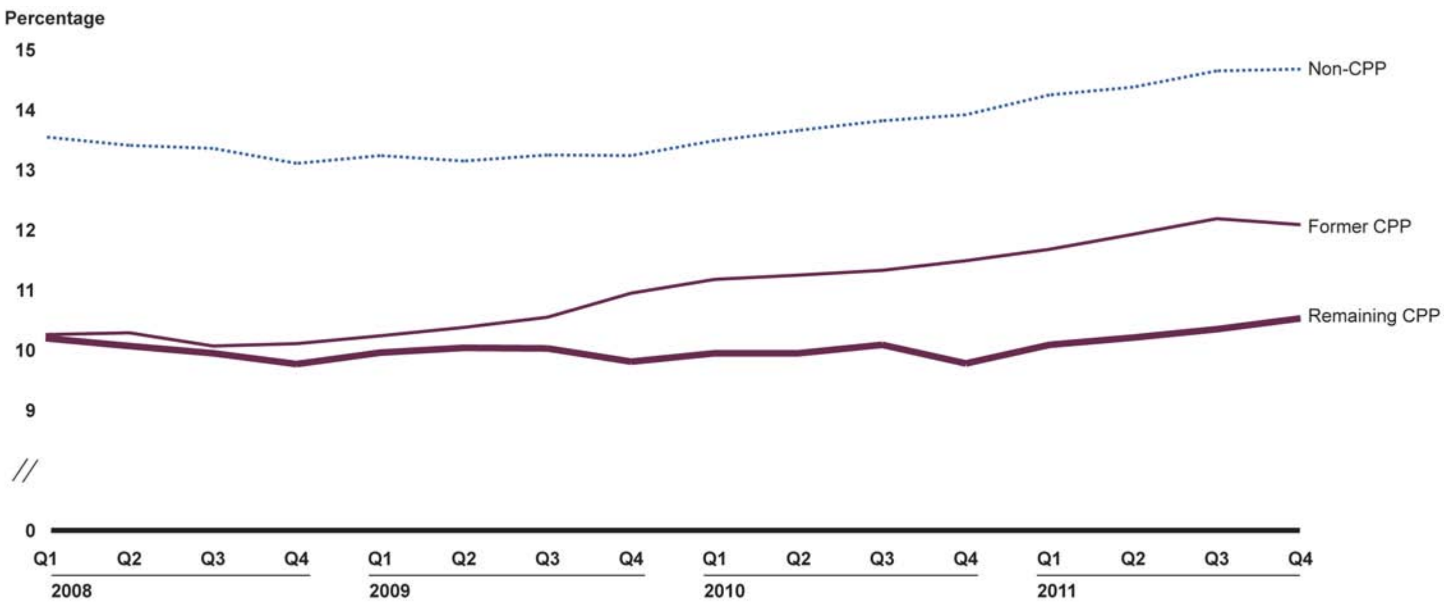
Source: GAO analysis of SNL Financial data.

Because Tier 1 capital for the remaining institutions includes funds received through TARP, ratios using common equity Tier 1—which generally does not include TARP funds—may better illustrate these institutions' capital adequacy. For the remaining CPP institutions, TARP funds comprised a median of 25 percent of the institution's Tier 1 capital. As was the case with the Tier 1 risk-based capital ratio, the common equity Tier 1 ratio for remaining CPP institutions generally remained well below those for the former CPP institutions and the non-CPP group from March 2008 to December 2011 (see fig. 12). However, the differences between both CPP groups and the non-CPP group were more pronounced possibly because common equity Tier 1 generally does not include TARP funds.[39] While the ratio for remaining CPP institutions stayed relatively stable from March 2008 to December 2010, it has since begun increasing slightly. As of December 31, 2011, the common equity Tier 1 ratio was lower for remaining CPP institutions than the other two groups. In particular, common equity Tier 1 for remaining CPP institutions

[39]As of January 31, 2012, Treasury had converted its original investment into shares of common stock for six institutions.

comprised a median of 10.53 percent of risk-weighted assets, compared with 12.09 percent for former CPP institutions and 14.68 percent for the non-CPP group.

