FINANCIAL SERVICES AND GENERAL GOVERNMENT APPROPRIATIONS FOR 2011

HEARINGS

BEFORE A

SUBCOMMITTEE OF THE

COMMITTEE ON APPROPRIATIONS

HOUSE OF REPRESENTATIVES

ONE HUNDRED ELEVENTH CONGRESS

SECOND SESSION

SUBCOMMITTEE ON FINANCIAL SERVICES AND GENERAL GOVERNMENT APPROPRIATIONS

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NOTE: Under Committee Rules, Mr. Obey, as Chairman of the Full Committee, and Mr. Lewis, as Ranking Minority Member of the Full Committee, are authorized to sit as Members of all Subcommittees.

LEE PRICE, BOB BONNER, ANGELA OHM, and ARIANA SARAR
Subcommittee Staff

PART 5

Printed for the use of the Committee on Appropriations

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(II)

FINANCIAL SERVICES AND GENERAL GOVERNMENT APPROPRIATIONS FOR 2011

WEDNESDAY, FEBRUARY 24, 2010.

FY2011 BUDGET FOR INTERNAL REVENUE SERVICE

WITNESS

DOUGLAS H. SHULMAN, COMMISSIONER, INTERNAL REVENUE SERVICE

Mr. SERRANO. The Subcommittee will come to order. We welcome the Commissioner of Internal Revenue, Douglas Shulman.

OPENING STATEMENT, CHAIRMAN SERRANO

Before we begin, we want to express our most sincere condolences to you, the staff, and the families of the folks that were caught up in that horrible tragedy. There is very little that can be said at times like these, but please stand assured that if there is any assistance you need from us to deal with that particular issue, we stand ready to assist you.

And please convey, on behalf of this Committee, to the employees of the IRS, that we support their work, that we feel their tragedy, and that we personally—I personally believe that no violent action against government employees can be justified, regardless of how anyone feels about any issue in this country.

So before we begin today's hearing, and this is the first hearing of the year for us, we just want to convey that. And I turn to Mrs. Emerson.

Mrs. EMERSON. Let me also express my sincere sympathies, and please let all of the almost 100,000 IRS employees know that we are very impressed by their resilience in the face of such tragedy. And our thoughts and prayers are with the family of Vernon Hunter and all of the employees.

Thank you.

Mr. SERRANO. Thank you. We welcome Commissioner of Internal Revenue, Douglas Shulman, back for his third appearance before the Subcommittee. The IRS employs more than 100,000 people, processes more than 140 million tax returns each year, and collects more than 95 percent of the revenues that fund the Federal Government.

Recently, the IRS has also been involved in implementing an array of tax benefits containing last year's Recovery Act, in addition to preparing for the requirements of the annual tax filing season.

What is still fresh in our minds is last week's tragedy at the IRS facility in Austin, Texas. Our hearts go out to those who were killed, those who were injured, and their families. This Subcommittee will do its part to ensure that the IRS will recover from the difficulties caused by the terrible event last week.

In its fiscal year 2011 budget submission, the IRS is requesting $12.6 billion, an increase of $487 million, or four percent above fiscal 2010.

I want to continue to emphasize the importance of the IRS's taxpayer service mission. Taxpayers who need information and assistance to deal with the complexities of the Tax Code should be able to come to the IRS for help. Good taxpayer service can lead to increased compliance and lower IRS costs in the area of enforcement. The IRS continues to provide assistance through its walk-in sites, partner organizations, and the IRS website and toll-free telephone hotline.

I am pleased that in this budget request the IRS is attempting to address its problems in the area of telephone assistance, and to implement improvements to the IRS website. At the same time, I am disappointed that the budget proposes to reduce funding for grants to low-income taxpayer clinics and volunteer income tax assistance sites. Both of these programs have provided essential assistance to low and moderate income taxpayers throughout the country.

The budget request also reduces funding for tax counseling for the elderly grants. However, I am pleased that the budget request continues the IRS enforcement initiative aimed at offshore tax evasion and corporate and high income taxpayers. The level of tax non-compliance in these areas continues to be a problem, and this initiative will help to address the problem.

In addition, I greatly appreciate Commissioner Shulman's announcement last month of an IRS proposal to increase its oversight of paid tax preparers by requiring registration, testing, and continuing education requirements for preparers not already subject to oversight. Paid preparers are a prominent part of the tax system, and the vast majority of paid preparers are both helpful and ethical, but, as I have pointed out before, there have been many cases of scam artists who bilk taxpayers out of their money.

We have also heard of incompetent preparers who do not make sure that people are able to get all of the benefits for which they are eligible. This has been a problem in neighborhoods, including my own in the Bronx, where the need for the tax benefits is greatest.

The paid preparer initiative is very much needed and will go a long way toward helping taxpayers utilize these services. And I really thank you and congratulate you for that. I thought it was a bold step and one that was due.

I look forward to a very interesting discussion today on these and other issues facing the IRS. Commissioner Shulman, we thank you for your testimony today. I would like to turn to my amiga—how is that? That will create—see, he is scampering all over.

Mrs. EMERSON. Instead of amigo, amiga.

Mr. SERRANO. Yes. There is a difference. Yes, it is amiga. Our ranking member, Mrs. Emerson.

OPENING STATEMENT, RANKING MEMBER EMERSON

Mrs. EMERSON. Thank you, Chairman. Since this is our first hearing, I just want to say for the record that I enjoyed working with you and other members of the Subcommittee last year.

Mr. SERRANO. Thank you.

Mrs. EMERSON. Because we have jurisdiction over such a diverse group of agencies, many of which have a profound impact on Americans' lives and financial stability of our economy, it is good when we try to work in a bipartisan way. And I look forward to continuing that practice this year.

I also want to say that, with the federal debt at more than $12 trillion, I sure hope we can work to find ways to minimize and reducing spending this year as we construct a bill that also safeguards the integrity of our nation's financial system.

Welcome back, Commissioner Shulman. I really do appreciate your being here with all of the—your employees and their families on your mind. And it is important for all of your employees, too. Hopefully they know how deeply moved and how deeply you have been touched by this tragedy as well.

Let me just start by addressing an issue that I know you are hard at work on, and that has to do with tax cheats, for lack of a better way of saying it. Over the last decade, surveys by the IRS oversight board have noted a general downward trend in the acceptability of cheating on your taxes.

However, the 2009 survey reported an increase from six to nine percent of those who feel it is acceptable to cheat on their taxes a little bit here, a little bit there, and similar increases over the next few years of those who believe it is acceptable to cheat on their taxes may highlight a major problem. So hopefully we will be able to work with you to find ways to prevent people from accepting the notion that it is okay to cheat.

As I have stated in the past, I am committed to making sure that you have all of the necessary resources to educate taxpayers on how to comply and identify those who have not paid their fair share, those who willfully file frivolous returns, or conceal assets at home or overseas. But I have to say, with our FY2010 deficit projected to be at $1.6 trillion, and deficit spending expected to continue throughout the next decade, I think it is really critical to review every single area of government spending.

So I need to ask, probably more rhetorically at this moment in time than not, if a $487 million increase to the total budget is really necessary. I am grateful and appreciate the fact that you have proposed a number of cuts and efficiencies in the budget request, but I am interested to know if there are any additional areas that might be trimmed back as well, and look forward to your testimony.

Thanks so much.

Mr. SERRANO. Thank you.

Commissioner, we are ready for you. And after all of these wonderful things we have said about you, we now have to tell you that you have five minutes, and that the rest of your statement can go in the record, so that we can take time to grill you today.

STATEMENT OF COMMISSIONER DOUGLAS SHULMAN

Mr. SHULMAN. Thank you, Chairman Serrano, Ranking Member Emerson, members of the Committee. I am glad to be here to talk about our 2011 budget. Before I do, let me say a couple of things about the tragedy in Austin.

As you know, a plane was intentionally flown into an IRS building targeting IRS employees. I just came back yesterday from Austin, and am going back down tomorrow. What I will tell you is what I told the employees. I am incredibly proud of this agency. Thousands of people have reached out to me from across the country, and (a) said they will do anything to support those employees who are traumatized—we lost a life—and (b) said that it is not going to deter them from their work.

I tell folks that as a leader of a government agency, I stand on the shoulders of those who came before me, to try to improve the agency, to continue with excellence. We are all now going to be standing on the shoulders of a colleague who served two tours in Vietnam, and then died at his desk working for the IRS.

We are going to stand on his shoulders and the shoulders of the people who are traumatized, and try to make this agency better. And I will definitely convey to the workforce your thoughts, and I very much appreciate them.

Moving to the budget, I am very pleased that the President recognized the critical role we play in this country, both serving taxpayers and collecting the money needed to run the government. The unique thing about the IRS is that we have a positive return on investment, so investing in us actually brings more money in and it does have a net positive outflow.

This budget recognizes that, but also recognizes the need to have a balance between service and enforcement, as well as technology and people investment, so we are investing in the long-term future, not just in next year.

On the service side, we tried to balance all of the IRS' needs, from processing paper to dealing with people in person. We increased funding for telephone service, and we increased funding for the web, which meet the greatest variety of needs. And I would be happy to talk to you more about the issues that you brought up earlier around VITA and low income taxpayer clinics.

On enforcement, we are continuing to focus on high income individuals, international evasion, and non-filers. This is a relatively balanced portfolio. We try to maximize impact, maximize deterrent effect across the entire economy, but do so in the least burdensome way to taxpayers while continually respecting their rights.

On the modernization side, we have asked for an increase in our funding for our taxpayer database. I believe that by making this investment we will be able to have all individual taxpayers on a centralized relational database by the end of fiscal year 2011, meeting the promise of faster refunds, better service, and providing consistent information about what a taxpayer owes in our database. I think we are on a path to that promise that we set out to meet in the late '80s, and actually finish it with the funding in this budget. There is also judicious investments in people, so we make sure we have the workforce to do the job.

Let me end by just saying there are a number of legislative proposals. A lot of the reason for our phone level of service going down and other things, is legislation being passed that results in us being given more and more responsibilities to both distribute money and collect taxes. We have asked for some legislative authorities that will actually allow us to better collect taxes, better serve customers, and better do our jobs.

Let me just highlight three. One is repealing the requirement of a partial payment when you try to get an offer in compromise, especially in these difficult economic times with high unemployment. We do not think people who want to settle their tax debt should have to pay a 20 percent downpayment. They should be able to come in, and we should be able to settle their tax debt with them and get them to pay what they owe.

Second is a proposal relating to Section 530 of the Tax Code, which would allow us to create more certainty for small businesses, large businesses, and individuals about whether they are an independent contractor or an employee. And, third, there are a variety of international proposals in the budget that will help us do our job better, including support for a bill that is before Congress right now, which is called FATCA, which gives us better tools to detect non-compliance by those hiding money overseas.

So, Mr. Chairman, this concludes my oral testimony. I would be happy to answer questions.

[The prepared statement of Commissioner Douglas Shulman follows:]

WRITTEN TESTIMONY OF DOUGLAS H. SHULMAN COMMISSIONER OF INTERNAL REVENUE BEFORE THE HOUSE APPROPRIATIONS COMMITTEE SUBCOMMITTEE ON FINANCIAL SERVICES AND GENERAL GOVERNMENT ON FY 2011 IRS BUDGET FEBRUARY 24, 2010

Introduction

Chairman Serrano, Ranking Member Emerson, and Members of the Subcommittee, thank you for the opportunity to appear today to discuss the President's FY 2011 Budget request for the Internal Revenue Service.

In recognition of the critical role that the IRS plays in the nation's economy, the FY 2011 Budget includes a judicious investment in the IRS' core service and enforcement programs. It also includes the funding needed to work toward timely completion of the core taxpayer account database, a key priority for the agency.

The funding in the President's Budget Request will be used to carry out the IRS' strategic and balanced agenda that includes: improved service to taxpayers; a robust and targeted enforcement program to address offshore tax evasion and improve tax compliance for corporate and high-income taxpayers; better use of data, such as credit card and securities basis information reporting; completion of the new taxpayer account data base and enhancements to our electronic filing platforms; and workforce development to ensure that we have a talented and capable workforce for the foreseeable future.

As part of this strategic agenda, the IRS has launched a number of important initiatives, such as our return preparer initiative and Global High Wealth Industry Group, which can improve the effectiveness and efficiency of our work while enhancing the integrity of our tax system. These and other initiatives are discussed in greater detail later in the testimony.

The IRS will also continue to administer on-going, tax-related provisions of the American Recovery and Reinvestment Act (Recovery Act), such as the Build America Bonds, the Worker, Homeownership, and Business Assistance Act of 2009, and any other tax provisions that may be extended.

The Budget also includes nearly $200 million in efficiency savings, reductions, and non-recurs. While these efficiency targets are substantial, and will require tough choices, I am confident that we will achieve them through continued optimization of our operations.

As discussed throughout this testimony, the IRS has achieved significant gains in its core programs, although numerous challenges remain. This Budget will help the IRS stay on a path of continuous improvement, rise to meet the challenges of today, and carry forward positive momentum into tomorrow.

Enforcement

Enforcement of the tax laws is an integral component of the IRS' effort to enhance voluntary compliance. IRS enforcement activities, such as examination and collection, target elements of the tax gap and remain a high priority. In FY 2009, the IRS expanded its enforcement presence in the international arena, continued to pursue high-wealth, noncompliant taxpayers, and initiated action to better leverage the tax return preparer community.

Total enforcement revenue was $48.9 billion in FY 2009. The IRS showed steady progress in increasing its audit coverage:

- Total individual audits increased 2.6 percent;
- Automated Underreporter (AUR) contact closures increased 2.6 percent;
- High-wealth audits increased 11.2 percent; and
- Large corporate audits increased 2.6 percent, a significant achievement given the size (more than $10 million) and complexity of these corporate entities.

The Administration's FY 2011 Budget will help us build on this success and carry out a number of new compliance initiatives that will: (1) address offshore tax evasion; (2) increase coverage of the most strategically important international issues, including complex enterprise structures; and (3) promote compliance in high-wealth individuals and large enterprises, including those with international components, operated by businesses and investors through multiple interrelated financial and tax entities.

International Tax Compliance

To meet the broad array of challenges that we face in the international arena, the Administration and the IRS are focused on a multi-year, multi-faceted tax compliance strategy that is tailored for both sophisticated corporate and individual taxpayers who operate on a global basis. It will require more people, particularly those with expertise in complex issues – such as transfer pricing. It will also require greater cooperation and stronger relationships among nations. Clearly, the success we seek in the international arena cannot be achieved by the US alone.

The ramifications from the IRS' offshore compliance efforts and voluntary disclosure program go far beyond the revenues the IRS will be collecting from these taxpayers. These efforts will change the current landscape and send a clear message that the IRS will vigorously pursue those illegally hiding income and assets overseas, no matter how remote or secret the location.

Moreover, the real effect will be seen over the next ten, twenty and thirty years. Those who came in under the voluntary disclosure program will be in our tax system going forward, and the risk calculus of people thinking about hiding assets overseas to avoid paying taxes has changed dramatically. That protects the US Treasury and our tax base in the long term.

The IRS also continues to seek heightened cooperation and interaction with other national tax authorities. There have already been positive steps in this direction, such as in April 2009, when the G-20 heads of state agreed in a show of unity to act against tax jurisdictions that impede legitimate tax enforcement. A month later, tax commissioners from 34 Organisation of Economic Co-operation and Development (OECD) countries and non-OECD countries agreed on a new cooperative roadmap to combat tax evasion and abusive tax avoidance.

