

September 26, 2008

**Troubled Assets Relief Program**  
**Highlights of the Discussion Draft Bill**  
*Currently being considered by Congress on*  
*Friday, September 26, 2008*

The following is a brief summary of the Discussion Draft Bill, dated September 25, 2008, providing for the Troubled Assets Relief Program, which Congress is now considering.

Also included is the full text of the [Discussion Draft Bill](#). We will provide you with updates and other information regarding this legislation as it progresses.

Please contact any of the following members of our Financial Services Regulation and Distressed Assets Practice Groups for further information.

**Highlights of the Discussion Draft Bill**  
*(as of September 25, 2008)*

*The numbers in brackets below refer to the page numbers in the Discussion Draft Bill.*

- The Act is titled the “Economic Recovery and Corporate Accountability Act of 2008.” [2]
- Key defined terms [5-6]:
  - “Financial institution” means any institution, including any bank, savings association, credit union, security broker or dealer, or insurance company, organized and regulated under the laws of the United States or any state, territory, or possession of the United States, the District of Columbia, Commonwealth of Puerto Rico, Commonwealth of Northern Marianas 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.
  - “Troubled assets” means residential or commercial mortgages and any securities, obligations, or other instruments that are based on or related to such mortgages, that in each case originated or issued on or before March 14, 2008, the purchase of which the Secretary determines promotes financial market stability; and, upon the determination of the Secretary in consultation with the Chairman of the Board of Governors of the Federal Reserve, any other financial instrument, the purchase of which the Secretary determines necessary to promote financial market stability.
- The Bill contains important findings [3], purposes [4-5], and considerations [10-11].

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- The Secretary of the Treasury has authority to establish a program, called the “Troubled Assets Relief Program” (the “TARP”), to purchase Troubled Assets through an Office of Financial Stability within the Office of Domestic Finance of the Department of the Treasury. [7]
  - In exercising this authority, the Secretary shall consult with the Board of Governors of the Federal Reserve System, the Federal Reserve Bank of New York, the FDIC, the Comptroller of the Currency, the Director of the Office of Thrift Supervision, and the Secretary of Housing and Urban Development. [8]
  - The Secretary shall coordinate, as appropriate, with foreign financial authorities and central banks to work toward the establishment of similar programs by such authorities and central banks. [32]
  - The maximum amount of authorized purchases outstanding at any one time is \$700 billion. However, this authority is subject to the following limitations:
    - The authority of the Secretary to purchase Troubled Assets shall be initially limited to \$250 billion outstanding at any one time. [38]
    - If at any time the President submits to the Congress written notification that the Secretary is exercising the authority, effective upon such submission, the limitation shall increase to \$350 billion outstanding at any one time. [38]
    - If at any time the President submits to the Congress a written report detailing the plan of the Secretary to exercise the authority under this paragraph, unless there is enacted within 15 calendar days of such submission, a joint resolution, effective upon the expiration of such 15 day period, the authority increases to \$700 billion outstanding at any one time. [39] The Bill provides detailed procedural requirements relating to the content and adoption of such a resolution.
  - The Secretary shall publish guidelines, including mechanisms for purchasing Troubled Assets, methods for pricing and valuing Troubled Assets, procedures for selecting asset managers, and criteria for identifying Troubled Assets for purchase. [9]
  - In making purchases under the authority of the Act, the Secretary shall take such steps as may be necessary to prevent unjust enrichment of Financial Institutions participating in TARP. [9]
  - The Secretary shall use market mechanisms to make efficient use of taxpayer resources, including auctions and reverse auctions. [33]
    - If the Secretary determines that using market mechanisms is not feasible or appropriate, and the purposes of the Act are best met through direct purchases from an individual Financial Institution, the Secretary shall pursue additional measures to ensure that prices paid for assets are reasonable and reflect the underlying value of the asset. [33]
  - The Secretary may not purchase Troubled Assets unless the Secretary receives a warrant giving the right to the Secretary to receive non-voting common stock or preferred stock in such Financial Institution in the case of a Financial Institution that is registered (or approved for registration) and traded on a national securities exchange or a national securities association. In the case of any Financial Institution other than one described in the previous sentence, the Secretary may not purchase Troubled Assets unless the Secretary receives a senior debt instrument from such Financial Institution. The Bill provides specific requirements for such warrants and debt. [33-37]
    - The Secretary shall establish a de minimis exception to the requirements of this subsection, based on the size of the Financial Institution or the size of the transaction. [37]