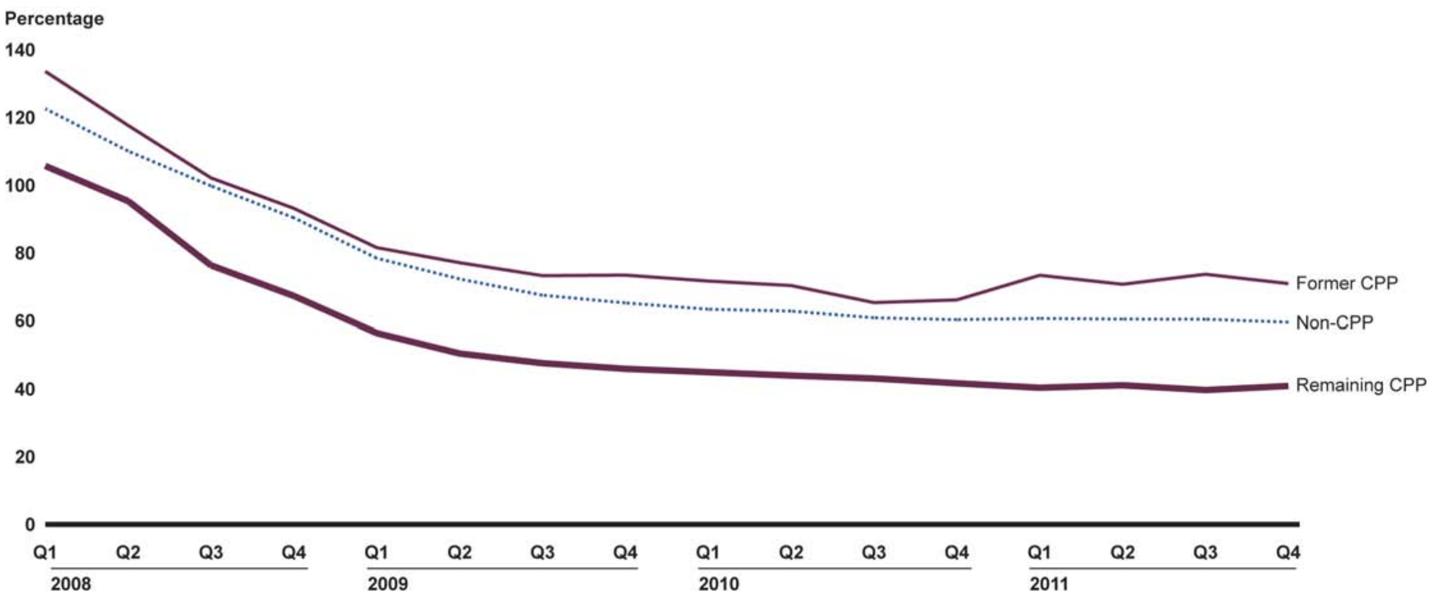
Figure 13: Quarterly Trend of Median Common Equity Tier 1 Ratio by CPP Status, March 2008 through December 2011



Source: GAO analysis of SNL Financial data.

In addition to holding less regulatory capital than former CPP institutions and the non-CPP group, remaining CPP institutions also had significantly lower reserves for covering losses. On a quarterly basis, the median ratio of reserves to nonperforming loans was consistently lower for remaining CPP institutions than for the other groups from March 2008 to December 2011 (see fig. 14). The ratio for all three groups declined in 2008 and 2009, and while it began to stabilize for the non-CPP group in 2010, it continued to decline for remaining CPP institutions. As of December 31, 2011, the ratio of reserves to nonperforming loans was lower for remaining CPP institutions (40.87) than for former CPP participants (70.93) and the non-CPP group (59.56). We also compared loan loss provisions to net charge-offs and found that the remaining CPP institutions had lower ratios (74.48) than former CPP institutions (92.47) but higher than the non-CPP group (72.78).

Figure 14: Quarterly Trend of Median Reserves to Nonperforming Loans by CPP Status, March 2008 through December 2011