Global High-Wealth Industry Group

In late 2009, the IRS launched the Global High Wealth Industry Group to centralize and focus IRS compliance expertise involving high wealth individuals and their related entities.

Initially, the IRS will be focusing on individuals with tens of millions of dollars of assets or income. Going forward, the IRS will take a unified look at the entire complex web of business entities controlled by high wealth individuals, which will enable us to better assess the risk such arrangements pose to tax compliance.

The IRS wants to better understand the entire complex economic picture of the enterprise controlled by the wealthy individual and to assess the tax compliance of that overall enterprise. We cannot do this by continuing to approach each tax return in the enterprise as a single and separate entity. The IRS must understand and analyze the entire picture.

Tax Return Preparer Regulation

The IRS recently unveiled a major initiative to oversee tax return preparers, who are a critical part of the tax system. Given the complexity of the tax code, more and more Americans now turn to a preparer to help them file their taxes. The IRS estimates that there are somewhere between 900,000 and 1.2 million paid tax return preparers. Making them an integral link to our service and compliance strategies will help the IRS to do its job.

The IRS plans to require registration, minimum competency testing, and continuing education of paid tax return preparers. In addition, once a testing process is set up and running, the IRS will create a public database of preparers, so that taxpayers can find out if they are dealing with a qualified preparer.

The IRS is also shifting enforcement resources to focus on preparers. Beginning this filing season, the IRS is expanding "knock and talk" and other programs to visit thousands of preparers to discuss their operations and ways to reduce preparer error rates.

The goals of the strategy are to leverage the return preparer community to improve service to taxpayers, increase compliance, and enhance the integrity of the overall tax system.

Taxpayer Service

In FY 2009, the IRS continued to improve its services by providing year-round assistance to millions of taxpayers through multiple channels. Demand for telephone services remained high as taxpayers called to obtain information regarding economic stimulus payments, new Recovery Act credits, and prior year adjusted gross income (AGI) numbers needed for electronic filing.

The significant increases in call demand stressed existing resources, resulting in a lower customer level of service (LOS). Level of Service is a measure used by the IRS for both planning and internal management of our live Customer Service Representative telephone assistance services. This measure is derived through a mathematical formula that essentially equates to the success rate of customers that call the IRS for live telephone assistance on our 1-800 help line at any given point in time. However, it does not account for those calling that choose to call back at another time based on anticipated wait time.

Level of Service is but one of many measure used by the IRS to manage its toll-free telephone performance. Others include total calls answered, which for FY 2009 were 39 million, or 5.8 million more than in 2007. For 2010, IRS is planning to answer 36 million calls, or 2.8 million more than in 2007.

Despite the high call volume, the IRS continues to focus on the accuracy of information provided to taxpayers as both Toll-Free Tax Law and Toll-Free Accounts Accuracy performance surpassed the FY 2008 record-breaking numbers.

The President's FY 2011 Budget provides a significant investment to increase level of service by adding resources to meet the ever increasing demand and continuing to make efficiency improvements, such as automated self-service applications that allow taxpayers to obtain information on less complex issues, such as refund inquiries. These improvements free up staff to deal with the more complex tax law issues stemming from the passage of the Recovery Act and the Worker, Homeownership, and Business Assistance Act of 2009.

IRS.gov Website

In FY 2009, there were more than 296 million visits to IRS.gov. Taxpayers visited the website for a variety of reasons, including, to: (1) obtain information on the Recovery Rebate Credit; (2) determine if they qualify for the Earned Income Tax Credit (EITC); (3)

track the status of their refunds using the "Where's My Refund?" application; and (4) get the most up-to-date information on Recovery Act credits.

More than 54 million taxpayers used "Where's My Refund?" – a 39 percent increase over the same period in FY 2008. During FY 2009, the IRS received more than 296 million calls and helped more than 6.2 million taxpayers at 401 Taxpayer Assistance Centers.

The Budget will continue to support these self-service options as well as sustain the development of additional enhancements, such as calculators, on-line tools and information on new legislation in an easy, accessible format.

In addition, the Budget supports a multi-year effort to improve the IRS.gov website to meet taxpayer needs and the growing demand for more electronic services. The new web environment will improve customer satisfaction by making navigation on the site easier, and improve the user's ability to locate desired information and access applications. The initiative will also support the Department of the Treasury's efforts to increase the number of paperless transactions with the public.

Another Successful Filing Season

Despite many challenges, the IRS delivered another successful filing season. During FY 2009, the IRS received 144.4 million individual returns, 11.2 million fewer than 2008, when millions of taxpayers filed solely to receive an Economic Stimulus Payment. The number of refunds issued increased 3.5 percent to 111.4 million. The percentage of individual returns filed electronically reached 66 percent, with more than 95 million individual tax returns filed electronically, compared to 89.6 million in 2008, an increase of 6 percent. During 2009, home computer filing increased to more than 32.2 million, an increase of 19 percent.

The IRS provided extensive media coverage and expanded electronic outreach activities to make taxpayers aware of new credits, deductions, and exclusions for which they qualified. A second Super Saturday event was held in FY 2009, and the IRS provided more than 11,000 taxpayers with tax assistance and return preparation. The event was the largest one-day outreach service event in IRS history.

Recovery Act

In the depth of the recession, IRS employees provided tangible and meaningful relief and guidance to individual and business taxpayers, such as on net operating loss carrybacks and the Make Work Pay Credit, and administering the expanded COBRA health care coverage provisions for employees who lost their jobs. The IRS also helped stimulate the economy through the First Time Homebuyer Credit, while ensuring that appropriate controls were in place to minimize errors and fraud.

Business System Modernization

In FY 2009, the IRS refined its CADE strategy to focus on the completion of the new taxpayer account database. The Budget will help the IRS implement the new taxpayer account database for the 2012 filing season. The new database will allow the migration of 140 million individual taxpayers to a modernized, relational database that will support better processing and result in faster refunds for all individual refund filers.

The new account database also will improve taxpayer service and accuracy and reduce interest paid on late refunds. In addition, it will improve data security and allow the development of new tools to combat fraud and improve enforcement activities. Completion of the taxpayer account database will allow for future expansion of paperless online services and transactions and the next generation of enforcement technologies.

Workforce

The Workforce of Tomorrow Task Force was created last year with the goals of making the IRS the best place to work in government and ensuring that five years from now we have the leadership and workforce ready for the next fifteen years. The Task Force teams conducted a thorough analysis of current processes and developed many recommendations, some of which have already produced valuable results, such as streamlining the hiring of a large number of enforcement personnel in 2009..

To continue the momentum of this key critical area, the IRS will be sponsoring a Workforce of Tomorrow 2010 Summit in early March 2010 to evaluate Task Force accomplishments to date, plan future steps and continue the program's forward momentum.

The Administration's FY 2011 Budget Request Funds Key Priorities

The total resources requested to support IRS activities for FY 2011 are $12,971,962,000. This amount includes $12,633,200,000 from direct appropriations, an estimated $144,592,000 from reimbursable programs, and an estimated $194,100,000 from user fees. The direct appropriation is a $487,147,000 increase, or a 4.01 percent increase over the FY 2010 enacted level of $12,146,123,000.

Enforcement Program

The FY 2011 President's Budget Request includes an Enforcement account increase of $293.4 million for investments in strong compliance programs, including a robust initiative to address offshore tax evasion. As previously noted, additional enforcement resources will address underreporting of income associated with international activities and expand enforcement efforts on noncompliance among corporate and high-wealth taxpayers.

Increased resources for the IRS compliance programs yield direct, measurable results through high return on investment activities. The new enforcement personnel funded through a program integrity allocation adjustment in the FY 2011 President's Budget will generate nearly $2 billion in additional annual enforcement revenue once the new hires reach full potential in FY 2013. Similar to past budgets, the allocation adjustment applies to the Enforcement and Operations Support accounts, and is founded on the net positive value enforcement resources are demonstrated to deliver. Vigorous enforcement also encourages voluntary compliance, further increasing revenue, by generating public awareness of the consequences of not meeting one's tax responsibilities. The return on investment estimate does not include the revenue impact from the deterrence value of these investments and other IRS enforcement programs, which is conservatively estimated to be at least three times the direct revenue impact.

Explanation of Enforcement Budget Activities

The FY 2011 President's Budget request is $5,797,400,000 in direct appropriations and an estimated $61,506,000 from reimbursable programs for a total operating level of $5,858,906,000. The direct appropriations level is an increase of 5.3 percent from the FY 2010 enacted level and includes additional tax enforcement activities funded through a program integrity allocation adjustment. This appropriation funds the following budget activities.

- **Investigations ($651,966,000 from direct appropriations and an estimated $50,567,000 from reimbursable programs)** This budget activity funds the criminal investigation programs that uncover criminal violations of the internal revenue tax laws and other financial crimes, enforce criminal statutes relating to these violations, and recommend prosecution as warranted. These programs identify and document the movement of both legal and illegal sources of income to identify and document cases of suspected intent to defraud. It provides resources for international investigations involving U.S. citizens residing abroad, non-resident aliens and expatriates and includes investigation and prosecution of tax and money-laundering violations associated with narcotics organizations.

- **Exam and Collections ($4,974,618,000 from direct appropriations and an estimated $10,245,000 from reimbursable programs)** This budget activity funds programs that enforce the tax laws and increase compliance through examination and collection programs that ensure proper payment and tax reporting. It also includes programs such as specialty program examinations (employment tax, excise tax and estate and gift exams), international collections and international examinations. The budget activity also supports appeals and litigation activities associated with exam and collection.

- **Regulatory ($170,816,000 from direct appropriations and an estimated $694,000 from reimbursable programs)** This budget activity funds the development and printing of published IRS guidance materials; interpretation of tax laws; advice on general legal services, rulings and agreements; enforcement of regulatory rules, laws, and approved business practices; and supporting taxpayers in the areas of pre-filing agreements, determination letters, and advance pricing agreements. The Office of Professional Responsibility is funded within this budget activity and is responsible for identifying, communicating, and enforcing the Treasury Circular 230 standards of competence, integrity, and conduct of professionals representing taxpayers before the IRS.

Taxpayer Service Program

The FY 2011 President's Budget Request includes a Taxpayer Services account increase of $43.1 million. The increase includes $20.9 million to improve telephone level of service, increasing the level of service performance target to 75 percent from 70 percent in FY 2009 and 71 percent in FY 2010.

Providing quality taxpayer service is especially important to help taxpayers avoid making unintentional errors. Assisting taxpayers with their questions before they file their returns prevents inadvertent noncompliance and reduces burdensome post-filing notices and other correspondence from the IRS.

Explanation of Taxpayer Service Budget Activities

The FY 2011 President's Budget Request is $2,321,975,000 in direct appropriations, an estimated $34,159,000 from reimbursable programs, and an estimated $127,000,000 from user fees, for a total operating level of $2,483,134,000. The direct appropriations level is an increase of 1.9 percent from the FY 2010 enacted level. This appropriation funds the following budget activities.

- **Pre-Filing Taxpayer Assistance and Education ($693,753,000 from direct appropriations and an estimated $1,459,000 from reimbursable programs)** This budget activity funds services to assist with tax return preparation, including tax law interpretation, publication, production, and advocate services. In addition, funding for these programs continues to emphasize taxpayer education, outreach, increased volunteer support time and locations, and enhancing pre-filing taxpayer support through electronic media.

- **Filing and Account Services ($1,628,222,000 from direct appropriations, an estimated $32,700,000 from reimbursable programs, and an estimated $127,000,000 from user fees)** This budget activity funds programs that provide filing and account services to taxpayers, process paper and electronically-submitted tax returns, issue refunds, and maintain taxpayer accounts. The IRS continues to make progress in decreasing paper returns and increasing the use of electronic filing and payment methods.

Operations Support

Explanation of Budget Activities

The FY 2011 President's Budget Request is $4,108,000,000 in direct appropriations, an estimated $48,927,000 from reimbursable programs, and an estimated $67,100,000 from user fees, for a total operating level of $4,224,027,000. The direct appropriation level is an increase of 0.6 percent from the FY 2010 enacted level. This appropriation funds the following budget activities as well as $25 million to improve the IRS.gov website infrastructure and redesign the website to meet taxpayer needs and the growing demand for more electronic services.

- **Infrastructure ($889,929,000 from direct appropriations, an estimated $398,000 from reimbursable programs, and an estimated $16,100,000 from user fees)** This budget activity funds administrative services related to space and housing, rent and space alterations, building services, maintenance, guard services, and non-IT equipment.

- **Shared Services and Support ($1,337,776,000 from direct appropriations and an estimated $33,110,000 from reimbursable programs)** This budget activity funds policy management, IRS-wide support for research, strategic planning, communications and liaison, finance, human resources, and equal employment opportunity and diversity services and programs. It also funds printing and postage, business systems planning, security, corporate training, legal services, procurement, and specific employee benefits programs.

- **Information Services ($1,880,295,000 from direct appropriations, an estimated $15,419,000 from reimbursable programs, and an estimated $51,000,000 from user fees)** This budget activity funds staffing, equipment, and related costs to manage, maintain, and operate the information systems critical to the support of tax administration programs. The IRS business programs rely on these systems to process tax and information returns, account for tax revenues collected, send bills for taxes owed, issue refunds, assist in the selection of tax returns for audit, and provide telecommunications services for all business activities, including the public's toll-free access to tax information.

Business Systems Modernization (BSM)

Explanation of Budget Activities

The FY 2011 President's Budget Request is $386,908,000 in direct appropriations. This is an increase of 46.6 percent from the FY 2010 enacted level. This appropriation funds the planning and capital asset acquisition of information technology (IT) to continue the modernization of IT systems and to move toward completion of the new taxpayer account database. The completion of the core taxpayer account database is the cornerstone of modernization and is a prerequisite to the development of the next generation of IRS service and enforcement initiatives. The integration strategy includes a particular focus on enhanced information technology security practices and robust accounting and financial management controls. This activity also funds the ongoing development of the Modernized e-File platform for filing tax returns electronically. It also funds BSM labor and related contract costs.

Health Insurance Tax Credit Administration (HITCA)

The FY 2011 President's Budget Request is $18,987,000 in direct appropriations. This is an increase of 22.4 percent from the FY 2010 enacted level. This appropriation funds the administration of a refundable tax credit for health insurance to qualified individuals, which was enacted as part of the Trade Adjustment Assistance Reform Act of 2002. The additional resources will help administer the Health Coverage Tax Credit expansion found in the Recovery Act.

FY 2011 Budget Adjustments

The IRS funding increase for FY 2011 is $487,147,000, which includes $219,523,000 for maintaining current levels, a temporary base adjustment of $3,494,000 to support the Recovery Act's expansion of the Health Coverage Tax Credit (HCTC), a decrease of $32,680,000 from non-recurring activities, a decrease of $157,958,000 from efficiencies and savings, and a program increase of $454,768,000 to improve taxpayer service, strengthen enforcement, and complete the new taxpayer account database. By FY 2013, the revenue-producing enforcement investments are projected to increase annual enforcement revenue by nearly $2 billion. The Budget Request supports these activities by proposing the following initiatives:

- $20,945,000 to increase the telephone level of service, which includes a $9.0 million reallocation from the FY 2010 enacted levels for Taxpayer Service grant and advocacy programs;
- $247,446,000 to reduce the tax gap by investing in a strong compliance program; and
- $167,585,000 to complete development of the new taxpayer account database and continue investments in electronic filing systems.