- The Secretary shall determine the public disclosure requirement for Financial Institutions participating in TARP. [37]
- The Secretary, in consultation with the FDIC, has authority to manage Troubled Assets purchased under the Act. [18-19]
- The Secretary, upon terms and conditions and at prices determined by the Secretary, may sell, or enter into securities loans, repurchase transactions, or other financial transactions in regard to, any Troubled Assets purchased under the Act. [19]
  - No less than 20% of any profits realized on sales of “Troubled Assets” shall be distributed as follows: (i) 65% to the Housing Trust Fund, which was established under Section 1338 of the Federal Housing Enterprises Regulatory Reform Act of 1992 (12 U.S.C. 4568) to preserve low-income housing; and (ii) 35% to the Capital Magnet Fund, which was established under Section 1339 of that Act (12 U.S.C. 4569) to create a grant program to increase investment in development and preservation of affordable housing, loan loss reserves, revolving loan funds, economic or community development funds, and risk-sharing loans. [19]
  - The remainder of the profits (80%) is to be distributed to the Treasury. [20]
- Oversight includes the following:
  - A Financial Stability Oversight Board is established to review the exercise of authority, make recommendations, and report any fraud, misrepresentations, or malfeasance to appropriate law enforcement agencies. [12]
    - The Financial Stability Oversight Board may appoint a Credit Review Committee to evaluate the exercise of the purchase authority. [14]
  - The Comptroller General shall conduct ongoing oversight of the activities and performance of the TARP, and the agents and representatives of the TARP, conduct a study to assess the impact of the program, and submit a report of the study to Congress. [44]
  - Disclosure to Congress and the public of financial statements of TARP, which are audited by the Comptroller General. [48-49]
  - A Special Inspector General for the Troubled Asset Program. [55-63]
  - A Congressional Oversight Panel is established in the legislative branch to review the current state of the financial markets and the regulatory system and submit monthly reports to Congress. [69-74]
- Required studies to be undertaken by the Comptroller General [51-53]:
  - A study to determine the extent to which leverage and sudden deleveraging of Financial Institutions was a factor behind the current financial crisis.
  - A study to assess the impact of TARP on the financial markets, the banking system, and taxpayers.
- Required reports include the following:
  - Monthly reports to Congress and weekly public reports by the Secretary. [15-16]
  - Reports by the Office of Management and Budget and the

Congressional Budget Office to the President and Congress to provide an estimate of the cost of the Troubled Assets acquired under the Act. [87-88]

- Inclusion in the President's Budget of an analysis of the budgetary effects of the actions the Secretary has taken or plans to take using any authority provided in the Act. [89-91]
- Foreclosure mitigation efforts include the Secretary encouraging the servicers of the underlying mortgages to take advantage of the HOPE for Homeowners Program, and the Secretary using loan guarantees and credit enhancements to facilitate loan modifications to prevent avoidable foreclosures. [22-23]
  - The Secretary shall coordinate with the FDIC, the Federal Housing Finance Agency, the Department of Housing and Urban Development, and other Federal Government entities that hold Troubled Assets. [23]
- Includes provisions for a systematic homeowner assistance program, including modification of loans secured by residences and availability of foreclosed properties to states and localities. [25-27]
- Sets certain criteria for standards to be set by the Secretary for executive compensation for all Financial Institutions seeking to sell assets through TARP, including limits on incentive compensation. [29-30] Also sets additional standards regarding corporate governance for Financial Institutions, in which the Secretary makes a direct purchase from an individual Financial Institution, including shareholder voting rights for directors of such Financial Institutions and limits on severance compensation. [30-32]
- Judicial Review [54-55]:
  - Any actions of the Secretary pursuant to the authority of the Act shall be held unlawful and set aside only if found to be arbitrary, capricious, an abuse of discretion, or not in accordance with the law.
  - Other than in cases involving constitutional claims, no injunction or other form of equitable relief shall be issued against the Secretary for actions pursuant to the authority of the Act except under extraordinary circumstances involving clearly irreparable harm or injury.
  - Other than in cases involving constitutional claims, any injunction or other form of equitable relief that is issued shall be automatically stayed until the Secretary has had the opportunity to seek a stay from a higher court and such higher court has ruled on the stay.
  - The terms of a residential mortgage loan that is part of any purchase by the Secretary shall remain subject to all claims and defenses that would otherwise apply.
- The authority of the Secretary to purchase Troubled Assets under the Act terminates on December 31, 2009, unless extended. [55]
- Includes amendments to Section 18(a) of the Federal Deposit Insurance Act (12 U.S.C. 1828(a)), adding prohibitions on false advertising, misuse of FDIC name, and misrepresentation to indicate insured status, and grant of enforcement authority in the case of violation to the appropriate federal banking agency, which is to be determined by the FDIC. [74-81]
  - Any Federal financial regulatory agency shall cooperate with the Federal Bureau of Investigation and other law enforcement agencies investigating fraud, misrepresentation, and malfeasance with respect to development, advertising, and sale of financial products. [81]