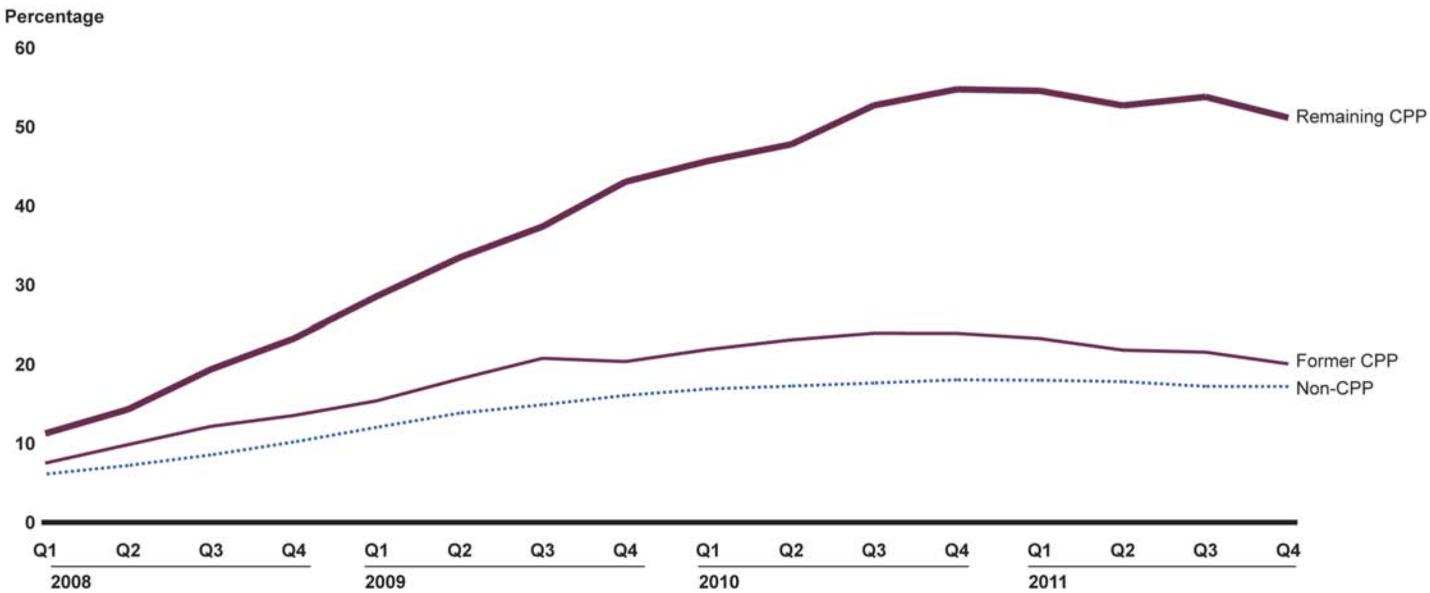


Source: GAO analysis of SNL Financial data.

Remaining CPP institutions also had noticeably higher Texas Ratios than former CPP institutions and the non-CPP group. The Texas Ratio helps determine a bank's likelihood of failure by comparing its troubled loans to its capital.[40] The higher the ratio, the more likely the institution is to fail. On a quarterly basis, median Texas Ratios for remaining CPP institutions remained consistently above those for former CPP institutions and the non-CPP group from March 2008 to December 2011 and rose at a faster rate (see fig. 15). Since December 2010, median Texas Ratios for remaining CPP institutions have stabilized, while those for former CPP and the non-CPP group have shown slight decreases. As of December 31, 2011, remaining CPP institutions had a median Texas Ratio of 51.14, compared with 20.06 for former CPP institutions and 17.20 for the non-CPP group. Moreover, about 19 percent (66) of the 352 remaining CPP institutions had a Texas Ratio of more than 100 percent, indicating an elevated likelihood of failure, compared with only about 1 percent (3) of the 256 former CPP institutions.

[40]The Texas Ratio is defined as nonperforming assets plus loans 90 or more days past due divided by tangible equity and reserves.

Figure 15: Quarterly Trend of Median Texas Ratio by CPP Status, March 2008 through December 2011



Source: GAO analysis of SNL Financial data.

Treasury's Quarterly CPP Analysis Could Better Distinguish between the Remaining CPP Institutions and Former Participants

To assess CPP's effect on lending by depository institutions, Treasury began publishing a quarterly analysis of CPP institutions.[41] The analysis included financial data in three categories: balance sheet and off-balance sheet items, performance ratios, and asset quality measures. Treasury grouped the institutions by asset size and separated institutions that received CPP funds from those that did not.

However, Treasury did not compare remaining CPP institutions to former CPP institutions. While Treasury's analysis is intended to measure CPP's effect on the financial institutions that participated, its analysis could also provide useful information about the relative likelihood of remaining institutions to repay their investments and exit the program. Our analysis found differences in the financial condition of remaining and former CPP institutions, suggesting that the remaining CPP institutions could face challenges in repaying CPP funds and exiting the program. Treasury said

[41]Department of the Treasury, *Quarterly Analysis of Institutions in the Capital Purchase Program*, Fourth Quarter 2010.

that it did not perform this analysis because the quarterly CPP report was designed only to group banks into categories based on asset size and to analyze the differences between CPP and non-CPP institutions.