Building on the FY 2010 Enacted Level

The FY 2010 enacted level for the IRS is $12,146,123,000, supporting an estimated 95,070 FTE.

Maintaining Current Levels

- ***Adjustments Necessary to Maintain Current Levels +$219,523,000 / 0 FTE***
  Funds are requested for: FY 2011 cost of the January 2010 pay increase of $47,473,000, the proposed January 2011 pay raise of $119,537,000, the cost of the increase in FERS agency contribution percentage of $16,392,000, and non-

labor related items such as contracts, travel, supplies, equipment, and a GSA rent adjustment of $36,121,000.

Base Adjustments

- ***Resource Adjustment to Support Recovery Act-HCTC Program Expansion +$3,494,000/ 0 FTE*** This temporary base increase will provide additional contractor funding for the continued support, sustainability, administration, and operation of the HCTC program. Taxpayer participation in the HCTC program is expected to grow because of the Recovery Act. The additional contractor support will allow HCTC to serve a significantly larger participant population.

- ***Technical FTE Adjustments $0 /-318 FTE*** This adjustment reflects permanent changes made to ensure FTE levels are fully funded in the base budget.

Efficiencies and Savings

- ***Non-Recur Savings -$32,680,000 / 0 FTE*** This is the net of reductions of non-recurring, one-time costs associated with the IRS FY 2010 enforcement initiatives (e.g., IT equipment and training).

- ***Increase e-File Savings -$22,808,000 / -472 FTE*** This decrease is a result of savings from increased electronic filing (e-File), which is projected to lead to fewer returns filed on paper in FY 2011. The number of returns filed electronically is expected to increase substantially in FY 2011 with the addition of the recently enacted Worker, Homeownership, and Business Assistance Act of 2009 (Public Law 111-92), which requires electronic filing by all tax preparers filing more than ten returns in a calendar year.

- ***Information Technology (IT) Infrastructure and Process Improvements - $75,000,000 / 0 FTE*** The IRS will reduce infrastructure costs through process improvements in IT infrastructure. Initiatives such as the Information Technology Infrastructure Library will allow the IRS to improve the quality of IT services. In addition, the IRS is working to achieve a Capability Maturity Model Integrated certification that will yield efficiencies in software engineering.

- ***Reduce Procurement/Contracting -$25,000,000 / 0 FTE*** In accordance with Presidential guidance on controlling contracting costs, the IRS will generate savings by improving the effectiveness of existing acquisition practices and reduce the cost of contracts.

- ***Reduce Printing, Travel, and Training -$10,000,000 / 0 FTE*** The IRS will generate savings by reducing agency-wide printing of selected internal manuals, selected training materials, and other items, non-case related travel and non-technical training.

- ***Reduce Tuition Assistance Program (TAP) -$5,150,000 / 0 FTE*** The Tuition Assistance Program provides funding to employees for courses that support both career development and the IRS mission. In FY 2011, the IRS will generate savings by restructuring this program.

- ***Eliminate Selective Mailing of Forms and Publications -$20,000,000 / 0 FTE*** The IRS will generate savings by eliminating the non-mandated notice inserts; the automatic mailing of Form 1040, U.S. Individual Tax Return, tax packages; and the automatic mailing of business tax products.

Program Reinvestment

- ***Submission Processing Consolidation (Atlanta) +$2,792,000 / 0 FTE*** Increased use of e-File has led to consolidation of the individual return processing sites. A portion of the Increased e-File Savings will be reinvested to fund the one-time separation costs associated with the September 30, 2011 closure of the Atlanta submission processing site. As the Atlanta consolidation approaches, the IRS will assist employees to find employment either in or outside the organization.

Program Decrease

- ***Reduce Taxpayer Service Grant and Advocacy Programs -$9,000,000 / 0 FTE*** The FY 2010 appropriation included an additional $3,500,000 to expand Taxpayer Advocate Service case processing activities; $500,000 to increase the Low-Income Taxpayer Clinic (LITC) grants program; $1,000,000 to increase the Tax Counseling for the Elderly (TCE) grants program; and $4,000,000 to increase the Volunteer Income Tax Assistance (VITA) grants program. These program decreases will realign the programs to the 2010 requested level to fund the Increase Telephone Level of Service initiative.

Program Increases

- ***Improve IRS.gov +$25,000,000 / 0 FTE*** This initiative, part of a multi-year plan, will initiate the migration of IRS web content and applications from the current outdated portal infrastructures to a new consolidated IRS web environment. These funds will enable the IRS to complete the first phase of the migration of the taxpayer-facing content and applications and to begin the second phase of the migration and transition of approximately 35 percent of the public and partner-facing applications to the new environment.

- ***Increase Telephone Level of Service +$20,945,000 / 0*** FTE Recent legislation has led to an unprecedented demand for telephone services over the past few years. In addition, the additional complexity of – and time needed to resolve – many phone calls, resulted in a decline in the telephone level of service. This initiative will improve the telephone level of service from a projected 71 percent in FY 2010 to a target of 75 percent in FY 2011 through a program increase of

$11.9 million and a $9.0 million reallocation from TAS and the LITC, TCE and VITA grant programs.

- ***Address Business and Individual International Compliance +$121,086,000 / +781 FTE*** This initiative supports the Presidential priority to address offshore tax evasion and builds on the IRS FY 2010 international enforcement initiative. It will allow the IRS to continue its multi-year investment in international tax compliance activities. It increases coverage of the most strategically important international issues, including large enterprises with international components operated by businesses and investors through multiple interrelated financial and tax entities and high-wealth individuals and the complex business enterprises they control.

  This initiative will increase examinations of additional international issues pertaining to international structures involving tiered pass-through entities, corporations, and high-wealth individuals by a projected 4,864 cases. The increase in examinations will generate $812.2 million in additional enforcement revenue once the new hires reach full potential in FY 2013.

- ***Reduce the Reporting Compliance Tax Gap +$77,679,000 / +700 FTE*** This initiative will improve compliance by increasing examination of field and correspondence individual return audits by 61,100 annually; business return audits by 1,200; audits targeting employment, excise, and estate and gift taxes by 9,300; and Automated Underreporter (AUR) document matching individual return audits by 234,000. This request will generate $659.6 million in additional enforcement revenue once new hires reach full potential in FY 2013.

- ***Reduce the Nonfiling and Underpayment Tax Gap +$38,181,000 / +406 FTE*** This initiative will allow the IRS to broaden its collection coverage and address the tax gap more effectively by increasing staff resources for field collection and the Automated Collection System (ACS) program. The additional staff will produce an additional 144,000 tax delinquency accounts (TDA) (i.e., balance due accounts where returns were filed, but the taxes have not been paid) and 22,500 tax delinquency investigations (TDI) (i.e., investigations of taxpayers with unfiled returns who have not responded to a notice). This request will generate $474.4 million in additional enforcement revenue once new hires reach full potential in FY 2013.

- ***Support of Increased Enforcement Activities +$5,000,000 / +65 FTE*** Most tax enforcement actions result in downstream Accounts Management activities, including account adjustments, assisted phone calls, amended returns, and installment agreement preparation. This funding will allow the IRS to assist taxpayers to resolve issues early in the enforcement process, pay their taxes, and respond to and close out various enforcement actions. Improving the response to taxpayers who have received enforcement notices should increase revenue and reduce interest paid.

- ***Maintain Recovery Act Staffing +$5,500,000 / +31 FTE*** Among other responsibilities, the IRS is mandated by the Recovery Act to administer the new bond provisions. The Treasury is required to issue a direct payment to the bond issuer. The unique nature of this new role requires continuous compliance reviews and verification throughout the administrative life of the bonds. This initiative will extend IRS staffing resources received in the Recovery Act to administer ongoing Recovery Act bond provisions.

- ***Business System Modernization (BSM) +$167,585,000 / +156 FTE*** The BSM increase is a top priority for the IRS and will allow the completion of the new taxpayer account database for the 2012 filing season. The new taxpayer account database will result in faster refunds for taxpayers, improve service accuracy and timeliness, and enhance data security. Completion of the taxpayer account database is a prerequisite for other major initiatives such as significant expansion of online paperless services and next-generation enforcement technologies. The ability of the IRS to support increasingly complex taxpayer service and compliance initiatives will be severely limited until it is completed.

Legislative Proposals

The FY 2011 President's Budget includes a number of legislative proposals intended to improve tax compliance with minimum taxpayer burden. These proposals will specifically target the tax gap and generate nearly $26 billion over the next ten years. Among other proposals, the Administration proposes to expand information reporting, improve compliance by businesses, strengthen tax administration, and expand penalties.

Expand information reporting – Compliance with the tax laws is highest when payments are subject to information reporting to the IRS. Specific information reporting proposals would:

- Require information reporting for private separate accounts of life insurance companies;
- Require information reporting on payments for services to corporations;
- Require a certified Taxpayer Identification Number (TIN) from contractors;
- Require increased information reporting on certain government payments;
- Increase information return penalties; and
- Require information reporting on expense payments relating to rental property.

Improve compliance by businesses – Improving compliance by businesses of all sizes is important. Specific proposals to improve compliance by businesses would:

- Provide Treasury regulatory authority to require that information returns be filed electronically;
- Require corporations and partnerships with assets of $10 million or more that are required to file Schedule M-3 to file their tax returns electronically;

- Provide Treasury regulatory authority to reduce the current threshold, filing 250 or more returns during a calendar year, to require electronic filing of certain other large taxpayers not required to file Schedule M-3 (such as exempt organizations);
- Implement standards clarifying when employee leasing companies can be held liable for their clients' federal employment taxes; and
- Increase certainty about the rules pertaining to classification of employees as independent contractors.

Strengthen tax administration – The IRS has taken a number of steps under existing law to improve compliance. These efforts would be enhanced by specific tax administration proposals that would:

- Expand IRS access to information in the National Directory of New Hires for tax administration purposes;
- Make repeated willful failure to file a tax return a felony;
- Facilitate tax compliance with local jurisdictions;
- Extend statutes of limitations where state tax adjustments affect federal tax liability;
- Improve the investigative disclosure statute;
- Repeal the requirement of a partial payment with an application for an offer-in-compromise;
- Allow assessment of criminal restitution as tax; and
- Codify the "economic substance" doctrine.

Expand penalties – Penalties play an important role in discouraging intentional noncompliance. A specific proposal to expand penalties would:

- Impose a penalty on failure to comply with electronic filing requirements; and
- Clarify that the bad check penalty applies to electronic checks and other forms of payment.

Improve Tax Administration and Other Miscellaneous Proposals

The Administration has put forward additional proposals relating to IRS administrative reforms. These proposals would:

- Improve the foreign trust reporting penalty;
- Apply the Federal Payment Levy Program to contractors before providing Collection Due Process; and
- Clarify that a vendor levy on "goods and services" would not exclude "property."

Conclusion

Mr. Chairman, thank you again for this opportunity to testify on the President's FY 2011 Budget for the Internal Revenue Service. We urge its passage. It provides the IRS with the much needed resources to provide taxpayers with high quality customer service and bolsters IRS enforcement in critical areas, such as unlawful offshore tax evasion. It also makes wise investments for the next generation of technology and the IRS workforce. I also urge this Subcommittee to support the enactment of the legislative proposals included in the Budget to improve compliance. I look forward to working with you and the Subcommittee on this important Budget Request and I will be happy to respond to any questions.

TAX RETURN STATISTICS

Mr. SERRANO. Thank you so much. Let me ask you a question. Does the agency have any information on how many tax returns we get in the country?

Mr. SHULMAN. Give or take, 140 million individual returns annually.

Mr. SERRANO. Okay. And of those, do we know how many folks prepare it themselves, how many have an accountant, and how many just go somewhere other than an accountant?

Mr. SHULMAN. The last year for which we have the data analyzed and collated is '08. About 60 percent of people used a preparer, some form of a paid preparer. About 20 percent used software packages, so they were doing it themselves with the assistance of technology. And then, about 20 percent just do it themselves on their own.

What I will tell you is, interestingly, the numbers are on the rise around people who do it themselves and file directly on the Internet. We have a horrendously complex tax code, but I believe we should have as many people as possible able to file themselves and do it for free. And so that is why we have a variety of outreach. We prepare millions of returns between us and our partners.

We also put online a web application that allows you just to fill out the form and the application does the math calculation for you. It does not go as far as the software, which guides you through your answers. And so I think more and more people are trying to do self-service. I would be happy to talk later about the return preparer initiative, which is incredibly important because of those 60 percent of people that are getting service from a return preparer, which is also affecting their compliance.

PAID PREPARER INITIATIVE

Mr. SERRANO. Right. And that was my question. It was a lead-in to the fact that I commended you for the position you took, and you noted in your written statement that the IRS is increasing its "knock and talk" visits with tax preparers this year. What are the specific steps that will be taken over the next year to begin implementing the paid preparers initiative?

Mr. SHULMAN. The preparer initiative has multiple components, and the goal is, really, to make sure preparers are providing people good service and making sure preparers are helping us make sure people pay the right amount of taxes. So it is a compliance and service initiative.

People are going to register, take a test, and make sure they are prepared through continuing education. We are going to have a database once everyone takes the test, so the public can look and say, "Am I using a registered preparer?" And then, we are increasing enforcement.

This is going to be a multi-year effort. We estimate about a million people are preparers, and so to implement this kind of regulatory regime for the preparer community is not an overnight thing. This year we sent out 10,000 letters reminding people of obligations, and we stepped up calling people and saying we were going to come talk to them, make sure they were doing things right, audit preparers, etcetera.

And so that effort is happening right now, and "knock and talks" include calling them and telling them, but also some undercover visits where we suspect fraud.

We are going to get guidance out this year. Our goal this year is to get everybody to have a preparer number, so we can start tracking them. Our goal next year is to start the testing regime and let everyone have about two years to test in and be a preparer, and also next year to start pushing out continuing education.

And so within three years, the initiative will be fully implemented. Anyone providing any peparation service will have been tested and be in a database available for the public. It is our goal, but this is all very fluid. One of the things I am committed to is a very open process for this initiative. We held public hearings. We have talked to people. We signaled what we were going to do. We took comment. And so we have listened to taxpayers, we have listened to consumer advocates, we have listened to the preparer community, and we are trying to make this a smooth transition to ultimately help the tax system.

The last thing I would say is that this initiative is potentially the most transformational step that we will take while I am here to really increase compliance and service. What we are really doing is saying let us make sure those million people who are part of the overall tax system are qualified. And if we are going to have a complex tax code where people have to go to preparers, let us make sure they are part of the overall solution to serving Americans.

Mr. SERRANO. Right. You know, with that in mind, we all come to Congress bringing with us our likes and dislikes, those things we feel strongly about, and those things that make us nervous. I may be totally off base here, but I tell you, it makes me nervous to see in my district a person dressed in a Statue of Liberty outfit handing out cards, saying down the block, "We will prepare your taxes for you."

Now, in a way, that is a contradiction to who I am, because the person who is dressed in the suit is probably otherwise unemployed, and that is the job they have. And the people who are taking the card to go see that preparer cannot afford to go to where I go or to where JoAnn goes to get her taxes done, or do not have access to a computer, or would not even dare try to fill out their own.

So, in a way, I realize that as I am making this statement I am kind of contradicting myself, because I am commenting on the very people that I know somewhat about the condition they find themselves in. But paying your taxes, filing your taxes, to me is one of those issues that is very serious.