- Includes amendments to the Truth in Lending Act (15 U.S.C. 1638(b)(2)), as amended by section 2502 of the Mortgage Disclosure Improvement Act of 2008 (Public Law 110-289), regarding mortgage disclosure requirements. [83-85]
- Includes amendments to Chapter 13 of the Bankruptcy Code relating to residential mortgages that would allow debtors to modify interest rates and repayment terms on non-traditional and subprime mortgage loans and to cram down claims under such mortgages to current property values. [65-69]
- The Secretary is authorized to establish an insurance or guarantee program for money market mutual funds similar to the insurance program provided to depositors by the FDIC; provided that such program shall not provide insurance in excess of the FDIC deposit insurance limits. [85-86]
- Tax and Executive Compensation provisions include the following:
  - The gain or loss from the sale or exchange of any applicable preferred stock by any applicable Financial Institution shall be treated as ordinary income or loss. Applicable preferred stock is preferred stock in FNMA and FHLMC held or sold on certain dates. [91-94]
  - Home Equity Debt Cancellation Income Not Taxable: Absent an exception, a taxpayer is required to include in income any debt that has been forgiven. Currently, the debt incurred to purchase a home is excluded. The bill extends this relief to \$100,000 of home equity indebtedness presently outstanding, which can exceed the purchase price of the home. In addition, the bill extends the expiration of both benefits by 2 years through 2012. [102]
  - No deduction shall be allowed in the case of executive remuneration for any applicable taxable year which is attributable to services performed by a covered executive during such applicable taxable year, to the extent that the amount of such remuneration exceeds \$400,000 for a public company, by amending Section 162(m) of the Internal Revenue Code. [94-99]
  - To backstop this provision, no deduction shall be allowed in the case of deferred deduction executive remuneration for any taxable year for services performed during any applicable taxable year by a covered executive, to the extent that the amount of such remuneration exceeds \$400,000 reduced by the sum of (i) the executive remuneration for such applicable taxable year, plus (ii) the portion of the deferred deduction executive remuneration for such services which was taken into account in a preceding taxable year. [94-99]
  - The golden parachute provisions of Section 280G of the Internal Revenue Code are amended to extend their application to a broader range of executives receiving severance payments from a financial institution having purchase troubled assets and without regard to whether or not there is a change in control of the entity. The Secretary is authorized to make parallel changes to Section 4999, which imposes a non-deductible penalty on the executive. [99-102]

**Summary of Republican “Economic Rescue Principles”**  
*(As released September 25, 2008 at 3 pm EST)*

The line items below were submitted for discussion as House Republicans entered negotiations today. It cannot be predicted if any of the following points will be added in any final bill.

- Wall Street Funded Recovery: Mortgage Insurance Approach:
  - Require the holders of such assets to pay for their own recovery through

insurance, rather than the purchase of frozen mortgage assets by taxpayers.

- Issue insurance for outstanding mortgage-backed securities and charge premiums to the holders of such mortgage-backed securities, approximately half of which are already insured by the Federal Government.
- Private Capital Injections:
  - Remove tax and regulatory barriers that block private capital formation in order to encourage private, rather than taxpayer, investment.
  - Free up capital for private companies to inject into the financial markets by granting temporary tax relief and temporarily suspending dividend payments by financial institutions.
- Immediate Transparency, Oversight and Market Reform:
  - Require participating financial institutions to provide the Treasury with the value of their mortgage assets, the value of any private bids for such assets, and their last audit report.
  - End the securitization of any unsound mortgages.
  - Require SEC to audit reports of failed companies to ensure that the financial standing of these companies was accurately reported and review the credit rating agencies' assessments of failed investment securities.
  - Prohibit Wall Street executives from benefiting from taxpayer funds.
  - Establish panel by January 1, 2009 to make recommendations to Congress on further financial sector reforms (to include representatives from the Treasury, SEC and the Federal Reserve).

### **Distressed Assets Practice**

Day Pitney's Distressed Assets Practice Group is a multi-disciplinary team serving buyers and sellers in connection with acquisitions, dispositions, restructurings, and workouts of distressed companies, including their securities and assets. The group services national and regional clients from our offices in New York, Connecticut, Massachusetts, New Jersey and Washington DC. As a result of the 2007 merger of Day, Berry & Howard and Pitney Hardin, Day Pitney has harnessed each firm's respective history of providing sophisticated distressed assets advice.

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