In our prior work, we noted that Treasury should ensure transparency in providing financial assistance to private market participants, especially given the unprecedented government assistance it provided to the banking industry during the recent financial crisis.[42] We also recommended that Treasury ensure that external stakeholders, including Congress and the public, are informed about the program's current strategy.[43]

Treasury's quarterly CPP analysis is a useful tool in providing transparency about the public's investment in financial institutions. In addition, Treasury makes public a variety of products on its website—including transaction reports, dividend and interest reports, and monthly 105(a) reports—that account for all investments and provide program-level summaries for all TARP programs. However, the usefulness and transparency of Treasury's quarterly CPP analysis—which includes detailed bank financial measures—could be enhanced by distinguishing between former and remaining CPP institutions because the financial characteristics of these two groups differ. As a result, Congress and the public would benefit from a more complete and meaningful picture of the condition of the remaining institutions.

Conclusions

CPP repayments and other income surpassed the program's original investment disbursements, and as institutions continue to exit CPP, this surplus continues to grow. Furthermore, Treasury's latest estimate (November 30, 2011) projects CPP's lifetime income to be $13.5 billion. However, a growing number of the remaining institutions have missed scheduled dividend or interest payments or appeared on FDIC's problem bank list. As a result, there is increased concern regarding the speed at which institutions will be able to repay remaining funds and how much of

[42]GAO, *Financial Assistance: Ongoing Challenges and Guiding Principles Related to Government Assistance for Private Sector Companies*, GAO-10-719 (Washington, D.C.: Aug. 3, 2010).

[43]GAO, *Troubled Asset Relief Program: Additional Actions Needed to Better Ensure Integrity, Accountability, and Transparency*, GAO-09-161 (Washington, D.C.: Dec. 2, 2008).

these funds Treasury will ultimately recover. In particular, our analysis showed that institutions remaining in CPP were generally less profitable, held riskier assets and less regulatory capital, and had lower reserves for covering losses compared with institutions that repaid their CPP investment and those that never participated in the program. Despite the noticeably different financial profiles for remaining and former CPP institutions, Treasury's quarterly analysis of CPP institutions does not distinguish between these two groups. As we have indicated in past reports on TARP, transparency remains a critical element in the government's unprecedented assistance to the financial sector. Such transparency helps clarify to policymakers and the public the costs of TARP assistance and the government's intervention in various markets. Enhancing the quarterly CPP analysis by distinguishing between remaining and former CPP participants will help Treasury provide Congress and the public with a more transparent and comprehensive understanding of the status of CPP and the institutions that participate in it.

Recommendation for Executive Action

To provide Congress and the public with more transparent and comprehensive information on remaining CPP institutions and enhance its reporting, the Secretary of the Treasury should consider analyzing and reporting on remaining and former CPP participants separately.

Agency Comments and Our Evaluation

We provided a draft of this report to Treasury for its review and comment. Treasury provided written comments that we have reprinted in appendix II.

In its written comments, Treasury stated that it would carefully consider our recommendation to further enhance transparency by analyzing and reporting on remaining and former CPP participants separately. Treasury emphasized its ongoing commitment to keep the public informed of its progress in winding down CPP. We believe that implementation of our recommendation would further strengthen Treasury's reporting to the Congress and the public on the status of CPP.

We are sending copies of this report to the Financial Stability Oversight Board, Special Inspector General for TARP, interested congressional committees and members, and Treasury. The report also is available at no charge on the GAO website at http://www.gao.gov.

If you or your staffs have any questions about this report, please contact A. Nicole Clowers at (202) 512-8678 or clowersa@gao.gov, or Daniel Garcia-Diaz at (202) 512-8678 or garciadiazd@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 major contributions to this report are listed in appendix III.

A. Nicole Clowers
Director
Financial Markets and Community Investment

List of Committees

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

The Honorable Tim Johnson
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 Jeff Sessions
Ranking Member
Committee on the Budget
United States Senate

The Honorable Max Baucus
Chairman
The Honorable Orrin G. Hatch
Ranking Member
Committee on Finance
United States Senate

The Honorable Hal Rogers
Chairman
The Honorable Norm Dicks
Ranking Member
Committee on Appropriations
House of Representatives

The Honorable Paul Ryan
Chairman
The Honorable Chris Van Hollen
Ranking Member
Committee on the Budget
House of Representatives

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

The Honorable Dave Camp
Chairman
The Honorable Sandy Levin
Ranking Member
Committee on Ways and Means
House of Representatives

Appendix I: Objectives, Scope, and Methodology

The objectives of our report were to examine (1) the status of the Capital Purchase Program (CPP), including repayments and other proceeds to date, restructuring of investments, and timeliness of dividend payments, and (2) the financial condition of institutions that received investments under CPP compared with institutions that exited CPP and those that did not participate in the program.