EARNED INCOME TAX CREDIT AUDITS

And the whole idea of a circus attitude around it makes me nervous, so I support anything that happens in the direction of finding out whether the person who taxpayers meet after they walk through the door is qualified to give them the best assistance. That is something that you will get a lot of support on from this Committee and from this Chairman, because it just makes me nervous that we are heading towards a major problem, which leads me to the next point, and that is, as you recall when we first met, my biggest complaint was the fact that—what was it, 44 percent of all the audits were being conducted on 17 percent of the taxpayers? Which were the—if I have got my numbers right, the EITC folks?

And I suspect that a lot of the EITC issues were not necessarily harassment by the IRS, but the people who were preparing these forms. What was there, intentionally or otherwise, that caused so many audits?

Mr. SHULMAN. You and I have talked a number of times about EITC. It is a tricky issue, because in one respect, we are incredibly proud that the IRS is part of the process of putting out about $50 billion a year to help raise people out of poverty, about 24 million people. But when there is a large refundable credit, there is also opportunity for fraud.

I think you hit the point right on, which is a lot of fraud is happening not because the taxpayer is intending to defraud, but they go to unscrupulous preparers who help coach them through. They say, "You can get more EITC if you have a child living with you for six months," and so the taxpayer says, "Well, they were with me five months." And the preparer says, "Well, why not just put down six months and you can get a bigger refund?" and then these people get a refund anticipation loan and it all churns.

We have, over the years, had a steady number of EITC audits. The have gone down as a percentage of overall audits, because we have been increasing the number of audits, for instance, in the last five years, on millionaires. And we have increased the audits on people earning over $200,000. We have not increased EITC audits.

With that said, EITC audits bring in or save, because we stop money before it goes out—about $3 billion a year. And so our main focus is to keep it steady, to not unfairly target people who get EITC, but in the same respect, have a decent coverage rate because big refundable credits are where there is often incentive for fraud. And then, the preparer strategy, we think, is a cornerstone to reducing that fraud and error, because error is a big issue with EITC. It is a 68-page form. It is incredibly convoluted.

And so part of this initiative is educational outreach, and our whole EITC program is all about maximized participation, minimized fraud. As with a lot of things we do at the IRS, we have got to get that balance right, and that is what we try to do.

Mr. SERRANO. Thank you.

Mrs. EMERSON. You know, let me mention something interesting. I recently, probably two weeks ago now, did a—had all of my community organizations come in and we actually did a taxpayer clinic with a lot of these community-based organizations and some of the organizations that actually do free computer—you know, like Intuit and, well, the TurboTax people and all those folks, just to help train some of these folks to then assist their clients who would be able to claim the EITC.

And one of the interesting things that we did talk about, too, though, are those refund anticipation loans which I hate. It is like going to the payday lender and getting all sorts of outrageously high interest rates and, in essence, you know, those companies are ripping off the people who, you know, need that short-term help.

But hopefully through your business systems modernization, and other services that you are able to provide, will make the refund so much faster that they do not have to get those anticipation loans, because I do not like that whole concept, just because they have to pay so much interest.

TELEPHONE LEVEL OF SERVICE

I wanted to ask you a little bit about the telephone service. And if I could, just because it is such an important part of your mission, just looking at the figures, between FY2007 and FY2008, the level of phone service plummeted from 82 percent to 53 percent. And we have been told that was attributable to all of the demands placed on the agency by the passage of nearly 50 new tax provisions, of course that we imposed upon you all from Congress.

But in looking at this year's budget request, your goal is to get from 71 to 75 percent, which I do not find particularly exciting. I mean, it does not seem to me for $20.9 million that four percent of an increase is enough of a stretch I guess. I would think that we would want to expand the phone service a little bit better.

But does not it make sense that if we want to improve tax compliance then the phone service should be a guaranteed avenue available to all taxpayers to get their answers? Are you comfortable, or do you find 75 percent acceptable?

Mr. SHULMAN. No. I am glad you asked me about phones because there has been a lot of focus on it. Let me just start by saying I am not happy where we went, but let me also put it in context. We were hitting the 80 percent level of service. Let me explain what level of service is because 80 percent level of service does not mean 20 percent are not getting through, which is important. But we were hitting our level of service internal numbers for a number of years when we were getting about 65 million calls a year.

When we sent out the stimulus checks we went from 65 million to 150 million calls that year. Last year, as we were cleaning up from the stimulus checks and implementing the Recovery Act, we had about 100 million calls. And so, while this one number everyone has been focusing on—level of service—has been dropping, we have been answering five million more calls every year.

Telephone level of service is a composite number that includes people who get through, people who cannot get through, and people who voluntarily hang up. And one new feature we made available is estimated wait time. If you call at peak season, first week of April, first thing in the morning, you are going to have a longer wait than if you call later in the evening or you call at a different time.

We put a wait time on the phone lines, which was a service, so you tell taxpayers it is going to be a six-minute wait to talk to an assistor. And if someone does not have six minutes, he or she hangs up and calls back at a different time.

If you look at last year, our 70 percent number, and you take away people who hung up within three minutes, because this is the first time it ever said it would take this long, that number went up to 79 percent. And so included in there is what we call voluntary disconnects.

I will also tell you the phone calls are taking longer, because the tax law is getting more complex. There are a bunch of new tax laws in place. We are doing a lot of Recovery Act calls, and so that is important.

And the last thing I would say before I answer your question directly about the 75 percent is look at the main service number, which is the American Customer Satisfaction Index. Again, it is not how many people are happy, but it is what is the taxpayer experience with filing, phones, walking in, Internet.

So it is really looking at all of our channels, not just one of our channels. That score actually jumped this year from 68 percent to 71 percent, so we continue to make it easier for people to deal with their taxes. But the phones are an issue.

The reality is demand is driving these numbers, and so we are going to answer more calls this year than we answered last year, and we are going to answer more calls next year than we answered the year before. We are anticipating more calls than before.

My goal is to next year, in '11, get it back up to 75 percent, but we have those wait times, so it is well over 80 percent if you take away the people who are hanging up right away. We will keep driving that back up to historical levels. Hopefully we do that by getting back to historical levels of tax changes every year, as well as helping drive demand down.

TAXPAYER SERVICE FUNDING LEVELS

Mrs. EMERSON. Well, I hope so, too, because since we are giving, you know, a fair—I used to think that $20.9 million was a lot of money, but as we start using the "trillion" word somehow it does not seem quite as high as it used to. But, nonetheless, hopefully you will be able to achieve those goals.

And let me just mention, too, because Joe did as well, the VITA services that you all provide have been tremendously helpful in my district, and I actually went on a couple. Have you ever been on one? They are great. To go with—to go to like a senior center and have the voluntary—the tax preparers there. And it is hugely popular, and I just would like—I am not happy with the amount of money for that service being cut, and hopefully, Mr. Chairman, you will be able to figure out how to add some more back, so that the Commissioner——

Mr. SERRANO. Is this without adding to the deficit, or what?

Mrs. EMERSON. I am sure we could take a little bit from here, but we do not——

Mr. SERRANO. I know.

Mrs. EMERSON [continuing]. Want to have to ask the Commissioner to say bad things about OMB.

Mr. SERRANO. Right.

Mrs. EMERSON. All right. I will stop there and——

[Laughter.]

Mr. SERRANO. Thank you so much. And, by the way, I was unpopularly trying to be funny.

Mrs. EMERSON. I know.

Mr. SERRANO. But you are right, there are services that should not be considered part of a concern about how we spend money, because those services have to be there.

I am supposed to make a statement right now, since it is the beginning of our second season of hearings, for members to stick to the five-minute rule. But I am not worrying too much about it, since I broke it at the beginning.

Ms. Lee.

OPENING STATEMENT, CONGRESSWOMAN LEE

Ms. LEE. Well, thank you very much. You are a very fair chairman. And thank you, it has been a pleasure being on your Committee. I think last year was my first year on the Committee, and it has been very enlightening and very helpful for me and my district, so thank you, Mr. Chairman.

Mr. SERRANO. You are quite welcome.

Ms. LEE. Good morning, Commissioner Shulman, and let me just thank you, first of all, for your testimony, also for your service during this very challenging period.

And I want to also associate myself with the remarks of my colleagues. My sympathy goes out to the family and members and staff of the IRS, and to yourself, and just know that we all stand to help you during this very tragic period in anything that we need to do to help your family, our family, move forward.

Mr. SHULMAN. Thank you very much.

Ms. LEE. I want to also just thank all of the dedicated staff for rapidly and efficiently putting into place some of the very vital tax breaks for working families that the Congress passed and the President signed during the height of the economic crisis.

I know that many of the provisions have really directly impacted the work of the IRS, like the homeowners tax credit, the make work pay credit, and the extended child tax credits, as well as the COBRA extension. Your leadership and the work of your staff really has ensured that taxpayers were able to take advantage of these vital programs during the downturn that really did help stabilize the economy and helped to reduce the terrible impact of this financial crisis.

The ongoing recession, rising unemployment, this means that millions of Americans continue to face the harsh reality of living in poverty. The work of the IRS to rapidly follow through on implementing the credits and other initiatives that the President, you know, put forth, that has kept untold families out of poverty, those hanging right on the edge, and also has provided vital assistance to families who find themselves facing the brunt of this economic crisis. So I have to thank the IRS for that.

Oftentimes we do not focus—at least many in my district do not focus on the positives of the IRS. The IRS sometimes becomes a very difficult agency for many people to deal with, but I think they have seen a different side of the IRS during this very serious economic downturn.

I want to ask you—well, first of all, I am glad that you are getting Americans to file taxes electronically and streamlining the filing process and the refund process. I also support the increased funding that the IRS requests for business systems modernization, and it is my hope that strategic investments in these systems will make tax time more efficient for the IRS and the American taxpayer.

READY RETURN PROGRAM

Now, in California, which is my home state, we have a program called Ready Return where the state sends a pre-populated or pre-filed—pre-filled tax return to tax filers, and they are very simple, these returns. Taxpayers then just simply review the form for errors, and, if everything is correct, they just sign it and mail it in. And I believe the President has supported the possibility of a pro-populated return as—a pre-populated return as well.

I think that the IRS could save a lot of money if you implement this national Ready Return Program. It will save time, it will increase compliance, it will make tax season really a lot less painful. And so I would like to know if you looked at that. Do you think that makes sense? And how can we help if it does?

TAX EXPENDITURE CHART

And then, secondly, let me just say I think it would really be an important public service to provide the American taxpayer a breakdown of how much of their tax dollars go to programs like housing, education, science, technology, transportation, infrastructure, health care, defense.

And I would like to ask you, and I would like to ask the chair, if we could consider including a detailed graph or chart of how the United States—how our government spends tax dollars with each tax form distributed by the IRS, you know, maybe a pie chart or some kind of a graph or something that really shows the taxpayer how their money is being spent.

BUSINESS SYSTEMS MODERNIZATION AND READY RETURNS

Mr. SHULMAN. On a couple of the points you raised, one is thank you for your support for BSM, our business systems modernization. I have run big technology projects outside of the government, and coming in I saw the IRS had some missteps in the '90s around its modernization, but for an agency that interacts with 140 million individual Americans, not to mention all the non-profits and businesses, and processes, two billion information returns, crunches huge amounts of data, I think we have underinvested in our technology over the years. And so getting us back on a prudent path makes sense.

I also think that modernization is linked to any concept of pre-populated returns. A lot of what this investment is is getting us to the point where we have all of the data on the taxpayer in one place. It is getting this relational database done.

And so we certainly have looked at and are very familiar with the California Ready Return example. I think there is a question of how many people would be eligible, because I understand the California program is for single people who take the standard deduction who only have wage income. There is a set of criteria around it, and so it is not 140 million eligible people.

But, you know, I think our goal is to get this modernization done, and then really open our eyes and say, "How can we better service taxpayers once we get this investment over the goal line?"

TAX EXPENDITURE CHART

On the chart idea, it is very interesting. I tell people that people say, "Oh, you are the tax collector." And I say, "Yes, well, that is our moniker, and that is what the IRS thinks of, but we are also the people who make it possible to have national defense, and to have environmental protection, and to have whatever else you want the government to do for you."

And so communicating that kind of a message is a big part of what I try to do as a leader of the IRS. I will not speak to the specific proposal. I view it as probably a broader policy call whether you want to tell people exactly where their tax dollars are going, but I know you directed that to the chairman. [Laughter.]

Ms. LEE. Thank you very much. But also, Commissioner, I would like to just hear your feedback, and thank you for your feedback.

But, Mr. Chairman, I would like to talk to you and our ranking member about that, because I think the more transparency taxpayers have about where their tax dollars go the better equipped taxpayers are, you know, to really communicate to us what they think about our priorities.

Mr. SERRANO. Thank you so much. As the saying goes, you collect it, we spend it. [Laughter.]

Mrs. EMERSON. And then spend and spend.

Mr. SERRANO. Please stop. [Laughter.]

We are very frugal on this Committee.

Every time that we have a hearing I ask my staff, are we on TV? And I want to tell you the reason is because I love that tie, and that tie should be on TV. [Laughter.]

Mr. Crenshaw.

Mr. CRENSHAW. Thank you, Mr. Chairman. I like your tie, too.

Mr. SERRANO. Thank you.

Mr. CRENSHAW. Yes, it is a nice tie.

TAX GAP, INVESTMENTS AND RETURN ON INVESTMENT

But thank you for your service in the difficult times, and thank you for your testimony today. I wanted to ask you about this so-called tax gap. You know, it has to do with compliance I guess. I mean, everything I understand about compliance is that either people—they underreport their income or they do not pay all their income, or they just do not even file a return.

But most of the non-compliance, as I understand it, is just underpayment. And everything I read that—for every dollar you collect you miss maybe $15 or $20, that the so-called tax gap is about 15, 20 percent of the overall tax revenues. And if that is the case—and you can comment on that—but if we collect, let us say I guess, $2.7 trillion, you figure it up, then maybe—and I have read that the tax gap is about $350 billion, which kind of fits, about 15 percent of that $2.7 trillion, I just wonder—and I guess from time to time we have all heard some of our colleagues, you kind of use the tax gap as kind of a piggybank. And they say, "Well, I have a new program. It costs $50 billion. So if we just spend a little more money on enforcement, then we will get $50 billion."

And in your budget, you have got almost $6 billion, almost half the money you spend you spend on enforcement. And so I have always been curious about that. Number one, how do you kind of determine what that tax gap is? How do you decide that this year's ballpark is going to be $350 billion, or whatever? And then, number two, how do you decide—I mean, obviously, it is not that simple, because if you say—if you appropriate $6 billion, then the tax gap will only be $350 billion, which is a lot of money, and somebody would say, "Well, why do you not ask for $12 billion, and then the tax gap maybe would go down by half, $175 billion, and that is money well spent."

So I guess it is not that easy, or you would just say, "Give us more money for enforcement, and we will eliminate the tax gap altogether." So talk about that. How do you kind of figure out what it is? And then, how do you decide how much money you want to spend on enforcement? For every dollar you spend, you know, is that money well spent in decreasing that tax gap?

TAX GAP

Mr. SHULMAN. Let me try to address it in a number of ways. The tax gap is basically the voluntary compliance rate in the country because we have a voluntary tax system in general. We are not going in to everybody and taking the money before you ever have it. Generally, people get their money, and they fill out a tax return themselves, and they send it in. Then we have audit coverage, we have programs, et cetera.

