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The Truth About TARP: All Banks Are Not Created Equal

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Much has been written about America's current economic dilemma and measures by the U.S. Treasury to unfreeze credit markets and stimulate lending activity. The Treasury's Troubled Asset Relief Plan, or TARP, as originally designed would permit the government to purchase troubled assets such as mortgage and commercial loans from financial institutions. This move would free capital that banks must reserve for bad loans and be available for new lending activity.

Instead today's TARP program allows the Treasury to inject dollars of new capital directly into banks, taking an ownership interest under specific terms and conditions. The "capital" represented by TARP funds can be used to absorb potential losses in the loan or securities portfolio, to provide "net worth" for the institution to "leverage" by borrowing additional money in the form of deposits or other liabilities, or could simply be "loaned out".

America's media outlets would have you and I believe that every bank that makes application and receives TARP funds is being "bailed out". The current program, as designed, is anything but a government bail out. Here are the facts.

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The nation's largest nine commercial banks, (including banks such as Bank of America, Wells Fargo, Citicorp and others) were deemed too big to fail because of the systemic risk to the U.S. and world economies. These banks control nearly fifty-four percent of the nation's deposits. Some filled their loan portfolios with toxic sub-prime loans, played heavily in the sub-prime securities market and got caught with bad assets and no market to place these assets, or made other strategic errors in judgment. All were "strongly encouraged" to take the first round of TARP money, and indeed did so. Several have received additional TARP funds as well as further guarantees intended to stabilize the system. But that is where the so called "bailout" begins and ends – at least in the commercial banking sector.

Healthy banks, such as the vast majority of our nation's nearly 7000 community financial institutions have also been deemed eligible to apply for TARP funds with specific conditions and limitations. Since October of 2008 the Treasury has committed \$195 billion to 359 institutions in 45 states and Puerto Rico. The banks that have received these funds are held to rigorous evaluation of the bank's management, historical profitability and safety and soundness by their primary federal regulator. Upon passing extensive due diligence, the bank is approved to receive TARP funds. Many of the banks that have opted to participate in the program view the new "capital" as an opportunity to expand lending activity, precisely what the program was designed to do. Despite what you are made to believe, there are many banks that have robust loan demand in this economy and put their dollars to work in local communities.

Community banks that have applied and received TARP funds are not "troubled" banks. So too it can be said that banks that have chosen not to apply for Treasury assistance, are not "troubled." Many bank managers and their respective boards of directors have made the determination that participation in the TARP program was simply not in the bank's best interest consistent with their local business conditions. Some have chosen not to be partners with the federal government; others have determined that current levels of bank capital are adequate to meet the lending demands in their community, and absorb any potential future losses. After all, banks must lend money to make money, and in the case of banks receiving TARP funds, a bank must earn money on this additional capital to meet the interest/dividend requirements mandated by the Treasury and still provide a reasonable return to bank shareholders.

You and I should be outraged by the irresponsible and unethical lending tactics of the too big to fail banks, investment bankers, giant insurance companies and others who have profited greatly from the excesses of the past, and now are in need of government assistance. Our free enterprise system teaches us that success, not failure, should be rewarded. But don't be confused. All banks are not created equal. Community banks are responsible lenders. And frankly, if community banks had the capacity to fill all the lending needs of the American public, we would never have experienced this economic mess in the first place.

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