To assess the status of CPP at the program level, we analyzed data from a number of sources including the Department of the Treasury (Treasury) and the Federal Deposit Insurance Corporation (FDIC). In particular, we used Treasury's January 2012 Monthly 105(a) Report to Congress to determine the dollar amounts of outstanding investments, the number of remaining and former participants, and the geographical distribution of each as of January 31, 2012. We also used data from Treasury's Dividends and Interest reports from February 2009 through November 2011 to determine the extent to which participants had missed payments throughout the life of the program. We interviewed Treasury officials to compare our missed payment counts with theirs and noted the reasons for any differences. Finally, we obtained from FDIC summary information on its quarterly problem bank list to show the trend of CPP institutions appearing on the list from December 2008 through December 2011.

To assess the financial condition of institutions that received investments under CPP, we reviewed industry documents—including summaries of monitoring data used by banking regulators and Treasury—to identify commonly used financial measures for depository institutions. These measures help demonstrate an institution's financial health related to a number of categories including profitability, asset quality, capital adequacy, and loss coverage. We obtained such financial data for all depository institutions using SNL Financial—a private financial database that contains publicly filed regulatory and financial reports. We merged the data with SNL Financial's CPP participant list to create the three comparison groups—remaining CPP institutions, former CPP institutions, and a non-CPP group comprised of all institutions that did not participate in CPP. We analyzed financial data on 352 remaining CPP institutions and 256 former CPP institutions that exited CPP through full repayments or conversion to the Community Development Capital Initiative or the Small Business Lending Fund, accounting for 608 of the 707 CPP participants (see table 1). Our analysis focused on institutions with less than $10 billion in assets, which constituted nearly all of the remaining CPP institutions. Of the 99 CPP institutions excluded from our analysis, 11 were active participants with more than $10 billion in assets; 37 were former participants with more than $10 billion in assets; and 51 had no data available in SNL Financial, had been acquired, or were defunct. We compared the remaining and former CPP institutions to a non-CPP group of 8,040 active financial institutions for which financial information was available. We chose to present median values, but we also analyzed weighted averages and found the results to be similar. Financial data were available from SNL Financial for 427 of the 608 CPP institutions, and we accounted for an additional 181 institutions using the financial information of the holding company's largest subsidiary from SNL Financial. All financial information reflects quarterly regulatory filings on December 31, 2011, unless otherwise noted. We downloaded all financial data from SNL Financial on February 20, 2012. Finally, we compared our analysis with Treasury's quarterly analysis of CPP institutions, and we also leveraged our past reporting on the Troubled Asset Relief Program (TARP), as well as that of the Special Inspector General for TARP, as appropriate.

Table 1: Median Financial Information on Analysis Population, as of December 31, 2011

Dollars in millions

	All CPP	Remaining CPP	Former CPP	Non-CPP
Number of institutions	608	352	256	8,040
TARP funds received	Not applicable	$12.9	$15.0	Not applicable
TARP funds outstanding	Not applicable	$12.6	Not applicable	Not applicable
Assets	$493.4	$395.7	$617.7	$176.8
Loans and leases	$320.2	$270.6	$405.9	$108.5
Reserves	$6.2	$6.2	$6.2	$1.8
Securities	$74.2	$53.3	$120.3	$33.5
Liabilities	$440.9	$359.6	$547.4	$157.6
Deposits	$384.9	$318.4	$497.4	$148.4
Tier 1 capital	$42.1	$32.5	$61.3	$17.3
Common equity Tier 1	$32.3	$24.4	$43.6	$17.1
Net income	$0.4	$0.1	$1.0	$0.2

Source: GAO analysis of SNL Financial data.

We determined that the financial information used in this report, including CPP program data from Treasury and financial data on institutions from SNL Financial, was sufficiently reliable to assess the condition and status of CPP and institutions that participated in the program. For example, we tested the Office of Financial Stability's internal controls over financial reporting as it relates to our annual audit of the office's financial statements and found the information to be sufficiently reliable based on the results of our audits of fiscal years 2009, 2010, and 2011 financial statements for TARP.[1] We have assessed the reliability of SNL Financial data—which is obtained from financial statements submitted to the banking regulators—as part of previous studies and found the data to be reliable for the purposes of our review. We verified that no changes had been made that would affect its reliability.