The tax gap number to which you are referring, I would say is imperfect. It is very hard to say what it is. You know what you get. It is hard to figure out what you do not get. The way we do it is through a National Research Program. Usually when we do an audit, we go and do it because there is some indication of error or fraud. We have a variety of formulas and algorithms that point us in the direction of places that it would be fruitful to do audits, as well as doing some geographic coverage and industry coverage, so people know that in general, they are just not going to get off scot-free.

NATIONAL RESEARCH PROGRAM

To study the tax gap, we actually have a program called the National Research Program, which does random audits. So instead of going and doing an audit and finding out how much someone really owed because we had some indication to conduct an audit, we audit people where we have no indication of issues and see what that spread is. And, as you said, the gap runs about 16 percent, but we then bring in about two percent, so it runs about 14 percent.

There are only five other countries that try to measure their tax gap, and generally it is all about the same as ours. There is some level of noncompliance, and it depends on how your society runs: how much cash economy you have, how much information you have. I have told a variety of people, there are some Nordic countries where you are born and you are given a number, and you have that number in the hospital, and that is your number at your school, and that is your number for your health care, and that is your number for your employment, and there is a lot of tracking.

That is not how our society works. We do not have as much government intervention. You could go in a different direction and probably narrow that gap.

LEGISLATIVE PROPOSALS

Half of the money we bring in, we bring in from people who pay their wages by having taxes withheld at the source. So half the taxpayers are 99 percent compliant. So your schoolteachers, your firemen, your policemen, we get their W–2, they get their W–2, their employer withholds taxes, and there is no noncompliance.

Almost all of the noncompliance in the tax gap comes where we do not have third party information or there is no withholding. And so a lot of the thrust of where you have seen my major initiatives and the administration's initiatives over the last several years, supported by President Obama and the Secretary and others, are around information reporting, better information reporting for us, so that we are less intrusive. So we are not doing audits, as much as we are matching information and sending a letter that says, "We see a mismatch." And there are a bunch of proposals in the President's budget.

For international compliance, where money crosses the border and you do not see it, it disappears, we are asking for some information on cross-border transactions, as well as heightening the responsibility for banks to give us information on their clients once they leave the country.

Then, we have this preparer initiative that the Chairman was talking about, again, enlisting them to help us do our job. In this budget we have roughly $300 million of pure enforcement investment. That is going to return $2 billion. We do audits, we get money from that effort. The deterrent effect is much higher than that, and we do not try to, especially for Appropriations Committees and budgets, say exactly what that is.

But if we are focusing on high income individuals who have nonreporting, the word is going to get out there. So we are going to get a certain amount in the audits, but we are also going to deter noncompliance. But a lot of the future to get the real money in the tax gap is some of these much broader programs, from information reporting, the preparer initiative, and some of our international strategy.

But I think there is a real tradeoff. You are never—I do not think you want a society where there is no tax gap because it means the government is so intrusive. I am the IRS Commissioner and I think it is a balance between how intrusive the IRS is, how much burden is imposed, and bringing in the money. And we try to balance all of those along the way.

RETURN ON INVESTMENT AND THE BUDGET

Mr. CRENSHAW. Just one quick followup. There is really not any empirical data, like if you spend an extra dollar—when you decide you want—like you said, it is not only enforcement money, it is a lot of the other programs, so that you really cannot quantify, say, "If I just had $1 million more to spend on enforcement, I could pick up an extra X dollars." It is not really that sophisticated.

Mr. SHULMAN. Oh, no. We absolutely can do that.

Mr. CRENSHAW. Then, why do you say, "We want $5.7 billion for enforcement," and not say, "We want $6 billion," which is another $300 million which might get you, you know, more than you spent.

Mr. SHULMAN. I mean, I think you have to balance the investment with capacity. And so we have rough orders of magnitudes. When we bring people on, it actually takes three years to get them fully up and trained and productive. We have to take our best people offline to recruit and analyze if we are getting a good person who can do financial forensics, who has an accounting degree.

Then, we take good people offline to do training. So a lot of this decision is about capacity. I mean, this is basically what we think we can handle. What you really want to do is a multi-year investment that is somewhere in this range over multiple years and buildup. If you gave me $1 billion and said, "Hire a bunch more agents next year," I would say, "I do not want that," because I have got to run the operation, I have got to have my exam coverage this year.

I think the way we came up with this $300 million is, how do we invest money to make sure we are part of bringing down the deficit, collecting the money that is due? What is a prudent investment, given what was invested last year? What are the other priorities of the agency?

But this revenue-producing enforcement money, we have formulas, and they are heavily vetted between OMB and CBO. They have done a 10-year look-back. They have said, "What have we brought in based on what has been invested?" And so the pure enforcement numbers are very clean, and we know that on average it is about a seven-to-one investment.

What is harder to quantify is BSM, our business systems modernization. I can guarantee you that is going to help compliance. There is going to be better service; there is going to be better enforcement. It is very hard to get a number that the budgeteers around Washington and the analysts will all agree on. The preparer strategy is going to bring in money.

Those investments do not have return on investment attached to them in the submission because we do not have the 10-year history around them. That is part of the trick of how do you run an agency? How do you make bets on the future? How do you keep getting better every year in a world in which throwing a dollar at an examiner is the thing that you know returns the investment but you have still got to move the agency forward?

Mr. CRENSHAW. Thank you. Thank you, Mr. Chairman.

Mr. SERRANO. Thank you. I want to take this opportunity to inform the Committee that David Reich, our Committee Clerk last year, is now the Committee Clerk for the Labor-HHS Subcommittee. And Mr. Lee Price, this very studious-looking gentleman watching over my shoulder here, is our new Committee Clerk. And he has promised, Mrs. Emerson, singlehandedly to make sure our bill gets through the Senate as a stand-alone bill. [Laughter.]

Mrs. EMERSON. And come to the House floor?

Mr. SERRANO. Oh, it will come to the House floor. It will pass. I mean, but then no omnibus bill. You know, there will be a signing ceremony for you and I to attend.

Mrs. EMERSON. And in return?
Mr. SERRANO. In return, I just told a lie. [Laughter.]
Welcome. Welcome aboard.
Mrs. EMERSON. Welcome, Lee.

EFFECT OF COLLECTION ACTIONS ON TAXPAYERS

Mr. SERRANO. Commissioner, the IRS taxpayer advocate, in her most recent annual report, argues that the IRS too often does not consider the impact of its enforcement actions on low income taxpayers. In particular, the taxpayer advocate argues that IRS lien filings are too often counterproductive, damaging the taxpayer's credit score and thus harming their ability to find employment, making them less able to pay their tax debt and future taxes, obviously, if they are not working.

How does the IRS respond to this concern? And, secondly, why does the budget propose a five percent cut in funding for low income taxpayer clinics, which help low-income taxpayers who experience difficulty as a result of an IRS enforcement action?

Mr. SHULMAN. Collection is one of the most difficult things we do because, obviously, Congress expects us to collect the taxes owed. If people are in a collection situation where they have not paid their taxes on time, or they have said they are not going to pay and we need to go find them, it is also where we need to be incredibly sensitive and respect taxpayer rights. We need to make sure that we are not doing anything that overly burdens someone while we are doing collections.

The history of the IRS is collection efforts is something that is expected of us. It is not easy to do. It is one of the toughest jobs at the IRS, but we try to do it with balance.

For low-income taxpayers, I am very focused on going the extra mile, especially in this last year where people were trying to make decisions such as, "Am I going to pay for my medical expense? Am I going to keep my kid in college? Or am I going to pay my taxes?" I mean, Americans were making some unprecedented decisions, given the economic downturn.

COLLECTION FLEXIBILITY

We gave our collectors extra flexibilities. We raised the threshold number where they could make judgments that someone could not pay. We let people skip payments if they previously were compliant taxpayers. We allowed people into offers in compromise programs. If their home equity was the only thing staying in the way, we let people subrogate liens if they were refinancing houses. And so we did a lot of extra special things to try to help people through this difficult time, while collecting the taxes owed.

As to the report that came out from the Taxpayer Advocate, because we are the IRS, we touch every American and it is very healthy for our agency to have lots of people pushing and prodding from different angles.

With respect to liens, one, I will tell you I am looking at that report and assessing what, exactly, we are doing and if we should take any of her recommendations. Two, liens are an authority that Congress gave us, and it protects the American taxpayers' interest.

It protects the public, the FISC, the whole government's interest. We try to use those judiciously.

I am looking at the report. I think lien authority is a tool we are given, we are expected to use it, we need to collect the money that is owed. But we want to do it in a way that gets us the money that the government is owed, but does not hurt taxpayers, if we can help it.

Mr. SERRANO. Do you have a schedule at which time you will say, "We looked at the report, and now we will either take some actions, make some changes based on the report, or ignore it?" And I am not being sarcastic, but, you know——

Mr. SHULMAN. Yes.

Mr. SERRANO [continuing]. A point where this Committee would know what happened to that report in terms of your actions?

COLLECTION PROCESS REVIEW

Mr. SHULMAN. Yes. I am a big fan of continuous improvement, and I challenged our leadership to not get complacent and to keep looking freshly at things and seeing how the program evolves. I have asked our new Deputy Commissioner for Services and Enforcement to do a thorough review of collection, taking input from Congress over the last several years, taking input from the GAO, taking input from the Taxpayer Advocate's report.

And so they have started taking a broad look at collection, and this is part of the mix. That review is going to be done in this fiscal year, and then we will see how to evolve the program.

OFFSHORE INITIATIVE

Mr. SERRANO. Okay. One further question here. Last year the President requested, and the Congress provided, funding to enhance the work of IRS enforcement aimed at the offshore tax evasion schemes. What can you tell us about the progress the IRS is making in hiring the additional personnel to address this issue?

Mr. SHULMAN. Last year the President gave us 800 new people for international enforcement. This year for FY11, he has requested funding again. We are well on track to hit those goals. This area is a priority of mine, it is a priority of the President, it is a priority of the Treasury Secretary, and so we are going to keep focusing on that.

Some of that money is going towards agents who are pursuing individuals hiding assets offshore. Some of that money is going to make sure that we have specialists who can identify corporations when they do things like transfer pricing, transfer of intangibles, financial products. We have economists, financial specialists, lawyers, who we can match up with business, which is getting more and more global.

On the international individual noncompliance we have made much more progress. I am very pleased with our progress there. We have gone much further than I think our team would have imagined a year and a half ago when we started down this path. We had a ground-breaking deal with UBS, in which the Swiss government made some agreements with us that they had not made in the past.

We ran a voluntary compliance program or a voluntary disclosure program, in which we told people the U.S. Government is beefing up enforcement and getting very serious about offshore tax evasion. The risk of being caught has just gone up. We are going to give you a chance to come in, pay your back taxes, pay a severe penalty, but avoid going to jail.

We thought maybe a couple thousand people would come in. We had 15,000 people come in under that program, which (a) is going to bring us a lot of money, but (b) means these 15,000 people are going to be tax-paying Americans for the next 10, 15, 20 years. The money is brought back. They are paying taxes now.

Also I have become Chairman of the Federation of Tax Administrators, which is the global forum on tax administrators. And we are stepping up our international cooperative efforts, and we are making great strides.

I think the next big thing that needs to happen, and that we hope happens, is Chairman Rangel and Chairman Baucus both put forward this Foreign Account Tax Compliance Act. It is in a number of things, including a jobs bill that is moving around now in the Senate. We are quite hopeful that passes, because it is going to give us a bunch more tools to continue on this effort.

Mr. SERRANO. Okay. Just one quick question. You know, we who serve in this House I find at times will use words or phrases, and we do not stop to say, "Do I really know what I am saying?" Not that we do not know what we are saying, but rather what does a term mean?

So we talk about offshore all the time. Can you very briefly tell us, what does that really mean? Is it people putting money in savings accounts? Is it people hiding money somewhere? Where do most of these accounts or these hiding places exist? What countries? And how does the scheme or the plan work?

For instance, if I take what little savings I have and put it somewhere else, I already paid taxes on it. It was taken out every month. Downstairs they take the taxes out. So how would I then be hiding that?

OFFSHORE INITIATIVE

Mr. SHULMAN. I think, generally, when people talk about offshore tax evasion by individuals they are talking about wealthy individuals who put money in a bank secrecy jurisdiction and keep it over there. So as they get dividends, they get interest, they get capital gains when they sell it, they are not paying their taxes on it.

Sometimes it is illegal source activity. So someone got money illegally, did not pay any taxes on it, and parks it offshore, so it is the double-compounded issue.

And regarding where it is and how the schemes work there was a well-publicized scheme last year where people from another country were sending bankers over here with encrypted laptops and secret words and hiding their travel records and going to a variety of locations around the U.S. selling to people. They were saying, "You are going to get a better return on your investment because you are not going to have to pay your taxes." And so that happens.

There are also promoters in foreign jurisdictions who work with intermediaries, whether it be disreputable accounting firms or law firms or others who are trafficking in setting up sham trusts. So you really control the trust, but you go down to the Cayman Islands or someplace and set up the XYZ Corporation, and all the monies flow to that. It is going to appear like a corporation, but it is really for your benefit. So there are a variety of schemes that are out there.

Regarding where this happens, our voluntary disclosure program had accounts flowing in from every continent, except for Antarctica, and over 60 countries. Anecdotally, one of the great things about this voluntary compliance program, as we are churning through submissions and analyzing and creating databases of these accounts, is we are seeing patterns of intermediaries, patterns of institutions, patterns of countries. There has been a lot of news media, and I am not going to confirm it here, but there has been news media about a lot of movement out of places like Switzerland, and into Asia, Latin America. We have been working with other law enforcement agencies and tracking the flow of money.

And, again, the interesting thing is one of the reasons we are doing so well, I think, is because the U.S. Government is very focused on this effort. It is a priority. All of our people know it is a priority. We are putting our best people on it. We are investing in technology. We are investing in our diplomatic relations around this effort.

But also, the world is changing. Most people in this room have a retirement account or a 401(k). Most of those have some investment in a foreign stock. You can trade a stock electronically while sitting on the beach in Perth, Australia, on the New York Stock Exchange. You used to actually have to, you know, call a broker or call someone on the floor who ran over with a ticket.

Technology is making things move, and countries who want to participate in the global capital markets know that they need to reach certain global capital norms to do so. And so I think both global trends, as well as our efforts, are helping move this in the right direction.

Mr. SERRANO. Great explanation. Thank you. Now we know what we are talking about. [Laughter.]

Mrs. Emerson.

EQUITY SWAPS

Mrs. EMERSON. Speaking of concealment, I have some questions about equity swaps. And perhaps I should define what an equity swap is. According to my notes here, it says financial derivatives that accomplish a number of goals basically by straddling the U.S. border.

Mr. SERRANO. I knew that.

Mrs. EMERSON. Have you made one before?

Mr. SERRANO. No. No.

Mrs. EMERSON. Anyway, so at least this is what we are told. So, number one, they enable a bank to avoid withholding taxes on the payment of a dividend by disguising who owns the stock. They enable an offshore hedge fund to collect a stock's dividend without actually owning the stock. And they enable both parties to somehow avoid paying any taxes on the transaction, which is ordinarily subject to a 30 percent tax.

So, anyway, I wanted to ask the Commissioner about it, because I know that the IRS has been scrutinizing these securities. And so, first, I want to know if you all have reached any conclusions. It just seems to me that it is pretty unfair that the big banks would be allowed to hold assets in offshore accounts with hedge funds for the sole purpose of avoiding taxes.

And I have also read that IRS regulations that govern equity swaps may be at the heart of the matter. So if that is the case, have you all considered changing the regulatory treatment of those equity swaps?

