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Watchdogs: Government overpaid for Wall Street assets

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The federal government overpaid by about \$78 billion for stock and other troubled assets when it bailed out big banks last year, and it lacks sufficient internal controls to police and protect taxpayers' investment in the institutions, government watchdogs said Thursday.

The new special inspector general for the bailout effort, formally called the Troubled Asset Relief Program, issued his first report Thursday and said that the Treasury Department needs to put more safeguards in place to protect taxpayers.

Neil Barofsky said that the Treasury Department, under the Bush administration, focused on purchasing assets from troubled banks and failed to put a plan in place for managing more than \$279 billion in preferred stock that was acquired during the bailouts.

Now he's asking 319 financial institutions for detailed accountings of how \$300 billion in taxpayers' bailout money has been spent. He said his office also would examine whether any bank had misrepresented the value of securities exchanged for the cash.

"If any entity lied to get our money, we will investigate that. We will find it out and we will ... make sure those people are brought to justice," Barofsky told McClatchy Newspapers in a telephone interview. "It is a fundamental part of our mission to root out those types of fraud."

The inspector general's office is working with the FBI and other federal law enforcement agencies, he said. It's hired veteran prosecutors and investigators with a broad range of experience, including securities law. Using about a half-dozen investigators detailed from the FBI and IRS, Barofsky said, his office is conducting several criminal investigations related to the relief program. He declined to discuss details.

The relief program is sure to be a hot topic in Washington on Friday morning, when Elizabeth Warren, the chairman of the program's congressional oversight panel, releases a report on the overpayment of \$78 billion for bank stocks and other assets.

Testifying before the Senate Banking Committee on Thursday, she said that the Treasury paid \$254 billion when it purchased stocks and other bank assets last year. It received assets worth only about \$176 billion, however. Her numbers are close but don't correspond exactly with the inspector general's.

"Because Treasury has failed to delineate a clear reason for such an overpayment, however, the panel is unable to determine whether these objectives have been met or whether they justified the large subsidy that was created," Warren said in prepared remarks. "Once again, Treasury needs clear goals, methods and measurements."

Warren challenged Bush administration assurances that all purchases of Wall Street bank warrants and stocks were at "par," meaning that for every \$100 injected into the banks, taxpayers got securities worth \$100.

A valuation study of 10 transactions - part of the oversight panel's report due to Congress on Friday - suggests that the government overpaid by \$78 billion, she told lawmakers.

While Warren looked backward, Barofsky looked forward and said that much greater internal controls were needed.

"Treasury needs, in the near term, to begin developing a more complete strategy on what to do with the very substantial portfolio that it now manages on behalf of the American people," his report says. "In particular, Treasury needs to develop effective valuation methodologies to value the preferred shares and warrants that it holds and an overall investment strategy to manage the equity portfolio it holds."

The Treasury, according to the report, has invested almost \$300 billion in 319 financial institutions and received \$279.2 billion worth of preferred shares in these lenders. It's received common stock from 230 institutions.

Yet there's no asset manager who's overseeing these shares, and no strategy in place for government stewardship.

"How long these securities should be held and when, and under what circumstances, they should be sold into the market are vitally important questions that implicate not only the taxpayers' return on investment but also the stability of the markets," the report says.

In the interview, Barofsky said that months had passed since the relief program had been established and that a management strategy was sorely needed.

"It would be unfair for us to say on November 10, you have (to have) a full asset-management plan in place. That time is now, or in the very near term," he said.

Treasury Secretary Timothy Geithner already has announced new executive compensation restrictions and other measures designed to improve transparency in the program. He's expected to outline his plans for new finance-sector rescue efforts Monday.

Barofsky's report also says that insufficient safeguards are in place for a \$600 billion program that the Federal Reserve is about to unveil. The Fed and Treasury Department are set this month to start buying top-rated asset-backed securities. These are pools of car loans, student loans and credit card debt that are bundled together and sold to investors in a secondary market.

Private investors won't touch these securities, so the Fed is stepping in to unfreeze this vital credit market. However, the Fed is relying too much on rating agencies and investor due diligence to evaluate the health of these assets, Barofsky warned, and needs better risk-screening procedures to protect taxpayer investments.

A Fed spokesman said efforts were under way to create "a robust compliance program" and that the central bank would "carefully consider" Barofsky's recommendations. The spokesman spoke on condition of anonymity because the Fed's response plan hasn't been completed.

ON THE WEB

Barofsky report: <http://tinyurl.com/buhe84>

Warren testimony: <http://tinyurl.com/btw6eo>

TARP Initial Report: excerpt on warrants: <http://www.mcclatchydc.com/static/TARP/Hall-SIGTARP-Feb-warrants.pdf>

TARP Initial Report: excerpt: <http://www.mcclatchydc.com/static/TARP/Hall-SIGTARP-Feb-132-141.pdf>

TARP Initial Report: excerpt on vendors: <http://www.mcclatchydc.com/static/TARP/Hall-SIGTARP-Feb-vendors.pdf>

TARP Initial Report: excerpt on expenditures: <http://www.mcclatchydc.com/static/TARP/Hall-SIGTARP-Feb-expenditures.pdf>

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