We conducted this performance audit from August 2011 to March 2012 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

[1] See GAO, *Financial Audit: Office of Financial Stability (Troubled Asset Relief Program) Fiscal Years 2011 and 2010 Financial Statements*, GAO-12-169 (Washington, D.C.: Nov.10, 2011); *Financial Audit: Office of Financial Stability (Troubled Asset Relief Program) Fiscal Years 2010 and 2009 Financial Statements*, GAO-11-174 (Washington, D.C.: Nov.15, 2010); and *Financial Audit: Office of Financial Stability (Troubled Asset Relief Program) Fiscal Year 2009 Financial Statements*, GAO-10-301 (Washington, D.C.: Dec. 9, 2009).

Appendix II: Comments from the Office of Financial Stability

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

ASSISTANT SECRETARY

February 24, 2012

A. Nicole Clowers
Director
Financial Markets and Community Investment
U.S. Government Accountability Office
441 G Street, NW
Washington, DC 20548

Dear Ms. Clowers:

I am writing in response to your draft final report regarding the Capital Purchase Program (CPP) entitled, *Revenues Have Exceeded Investments, but Concerns about Outstanding Investments Remain* (Draft Report). The Department of the Treasury (Treasury) appreciates the efforts of the Government Accountability Office (GAO), and this letter provides our official comments to the Draft Report.

The Draft Report provides a useful snapshot of CPP and the institutions that remain in the program. As the report acknowledges, Treasury has made significant progress in recouping its CPP investments. We have already recovered an amount from all bank programs which exceeds the amount invested -- $258 billion compared to $245 billion. In addition, the pace of recovery and exit has been faster than anyone expected. Overall, Treasury expects to achieve a lifetime positive return of more than $20 billion on our investments in banks.

As you note in your report, over half of the participating banks have already exited TARP. Today, 364 banks have remaining CPP investments outstanding. Under the terms of the Securities Purchase Agreement, Treasury cannot require banks to repay the CPP investments. In addition, any CPP repayment requires regulatory approval. As has been our policy, however, we encourage CPP institutions that have regulatory approval to repay their TARP investment. Replacing government capital with private capital is an important component of fully restoring financial stability.

Recently, as part of our efforts to wind down the CPP, we began working with Houlihan Lokey Capital, Inc. to explore options for the management and ultimate recovery of our remaining CPP investments. That process is ongoing and we will continue to work to wind down the program in a way that ensures financial stability and protects the interest of taxpayers.

As we continue to wind down CPP, we remain committed to keeping the public informed of our progress. As you know, Treasury has established comprehensive accountability and transparency measures regarding CPP. We therefore appreciate GAO's acknowledgement that "Treasury's quarterly CPP analysis is a useful tool in providing transparency about the public's investment in financial institutions" as well as your acknowledgment that "Treasury makes public a variety of products on its website … that account for all investments and provide program-level summaries of all TARP programs." Beyond its quarterly CPP Analysis, Treasury publishes a CPP Monthly Lending Report, which includes outstanding consumer and commercial loan balances for all CPP participants, and a Monthly Lending and Intermediation Snapshot, which provides quantitative information on banks' consumer and commercial lending activities. Treasury also publishes a monthly report which describes dividends and interest received from CPP investments. Additionally, Treasury periodically issues reports detailing warrant repurchases and auctions and the disposition of CPP warrants.

The Draft Report suggests that Treasury could enhance its transparency and provide more comprehensive information on remaining CPP institutions by considering ways to improve its reporting regarding current and former CPP participants. As we have previously indicated to GAO, we will review our current reporting and consider this recommendation carefully.

Treasury values GAO's review of CPP and looks forward to continuing to work with you and your team as we move forward.

Sincerely,

Tim Massad

Timothy G. Massad
Assistant Secretary for Financial Stability

Appendix III: GAO Contacts and Staff Acknowledgments

GAO Contacts

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Staff Acknowledgments

In addition to the contacts named above, Christopher Forys, Emily Chalmers, William Chatlos, Rachel DeMarcus, Michael Hoffman, Marc Molino, Tim Mooney, and Patricia Moye made significant contributions to this report.

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