And my last question, or maybe two more, with regard to that is, how successful have you all been at capturing dividend tax revenues at offshore hedge funds that are collected by foreign investors? And what can we do, or are there things that we can do legislatively that would make it easier for you to do your job and close that gap?

Mr. SHULMAN. Let me say a few things about it. A swap is basically a contract where two parties, usually big parties—an institutional investor or a brokerage firm or a bank—enter into a contract that says, you will get this economic benefit based on this, and so it can be any number of things.

I think the issue you are referring to is about publicity around some ongoing investigations about institutions that own a U.S. stock—say IBM, although this is all hypothetical—two weeks before or a week before there is going to be a big dividend, and there would have to be 30 percent withholding in it, they actually change that ownership into a swap contract. It gives them the same kind of economic benefit as if they owned the stock.

And so they go into a swap contract, and they are basically going to get that dividend, but they no longer officially are the owner of record of the stock. And then, there is an agreement around not paying taxes on that or how you allocate those taxes.

We continue to be focused on this issue and we look at that action. And some taxpayers have publicized what we cannot, what we are doing with individual taxpayers.

I think the whole issue around the complexity of financial markets and people using financial instruments, whether you in Congress find the current laws tasteful or not, they are legal. Some things they do are not legal. When they are not legal, we are willing to push it, and we have been pushing it. That is why some of the 800 people who we are hiring are financial specialists and others who can look at these issues.

I will say one more thing about swap contracts. In the old world everybody said, “Okay. You deal with a big counterparty, and you do a swap with them, and it is just like owning the stock.” I think over the last year where some big counterparties failed, people say, “Okay. There is some counterparty risk involved,” and that is the argument on the other side.

When you ask what to do, and you and I talked a little bit about it at other times, is you could potentially do something around swaps, but then you still have equity-linked notes, you still have securities lending, you still have other derivatives. I think there is disparate tax treatment for different financial instruments. And as long as you have an incredibly complex global capital market, and complex tax laws around financial products, you are going to have opportunities for arbitrage.

And our job is to hone in on it, make sure we keep people on the right side of the law, make sure that we are as sophisticated as folks, so if they are doing things legally and structuring it legally, so be it, but, if they are pushing the envelope, we are able to call them on it.

And so this is not an issue that is going away. When people ask me, "what is the focus on large corporate audits?" in a world with this kind of global capital flows, complex financial markets, complex tax laws, we are going to have to keep investing to be able to keep up with people who are looking to make money.

Mrs. EMERSON. And it is very complex, and it seems to get more complex, and the more complex it is the better.

But, anyway, let me ask another couple of question, because I really do not have too many more, Mr. Chairman.

EFFECT OF ECONOMY ON TAX REVENUES

You know, we are all concerned—so very much concerned with the declining economy, and the impact, though, that that has on the amount of incoming revenue collected by all of you. Do you all estimate, talk about—I mean, internally, do you estimate the impact on your revenues by the declining economy? I mean, is that even a measure that you all specifically take other than simply revenues? You know, we have this many—this much less revenue this year? And so I want to know that.

And then, I have to assume that the bad economic state also affects the amount of your enforcement collections.

Mr. SHULMAN. Yes.

Mrs. EMERSON. We talked about that a little bit. Can you all provide estimates of how much revenue has declined in the 2009 tax year? Do you all know that answer?

Mr. SHULMAN. Yes, we do. I am happy to get them to you. Let me answer off the top of my head, and with a big disclaimer for the man typing to my right—and we will get you the exact numbers—tax revenues went down in the 20 percent range. Corporate revenues, though, dropped from $300 billion down to $140 billion because people were experiencing so many losses.

Our actual enforcement dollars dropped, but not as dramatically. And they dropped because people did not have the money. There are lots of ways we measure enforcement, but we have an enforcement revenue number which is literally cash in the door that year, resulting from some sort of action we took, and those dropped. People just did not have the cash.

We also had a lot more people file—a lot of times people file a balance due. So, I owe $3,000 taxes, I file my tax return on time, April 15. I say I owe $3,000, but here is $1,000. We send out a collection notice, and within six months, these are compliant taxpayers, and they send the other $2,000 in and we are done. A lot of those people just did not catch up, and so that decreased the dollars in.

And then we went and examined you and said, "No, you owed money from two years back or three years back." Usually we get checks when we close the exam. This year we had people not able to write checks. And so our enforcement dollars went down less than the overall revenues.

Those revenue projections, though, are in the President's budget, and so we will get you the specific numbers.

Mrs. EMERSON. But you did say corporate revenue decreased, you thought ballpark, $300 billion to $140-?

Mr. SHULMAN. That is the number I have in my head, but let us have the staff follow up and——

Mrs. EMERSON. Okay. Thank you so much.

Mr. SHULMAN. No, no, that is not corporate revenue. That is tax——

Mrs. EMERSON. Tax.

Mr. SHULMAN [continuing]. Revenue coming in. So a difference. That is how much the corporations are paying the government in taxes, not their revenues.

[The information follows:]

Table 2.1—RECEIPTS BY SOURCE: 1934–2015

(in millions of dollars)

Fiscal Year	Individual Income Taxes	Corporation Income Taxes [1]	Social Insurance and Retirement Receipts [2]			Excise Taxes [2]	Other [3]	Total Receipts		
			Total	(On-Budget)	(Off-Budget)			Total	(On-Budget)	(Off-Budget)
1934	420	364	30	(30)	....	1,354	788	2,955	(2,955)	....
1935	527	529	31	(31)	....	1,439	1,084	3,609	(3,609)	....
1936	674	719	52	(52)	....	1,631	847	3,923	(3,923)	....
1937	1,092	1,038	580	(315)	(265)	1,876	801	5,387	(5,122)	(265)
1938	1,286	1,287	1,541	(1,154)	(387)	1,863	773	6,751	(6,364)	(387)
1939	1,029	1,127	1,593	(1,090)	(503)	1,871	675	6,295	(5,792)	(503)
1940	892	1,197	1,785	(1,235)	(550)	1,977	698	6,548	(5,998)	(550)
1941	1,314	2,124	1,940	(1,252)	(688)	2,552	781	8,712	(8,024)	(688)
1942	3,263	4,719	2,452	(1,557)	(896)	3,399	801	14,634	(13,738)	(896)
1943	6,505	9,557	3,044	(1,913)	(1,130)	4,096	800	24,001	(22,871)	(1,130)
1944	19,705	14,838	3,473	(2,181)	(1,292)	4,759	972	43,747	(42,455)	(1,292)
1945	18,372	15,988	3,451	(2,141)	(1,310)	6,265	1,083	45,159	(43,849)	(1,310)
1946	16,098	11,883	3,115	(1,877)	(1,238)	6,998	1,202	39,296	(38,057)	(1,238)
1947	17,935	8,615	3,422	(1,963)	(1,459)	7,211	1,331	38,514	(37,055)	(1,459)
1948	19,315	9,678	3,751	(2,134)	(1,616)	7,356	1,461	41,560	(39,944)	(1,616)
1949	15,552	11,192	3,781	(2,091)	(1,690)	7,502	1,388	39,415	(37,724)	(1,690)
1950	15,755	10,449	4,338	(2,232)	(2,106)	7,550	1,351	39,443	(37,336)	(2,106)
1951	21,616	14,101	5,674	(2,554)	(3,120)	8,648	1,578	51,616	(48,496)	(3,120)
1952	27,934	21,226	6,445	(2,851)	(3,594)	8,852	1,710	66,167	(62,573)	(3,594)
1953	29,816	21,238	6,820	(2,723)	(4,097)	9,877	1,857	69,608	(65,511)	(4,097)
1954	29,542	21,101	7,208	(2,619)	(4,589)	9,945	1,905	69,701	(65,112)	(4,589)
1955	28,747	17,861	7,862	(2,781)	(5,081)	9,131	1,850	65,451	(60,370)	(5,081)
1956	32,188	20,880	9,320	(2,896)	(6,425)	9,929	2,270	74,587	(68,162)	(6,425)
1957	35,620	21,167	9,997	(3,208)	(6,789)	10,534	2,672	79,990	(73,201)	(6,789)
1958	34,724	20,074	11,239	(3,190)	(8,049)	10,638	2,961	79,636	(71,587)	(8,049)
1959	36,719	17,309	11,722	(3,427)	(8,296)	10,578	2,921	79,249	(70,953)	(8,296)
1960	40,715	21,494	14,683	(4,042)	(10,641)	11,676	3,923	92,492	(81,851)	(10,641)
1961	41,338	20,954	16,439	(4,331)	(12,109)	11,860	3,796	94,388	(82,279)	(12,109)
1962	45,571	20,523	17,046	(4,776)	(12,271)	12,534	4,001	99,676	(87,405)	(12,271)
1963	47,588	21,579	19,804	(5,629)	(14,175)	13,194	4,395	106,560	(92,385)	(14,175)
1964	48,697	23,493	21,963	(5,597)	(16,366)	13,731	4,731	112,613	(96,248)	(16,366)
1965	48,792	25,461	22,242	(5,519)	(16,723)	14,570	5,753	116,817	(100,094)	(16,723)
1966	55,446	30,073	25,546	(6,460)	(19,085)	13,062	6,708	130,835	(111,749)	(19,085)
1967	61,526	33,971	32,619	(8,217)	(24,401)	13,719	6,987	148,822	(124,420)	(24,401)
1968	68,726	28,665	33,923	(9,007)	(24,917)	14,079	7,580	152,973	(128,056)	(24,917)
1969	87,249	36,678	39,015	(10,062)	(28,953)	15,222	8,718	186,882	(157,928)	(28,953)
1970	90,412	32,829	44,362	(10,903)	(33,459)	15,705	9,499	192,807	(159,348)	(33,459)
1971	86,230	26,785	47,325	(11,481)	(35,845)	16,614	10,185	187,139	(151,294)	(35,845)
1972	94,737	32,166	52,574	(12,667)	(39,907)	15,477	12,355	207,309	(167,402)	(39,907)
1973	103,246	36,153	63,115	(17,031)	(46,084)	16,260	12,026	230,799	(184,715)	(46,084)
1974	118,952	38,620	75,071	(21,146)	(53,925)	16,844	13,737	263,224	(209,299)	(53,925)
1975	122,386	40,621	84,534	(22,077)	(62,458)	16,551	14,998	279,090	(216,633)	(62,458)
1976	131,603	41,409	90,769	(24,381)	(66,389)	16,963	17,317	298,060	(231,671)	(66,389)
TQ	38,801	8,460	25,219	(7,203)	(18,016)	4,473	4,279	81,232	(63,216)	(18,016)
1977	157,626	54,892	106,485	(29,668)	(76,817)	17,548	19,008	355,559	(278,741)	(76,817)
1978	180,988	59,952	120,967	(35,576)	(85,391)	18,376	19,278	399,561	(314,169)	(85,391)
1979	217,841	65,677	138,939	(40,945)	(97,994)	18,745	22,101	463,302	(365,309)	(97,994)
1980	244,069	64,600	157,803	(44,594)	(113,209)	24,329	26,311	517,112	(403,903)	(113,209)
1981	285,917	61,137	182,720	(52,545)	(130,176)	40,839	28,659	599,272	(469,097)	(130,176)
1982	297,744	49,207	201,498	(58,031)	(143,467)	36,311	33,006	617,766	(474,299)	(143,467)
1983	288,938	37,022	208,994	(61,674)	(147,320)	35,300	30,309	600,562	(453,242)	(147,320)
1984	298,415	56,893	239,376	(73,301)	(166,075)	37,361	34,392	666,438	(500,363)	(166,075)
1985	334,531	61,331	265,163	(78,992)	(186,171)	35,992	37,020	734,037	(547,866)	(186,171)
1986	348,959	63,143	283,901	(83,673)	(200,228)	32,919	40,233	769,155	(568,927)	(200,228)
1987	392,557	83,926	303,318	(89,916)	(213,402)	32,457	42,029	854,288	(640,886)	(213,402)
1988	401,181	94,508	334,335	(92,845)	(241,491)	35,227	43,987	909,238	(667,747)	(241,491)
1989	445,690	103,291	359,416	(95,751)	(263,666)	34,386	48,321	991,105	(727,439)	(263,666)

See footnotes at end of table.

Table 2.1—RECEIPTS BY SOURCE: 1934–2015—Continued

(in millions of dollars)

Fiscal Year	Individual Income Taxes	Corporation Income Taxes [1]	Social Insurance and Retirement Receipts [2]			Excise Taxes [2]	Other [3]	Total Receipts		
			Total	(On-Budget)	(Off-Budget)			Total	(On-Budget)	(Off-Budget)
1990	466,884	93,507	380,047	(98,392)	(281,656)	35,345	56,188	1,031,972	(750,316)	(281,656)
1991	467,827	98,086	396,016	(102,131)	(293,885)	42,402	50,665	1,054,996	(761,111)	(293,885)
1992	475,964	100,270	413,689	(111,263)	(302,426)	45,569	55,731	1,091,223	(788,797)	(302,426)
1993	509,680	117,520	428,300	(116,366)	(311,934)	48,057	50,783	1,154,341	(842,406)	(311,934)
1994	543,055	140,385	461,475	(126,450)	(335,026)	55,225	58,440	1,258,579	(923,554)	(335,026)
1995	590,244	157,004	484,473	(133,394)	(351,079)	57,484	62,596	1,351,801	(1,000,722)	(351,079)
1996	656,417	171,824	509,414	(141,922)	(367,492)	54,014	61,386	1,453,055	(1,085,563)	(367,492)
1997	737,466	182,293	539,371	(147,381)	(391,990)	56,924	63,186	1,579,240	(1,187,250)	(391,990)
1998	828,586	188,677	571,831	(156,032)	(415,799)	57,673	74,966	1,721,733	(1,305,934)	(415,799)
1999	879,480	184,680	611,833	(167,365)	(444,468)	70,414	81,052	1,827,459	(1,382,991)	(444,468)
2000	1,004,462	207,289	652,852	(172,268)	(480,584)	68,865	91,730	2,025,198	(1,544,614)	(480,584)
2001	994,339	151,075	693,967	(186,448)	(507,519)	66,232	85,529	1,991,142	(1,483,623)	(507,519)
2002	858,345	148,044	700,760	(185,439)	(515,321)	66,989	79,011	1,853,149	(1,337,828)	(515,321)
2003	793,699	131,778	712,978	(189,136)	(523,842)	67,524	76,342	1,782,321	(1,258,479)	(523,842)
2004	808,959	189,371	733,407	(198,662)	(534,745)	69,855	78,534	1,880,126	(1,345,381)	(534,745)
2005	927,222	278,282	794,125	(216,649)	(577,476)	73,094	80,902	2,153,625	(1,576,149)	(577,476)
2006	1,043,908	353,915	837,821	(229,439)	(608,382)	73,961	97,271	2,406,876	(1,798,494)	(608,382)
2007	1,163,472	370,243	869,607	(234,518)	(635,089)	65,069	99,610	2,568,001	(1,932,912)	(635,089)
2008	1,145,747	304,346	900,155	(242,109)	(658,046)	67,334	106,417	2,523,999	(1,865,953)	(658,046)
2009	915,308	138,229	890,917	(236,908)	(654,009)	62,483	98,058	2,104,995	(1,450,986)	(654,009)
2010 estimate	935,771	156,741	875,756	(240,573)	(635,183)	73,204	123,647	2,165,119	(1,529,936)	(635,183)
2011 estimate	1,121,296	296,902	935,116	(261,048)	(674,068)	74,288	139,579	2,567,181	(1,893,113)	(674,068)
2012 estimate	1,326,045	366,361	1,004,907	(284,432)	(720,475)	81,085	148,002	2,926,400	(2,205,925)	(720,475)
2013 estimate	1,468,410	393,474	1,070,236	(304,511)	(765,725)	84,994	171,001	3,188,115	(2,422,390)	(765,725)
2014 estimate	1,603,861	444,805	1,132,205	(323,162)	(809,043)	86,503	188,077	3,455,451	(2,646,408)	(809,043)
2015 estimate	1,733,476	411,055	1,194,638	(338,701)	(855,937)	87,829	206,681	3,633,679	(2,777,742)	(855,937)

[1] Beginning in 1987, includes trust fund receipts for the hazardous substance superfund. The trust fund amounts are as follows (in millions of dollars): 1987: 196; 1988: 313; 1989: 292; 1990: 461; 1991: 591; 1992: 380; 1993: 886; 1994: 653; 1995: 612; 1996: 323; 1997: 4; 1998: 79; 1999: 10; 2000: 3. In 1989 and 1990, includes trust fund receipts for the supplementary medical insurance trust fund. The trust fund amounts are (in millions of dollars): 527 in 1989 and –527 in 1990.

[2] See Table 2.4 for additional details.

[3] See Table 2.5 for additional details.

Mrs. EMERSON. So, well, it would be interesting to carry on that discussion further to determine whether or not there are different tax schemes they are using or whether it was just simply a reduction across the board in——

Mr. SHULMAN. There are a lot of people in the loss position last year.

Mrs. EMERSON. Yes.

Mr. SERRANO. Thank you.

Ms. Lee.

AUDITS OF ORGANIZATIONS IN RECEIPT OF BAILOUT FUNDS

Ms. LEE. Thank you very much. Let me just ask you, in terms of a list of all of the banks, financial service companies, and other corporations who have received TARP or TALF funding, and have sold any of the assets of the Treasury programs like commercial paper funding facility or mortgage-backed securities to Fannie Mae or Freddie Mac, let me ask you if you are actually auditing any of those companies.

Do they have any outstanding tax liabilities? They are benefiting from billions of dollars of taxpayer funds, and so how are you all kind of looking at what is taking place within those companies?

Mr. SHULMAN. Without talking about any company specifically, a lot of the very biggest companies in the country are under continuous audit by us, and always have a variety of things in the pipeline that we are auditing, pending appeals of our decisions, things in the Tax Court. And so they have a variety of different books.

I think when I was up here last year there was a number out there about money that TARP recipients had not paid. I actually think that number was a little skewed, because any big company in the country always has a variety of disputes going on, five or six tax years open with us, some things that are in appeals. So that is their right.

We, obviously, are continuing to be part of the whole recovery effort. I would tell you I think we run a pretty fair, even-handed, long-term audit program. And so we are not doing anything special, but we are also not giving anyone any breaks——

Ms. LEE. Okay.

Mr. SHULMAN [continuing]. In that regard.

Ms. LEE. I know you may not be doing anything special, but maybe you should. I mean, these are low interest loans that these companies have received. This is a special effort, and I would think that if these companies—or at least you would want to know if they have any outstanding tax liabilities or would consider doing some special audits, because it is a special, you know, type of initiative. But you are not.

Mr. SHULMAN. We will definitely take that under consideration.

Ms. LEE. Yes. I think it would be, Mr. Chairman, very prudent to do that. I think taxpayers——

Mr. SERRANO. Well taken.

Ms. LEE [continuing]. Are angry enough about what has taken place, and I think any way to ensure transparency, to ensure that their tax dollars are being spent appropriately as it relates to TARP and TALF, I think that would be very helpful.

Thank you.

Mr. SERRANO. Thank you.

I have a set of questions that I will submit for the record. Any other member also that has——

Mrs. EMERSON. I have some for the record, yes.

TAXES ON FOREIGN NATIONALS

Mr. SERRANO. I just have one more question to ask, Commissioner, but I have a fun question ahead of that, because, you know, it is about 39 days before the baseball season starts.

Mrs. EMERSON. Oh, I was waiting for this.

Mr. SERRANO. Right?

Mr. SHULMAN. We are all looking forward to this, Mr. Chairman.

Mr. SERRANO. So if you are here on a work visa from another country playing baseball, as so many are now, I know you pay your federal taxes for working here, for any money earned here. My understanding also is that you file state taxes for every state that your team visits during the season. So you have your home state, and then, you know, California, Georgia, whatever, those states.

Now, the folks who still have their legal address, if you will, back home—Dominican Republic, Venezuela, China, Japan, wherever the countries are—Mariano Rivera, Panama—some of those folks who maintain those addresses, legal residents, still pay taxes there.

Now, I know there are deals—there are arrangements made between state taxes and federal taxes where sometimes you get credit for that, that does not go on, does it? I mean, we do not give these millionaires a break on their federal taxes here because they are paying taxes somewhere else?

Mr. SHULMAN. Before I answer, can I clarify, is this the Red Sox or the Yankees you are referring to? [Laughter.]

Mr. SERRANO. When it comes to the money they make, it is any——

[Laughter.]

The fact that the Yankees have had a cost-effective and——

[Laughter.]

Mrs. EMERSON. Excuse me? They have——

Mr. SERRANO. And actually do something with the money they pay——

Mrs. EMERSON. Like build $2 billion stadiums?

Mr. SHULMAN. You know, I believe the——

Mr. SERRANO. By the way, you know that I passed a resolution in the House congratulating the Yankees for the World Series. Let me tell you what we have. Resolutions like that pass 400 to zero. No. There are people who abstained, people who voted no. Mostly it is from Massachusetts and Pennsylvania, but——

Mrs. EMERSON. The Cardinals fans, we would get in trouble if we voted for the Yankees.

Mr. SERRANO. See what I mean? Go ahead.

Mr. SHULMAN. I think the law, generally, is in the U.S. you pay taxes where you make the money, and it follows folks. I think if you fly over New York air space and you live in another state, but you are going there for work, you, in theory owe taxes. And so I think that is how it works, and we try to just apply the law——

Mr. SERRANO. Right.

Mr. SHULMAN [continuing]. As it stands.

Mr. SERRANO. But to your knowledge there are no arrangements with other countries. In other words, just because they pay taxes there, but they work here, there is no——

Mr. SHULMAN. Not to my knowledge.

Mr. SERRANO [continuing]. Not given a break.

TAX ON FOREIGN NATIONALS

Mr. SHULMAN. I mean, we have treaties. We have treaties with a variety of countries a lot of times in the corporate or individual setting where if someone pays taxes—the basic theory of treaties is around double taxation, which is you should only pay tax once. And so they may actually, when they pay here, not have to pay it on their income there, so they are paying on their taxes once. But, you know, our general rule is if you make it here, you pay taxes here.

Mr. SERRANO. Yes. I would be concerned if it is the other way, that we would not tax them because they are paying taxes somewhere else.

Mrs. EMERSON. But if, in fact, you have let us just say a German guy who worked for a woman who works for a German company, and their residence is there but they spent more than 50 percent of their time here, and they work here and get paid here, I mean, there is the credit. I mean, that is what happened when I used to work abroad and live here at the same time. I paid taxes where I lived and then got a credit and then paid the difference if it was less I think——

Mr. SERRANO. Yes, but you were not making $25 million a year.

Mrs. EMERSON. I was not even making $25,000 a year. [Laughter.]

Mr. SERRANO. There you go.

Mrs. EMERSON. But I still was complying with—I mean, the law was the law I guess is what I am trying to say.

Mr. SERRANO. I better end this, because I suspect that after a very good hearing this may be the story in tomorrow's papers about baseball players. And I do not want to do that to this hearing, you know?

ELIMINATION OF AUTOMATIC MAILINGS

But I have one last question. It seems—well, the budget request assumes a savings of several million dollars by eliminating the automatic mailing of Form 1040 booklets. That is that thick, soft booklet that we all expect in the mail, and we cheer when we get it, or we cry, but there it is.

So here is the question. Will you really save money? Will people now for the first time, in as long as I can remember not seeing that booklet, decide something is not happening? You may even get calls asking you, "Does that mean I do not have to pay taxes this year?" So the cost of those calls, the cost of the time you will be dealing with that, does that really offset the savings for not mailing the book out? And how much confusion?

I mean, I know it sounds silly, but there are people who actually wait for that booklet to come, and then they open it up the middle, they rip out the——

Mrs. EMERSON. They are so excited.

Mr. SERRANO [continuing]. They rip out the form, right?

Mr. SHULMAN. Yes.

Mr. SERRANO. That is the form they fill out. Now some folks must be going to go to your offices to look for forms. So was that truly a cost-saving move?

Mr. SHULMAN. That is a great question. The President challenged all of us to say, "Look, we will make prudent investments where needed," and I am very pleased that he decided to make an investment in the IRS. But he said, "I want you to challenge yourselves and see where you can have efficiency savings."

This is one we debated. There is the issue of compliance, and it is unknown whether getting that book actually increases compliance. With that said, 60 percent of the people are using preparers; they do not need to get a book. Twenty percent are using software; they do not need to get a book. We only send the books now to people who filed on paper, and the paper filing decreased. The e-filing went up over 10 percent last year. It went up to 66 percent, and so we made this prudent choice.

I will tell you there is a general target to decrease mailings, and the 1040 is an example. I have challenged our staff around inserts, can we decrease inserts, can we decrease all mailings? And so if this budget gets approved, we will make decisions about exactly what we do mail and do not. But we are committed to $20 million in mailing savings. That is really what the budget means.

Mr. SERRANO. Do you realize you are helping to kill another one of your accounts that we oversee, the Postal Service?

Mr. SHULMAN. So be it. [Laughter.]

Mrs. EMERSON. Well, they could send out "save the date to file your tax" cards. That is expensive to print.

Mr. SHULMAN. I know, I know.

Mr. SERRANO. So you think in the long run the push is to do as little mailing as possible.

Mr. SHULMAN. It is kind of like I talked about with Mr. Crenshaw. You have got to move an agency forward. You have got to make the best decisions you can with the information you have. We think this is a prudent move. If we find out it is a big problem, we will deal with that and correct ourselves. But we are going to try cutting down some mailings.

ELIMINATION OF AUTOMATIC MAILINGS

Mr. SERRANO. In closing, you are not going to believe this. This falls under the category of "You Are Not Going to Believe This." Someone on the street came up to me—as you know I have a walking district in the Bronx, and I walk around all the time—and this person said, "And I understand, because there are no secrets, that the IRS is not going to send that book out anymore." I said, "That is what we hear." He says, "You have got to get me one, because I collect them."

Mr. SHULMAN. I will get him an autographed copy. [Laughter.]

Mr. SERRANO. Absolutely. It will be sold on eBay.

I have no further questions. Do you?

Mrs. EMERSON. I only have questions to submit for the record, Mr. Chairman.

Mr. SERRANO. All right. So will I.

I want to thank you. We want to thank you for your testimony today. We repeat our desire to stand ready not only on our budget issues, but also to stand ready to assist you in any way during this very difficult time. And please, once again, convey to the staff and to the folks at IRS this Committee's concern and heartfelt condolences for your tragedy. And we thank you for your testimony today.

Mr. SHULMAN. Thank you.

SUBCOMMITTEE ON FINANCIAL SERVICES AND GENERAL GOVERNMENT

HEARING

ON

THE FY 2011 BUDGET REQUEST OF THE INTERNAL REVENUE SERVICE

Questions for the Record

for

The Internal Revenue Service

February 24, 2010

Questions for the Record
Submitted by Chairman Serrano

1. I appreciate the efforts the IRS has made in recent years in publicizing the Earned Income Tax Credit for eligible taxpayers who need it but may not be aware they qualify for it. But even with these efforts, there are still millions of households who qualify for the EITC but do not claim it. What more can be done, both by the IRS and others, to ensure that all taxpayers who qualify for the EITC are in fact claiming it and receiving it?

Response: With over 24 million taxpayers claiming EITC, participation is relatively high compared to other benefits programs. Current estimates of the participation rate are between 75 to 80%, indicating our current outreach approach is working. We have an aggressive marketing and outreach strategy to encourage every eligible taxpayer to claim the EITC. This strategy includes efforts to reach the hardest to reach taxpayers who traditionally are the least likely to claim the credit. Our strategy incorporates integrated direct marketing and public service campaigns using traditional media, as well as new emerging social media channels.

We spearhead national outreach initiatives such as EITC Awareness Day. The goal of this day is to saturate the country with local and national media events to obtain maximum reach. Our model is to partner with over 300 community-based organizations, as well as congressional, state and local governments on EITC awareness and eligibility, as well as to promote and provide free tax help to EITC eligible taxpayers.

We provide online EITC information, best practices and tools for taxpayers, partners, and preparers to clarify eligibility requirements and to promote EITC awareness.

Finally, we review all returns for potential EITC eligibility, and for those who appear to be eligible, we send a notice to encourage them to check their eligibility and if qualified, to claim the credit. We send about 600,000 notices annually. We also partner with the states to further increase participation. We initiated a pilot program to reach out to eligible taxpayers with a second notice from state taxing agencies. This year we will expand the pilot program with the addition of California, and we will enhance the process with the support of several academics.

Although we have been effective with EITC outreach, we can make improvements. We will continue to use research on non-claimants to refine our targeted audiences and understand reasons for non-participation. We also will continue to engage our partners and expand our network to promote EITC awareness and eligibility. Finally, we will look to improve and market our current services to make filing and claiming the credit as easy as possible.

2. With respect to the recent attack on the Austin facility, I have three concerns. First, what is the IRS currently doing to assist the affected employees and their families, including the families of those who have been injured or killed?

Second, do you feel that the IRS is doing its utmost to ensure the safety of its employees? And lastly, what is the impact on IRS operations?

Response: When an emergency places IRS employees, facilities, and/or operations at risk, the first and foremost consideration is the safety of our employees. Within minutes of the incident in Austin, we activated an interim Emergency Operations Center (EOC) in Dallas, serving as a focal point for communication and information until the Senior Commissioner Representative serving as the Incident Commander could reach Austin. By the evening the incident occurred, the Austin EOC was up and operational, managing the incident which includes addressing employee issues and conducting activities to resume business operations. The Austin EOC arranged for specialists in various Human and Employee Relations fields to be on-site. These specialists were on-site for three weeks and are continuing to provide support and assistance to affected employees.

The Treasury Secretary and IRS Commissioner met with employees on February 22, 2010, offering their support. In addition, they met privately with the decedent's spouse, who also was one of the IRS employees in the building at the time of the incident. The Commissioner spoke at the deceased employee's funeral. The immediate Group Manager of the decedent's spouse was in close contact with her for several days after the event providing support. The Territory Manager also played a significant role by serving as a focal person with IRS contacts for the decedent's spouse. Senior Leadership from the various Business Operating Divisions (BODs) met with their respective employees offering support and assistance. These efforts have continued to ensure we are meeting employee needs.

On February 22, 2010, we set up a "One Stop Shop" at the Austin EOC to provide the employees with a single point of contact to ask and receive answers to specific questions. The "One Stop Shop" was available to employees for three weeks. Various service providers such as the IRS Benefits and Services Team (BeST), the Employee Assistance Program (EAP), and the IRS Worker's Compensation Center were on-site to talk with employees and provide individual assistance. The EAP personnel provided immediate on-site individual and group counseling services to affected employees. The employees and families have access to and were encouraged to seek individual counseling beyond what is normally provided through the EAP. The IRS expanded the number of individual counseling sessions for affected employees. In addition to the individual and/or group EAP counseling services, we provided employees packets and information to address various potential issues, including the following:

- the FBI's Victim's Assistance Program and the American Red Cross contact information;
- the IRS Worker's Compensation Center benefits counseling information and application forms for those considering filing a Workers' Compensation claim;
- the IRS Benefits and Services Team (BeST) information;
- the Social Security Administration (SSA) contact information for those who lost their SSA cards;
- the Texas Department of Public Safety contact numbers for those who lost their drivers license;
- information on how to file a claim for those individuals whose personal items were destroyed, and;

- assistance in obtaining, without charge, replacement of professional certificates and other documents, e.g. Certified Public Accountant certificates.

In addition to the services previously described, the IRS Workers' Compensation Center and the IRS BeST areas provided the decedent's wife a private survivor benefits session, which included all options available to her. This benefit package included expedited processing of life insurance payment through the Office of Personnel Management. These IRS offices continue to provide ongoing assistance and support to the decedent's wife with benefits and compensation issues.

The IRS continues to manage and implement security services and program components that are aimed at protecting IRS employees, facilities, systems, and data. The IRS provides enterprise-wide physical security and emergency preparedness program and operations support for the protection of IRS assets.

The IRS conducts facility reviews to identify risk vulnerabilities and deployment of mitigation strategies to reduce and/or eliminate threats. As mandated by the Homeland Security Presidential Directive 12, the IRS continues to enroll and issue the new SmartID card, which is based on sound criteria for verifying an individual employee or contractor's identity to secure against unauthorized access. The IRS develops, facilitates, and evaluates existing security measures through tests and exercises to ensure that employees are prepared to respond to, and recover from, incidents.

Subsequent to the Austin incident, the IRS temporarily elevated the level of protection through armed guards posted at all Taxpayer Assistance Centers to increase visibility for employees, visitors and taxpayers. The IRS continues to partner with federal, state and local agencies, public and private sector entities, and other law enforcement organizations to exchange information and monitor threats.

Regarding the effect to IRS operations, each affected IRS Business Operating Division implemented their Business Continuity Plan at the time of the event. These plans address how the IRS resumes critical business processes when interrupted.

One affected area of IRS operations is the potential damage and/or destruction of records. Currently, the IRS is undergoing the retrieval, restoration, and salvage process, including retrieving computers from the site and efforts to secure information from the hard drives of those systems. Since information is accessible via the various IRS electronic systems, there was little workload interruption. The affected IRS functions have taken steps to access their case activity based on status from the time of the incident. They will follow through on the appropriate course of action, which in some cases is contingent upon the retrieval or rebuilding of case files.

On March 8, 2010, employees returned to work in alternate locations (the Austin Campus and the Pickle Federal Building) until the identified replacement space can be occupied, which is targeted for June 2010.

3. Regarding the August 2009 agreement between the Swiss Government and the IRS and Department of Justice, and the related Voluntary Disclosure Program

instituted by the IRS, what is the IRS's evaluation of the performance of the Voluntary Disclosure Program, and what are the lessons learned? In addition to resources, what else does the IRS need to ensure the success of the international tax enforcement initiative?

Response: We will not be able to evaluate fully the performance of the program until we have completed processing all of the voluntary disclosure cases. Our preliminary assessment, however, is that the program will prove to have been very successful in bringing a large number of individual U.S. taxpayers back into compliance with respect to their offshore holdings and income, and in collecting a substantial amount of previously unreported taxes, plus interest and penalties, with respect to the years covered by the program. This program should have a significant effect on increased compliance by these individuals for many years to come. We also expect the significant amounts of account and other information obtained in this process will help us identify banks, attorneys, accountants, financial advisors, and others who promoted or otherwise assisted U.S. taxpayers in hiding income and assets offshore.

At this point, the most significant difficulty we have experienced in processing these cases is obtaining and verifying the substantial amount of information required to be provided so we can confirm the accuracy of the income amounts reported by the taxpayer and calculate the appropriate tax, interest and penalties. Much of this information, e.g. the highest account balance during this period, was not readily accessible to many taxpayers, either because they did not have it in their possession or it was difficult to locate. In many cases, it took taxpayers several months to obtain this information from their banks. In this regard, we could have done a better job of informing the program applicants earlier in the process about all of the types of information they would have to provide so that we could develop and close their cases more quickly.

Other than our primary need for additional resources provided in the President's Budget, the recently passed HIRE Act will also be a great help to international tax enforcement. In addition, a variety of legislative proposals have been made within recent months, many of which would provide assistance in our efforts to enforce our international tax rules.

4. The Taxpayer Advocate's 2009 report highlighted the need for the IRS to develop an overall strategy to address issues of low-income taxpayer services and compliance. As you know, low-income taxpayers frequently face concerns that differ greatly from the rest of the taxpayer population. Among the recommendations in the report is a needs assessment of low-income taxpayers that goes beyond the EITC. Does the IRS agree with the Taxpayer Advocate's assessment, and has the IRS taken steps to address these issues?

Response: Continuing IRS efforts to understand the general taxpaying population do much to help understand that group defined by the National Taxpayer Advocate as low-income. In fact, the IRS already enjoys the benefits of substantial amounts of research covering these taxpayers, much of which goes beyond the EITC-eligible taxpayer population.

For example, the IRS has specific programs in place, wholly detached from EITC, that help explore and meet the needs of low-income taxpayers. Each year, Wage & Investment Research conducts an "environmental scan" describing trends in the W&I taxpayer population. This research includes emphasis on underserved groups, including taxpayers with low English proficiency, elderly taxpayers, taxpayers with disabilities, and other undeserved or low income taxpayers. This research brings knowledge about these taxpayers into the planning and delivery of IRS services specifically designed to meet their needs.

In addition, to help the IRS better serve more vulnerable low-income taxpayers we maintain an Outreach Initiatives Database. This helps the IRS leverage the services of national and local community groups and partners to provide service to populations that may be difficult for the IRS to reach through more direct means. Examples of the topics included in these outreach initiatives include: First Time Homebuyer Credit, Effects of Economic Hardship, Recruiting & Hiring, New Schedule C Initiative, Education Tax Credits, and the Making Work Pay Credit.

5. Both the IRS Taxpayer Advocate and a recent Washington Post article have highlighted the problem of too many taxpayers being unable to get through to the IRS over the phone in a timely manner. The fiscal year 2011 budget request addresses this, but the level of service on the IRS phone lines would improve only slightly. The IRS telephone hotline is important for families who don't have internet access, and 40 percent of all families earning less than $100,000 do not have internet access at home. Does the IRS believe that it needs an additional approach, and not just more resources, to improve its telephone hotline service, and does the IRS have a long-term plan for ensuring that taxpayers without internet access can reach the IRS over the phone in a timely manner?

Response: The IRS is dedicated to providing the best possible service regardless of the channel the customer chooses, be it telephone, internet, correspondence or face-to-face. Specifically regarding telephone service, in addition to requesting additional resources, the IRS is using several approaches to improve service. For example, we are providing an Estimated Wait Time (EWT) tool to customers so that they can make an informed decision about whether they want to wait or call back later. On most days, taxpayers who choose to wait are able to get to an assistor after a short time. We are also improving or designing new automated self-service tools, such as "Where's my Refund," that provide answers for less complex questions and free our assistors to handle more difficult issues that require personal interaction with the customer. We are segmenting the workload differently to improve our efficiency and enable us to answer more calls. And finally, we are increasing the total number of employees available to better address peak workload periods.

These and other initiatives, coupled with the additional resources requested in our budget submissions, will allow us to incrementally improve telephone service over the next few years.

6. The IRS has requested an increase for the Business Systems Modernization program, to complete the modernized taxpayer database. What kind of benefit will the taxpayer see when this database is completed, and how confident is the IRS that the modernized database will be ready in time for the 2012 tax filing season?

Response: Completion of IRS's CADE 2 relational taxpayer account database is fundamental to significant transformation opportunities, allowing the IRS to expand its online services and develop sophisticated next generation service and compliance systems. The new database will serve as the central repository of tax account information for all individual taxpayers and it will operate in a daily processing environment. This upgrade will result in improved taxpayer service through faster disbursement of refunds, increased timeliness and accuracy of taxpayer transactions, and faster resolution of taxpayer issues. With the use of business intelligence tools to access an analytical data store, there will be additional opportunities for improvements in compliance, which will benefit the taxpayer as the IRS is better able to apply the tax law with integrity and fairness to all. Such opportunities include better case selection, enhanced fraud detection for all individual taxpayer accounts, increased speed and accuracy in identifying preparer non-compliance, and expanded data analytics. There will also be increased capacity to leverage expanded data collected from information returns to increase the effectiveness of compliance efforts altogether. In addition, we will begin to address our custodial accounting material weakness and other long-standing significant deficiencies that exist in our core taxpayer account processing that will likely result in some compliance benefits early on and will position us to address full Federal Financial Management System Requirements (FFMSR) compliance for core taxpayer account processing by 2014. Finally, the modernized environment will improve the security posture of the data and improve the efficiency of IT operations by faster integration into a single tax processing environment.

There is very high confidence that we will deliver the CADE 2 modernized database (Transition State 1) according to plan in time for the 2012 tax filing season. There is a comprehensive governance process that gives accountability to some of the highest level executives in the IRS for oversight of the CADE 2 program. In addition, CADE 2 integrated development efforts are managed by a Program Management Office that is led by a mix of executives who have industry best practice experience in leading large systems development programs such as CADE 2, as well as Government executives who are very familiar with the IRS's current IT and business environments. The CADE 2 program will follow a structured method to plan, execute and monitor the success of this information technology program through a Program Framework for Enterprise Life Cycle (ELC). This program framework will better clarify phases, activities, milestones and review points needed to establish and operate a program of this magnitude. This Program Framework for ELC enhances IRS's existing project ELC with additional guidance for programs that have unique needs for planning, management and operation vs. those of stand-alone projects. And, finally, a formal risk management process is in place to support regular identification of risks and issues, development of mitigation strategies, monitoring through formal risk reviews, and dashboard reporting for governance and oversight at all levels of the program.

7. With regard to the $25 million in the budget request for improvements to the IRS web site, what kinds of improvements can taxpayers expect to see? Does the IRS expect that this will result in efficiency savings elsewhere in the IRS?

Response: This initiative will leverage a new IRS Web environment to improve and expand self-service options, reduce taxpayer burden, increase compliance, reduce costs on other communication channels, and continue to position IRS.gov as the preferred choice for taxpayer service. We expect the initiative to improve taxpayer satisfaction with IRS.gov, including navigation, content quality, and ability to locate desired information.

By leveraging the new Web environment, the IRS will ensure the IRS.gov design can adapt to meet taxpayer user experience expectations based on their online interactions with other financial services Web sites. This redesign effort will allow the IRS.gov environment to grow to accommodate evolving taxpayer needs for tax-related information and online tools or services from the IRS.

This initiative also will allow the IRS to begin the second phase of migration by incrementally building out the new consolidated Web environment for hosting secure public/partner-facing applications that are currently hosted on the existing Registered User Portal (RUP) environment and transitioning approximately 35 percent of the current RUP applications to the new environment. This new environment will replace infrastructure that has reached its end-of-life or end-of-support period.

This second phase will improve the response time and stability of applications transferred and that are used by taxpayers such as:

- Where's My Refund – Enables authorized users to look up the status of refunds reported on their (or their client's) tax return
- Online EIN Application – Enables users to apply online for a new Employer Identification Number and in most cases receive the new number immediately
- Online Payment Agreement – Allows qualified users to apply online for a payment agreement that facilitates installment payments if they cannot pay the entire amount of taxes owed

Completion of the migration of the entire RUP to the new environment (FY2011-FY2013) will result in additional capacity to more efficiently deliver new online tools and services to taxpayers and tax-preparers in subsequent years.

8. The budget request includes language allowing up to $6 million to be transferred from the Taxpayer Services account to the Health Insurance Tax Credit Administration account upon advance notification to the Appropriations Committees. How could the IRS avoid placing a negative impact on tax return processing or taxpayer service if funding is transferred from the Taxpayer Services account to the Health Insurance Tax Credit Administration account? What is the likelihood that funding would need to be transferred? Why aren't these funds simply included in the budget request for the Health Insurance Tax

Credit Administration account? Should it appear that these additional funds are necessary, would the IRS consider making a supplemental appropriations request instead?

Response: If a transfer to Health Insurance Tax Credit Administration (HITCA) account were deemed necessary, the IRS would continue to provide the highest level of customer satisfaction and telephone level of service possible.

The Health Coverage Tax Credit (HCTC) program is required to support the more than 1 million potentially HCTC-eligible taxpayers to gain access to the program as provided by ARRA and to ensure approximately 56,000 HCTC-enrolled taxpayers maintain health insurance. Beginning in FY 2011, taxpayer participation in the HCTC program is expected to grow 400 percent because of the American Recovery and Reinvestment Act (ARRA).

Although not a certainty, additional staff and contractor support may be required to allow HCTC to serve a significantly larger participant population and potentially eligible taxpayers.

In its FY 2011 Budget request, the requested $3.5 million resource adjustment for HCTC represents a balance of HCTC Program needs and the IRS need to maintain and improve other taxpayer service and enforcement priorities.

In the event of a shortfall in the HITCA administration account, the IRS would not transfer funding from the Taxpayer Services account without exploring all alternative means of maintaining HCTC service.

9. Is the IRS confident that the level of decline in paper tax returns and the increase in e-filing are consistent with the IRS submission processing center consolidation effort in Atlanta? Is there a risk that the IRS will not be able to realize all of its projected $22.8 million in efficiency savings from increased e-filing? Is there a risk that the Atlanta site is being closed too early, and that the remaining submission processing sites will be receiving an unanticipated excess of paper returns and incurring additional submission processing costs once the Atlanta site closes? Please explain the research methodology under which the IRS projects the increase in e-filing such that the Atlanta submission processing site will soon no longer be needed.

Response: The IRS has gained efficiency from increases in electronically filed (e-filed) returns and decreases in the more labor-intensive paper-filed returns. The number of individual e-filed returns has grown from 4 million in 1990 to an estimated 97.4 million in 2010, reducing the need to process paper returns. Approximately 70% of individual returns are currently e-filed, and with the recently passed practitioner mandate, that figure is expected to substantially increase beginning in 2011.

In 2002, the IRS implemented the Submission Processing (SP) site consolidation strategy for changing future paper processing workforce needs. Consolidation and centralization of paper processing from ten IRS campuses to five and, eventually, three is a key element in our overall strategy to streamline the IRS, improve efficiency and customer satisfaction and, significantly, to achieve maximum savings through rent and salary reductions.

Since implementing the Submission Processing site consolidation strategy, the IRS has conducted multiple analyses to regularly validate our ability to deliver successful filing seasons within the smaller projected footprint for paper return processing. For example, we conduct a yearly state mapping exercise to realign workload based on projected return volumes and capacities at the processing sites, computing centers, and lockbox banks. We have further validated our planned order of consolidations based on comparative costs using productivity, real estate, and strategic human resource data.

Significant capital investments have been made to ensure that the three designated end-state sites for individual returns processing in Fresno, Kansas City and Austin, are prepared to handle the workload. In 2008, when the Economic Stimulus legislation resulted in 8.6 million more paper returns than originally projected, Fresno, Kansas City, and Austin responded by processing 18.4M, 16.3M, and 9.6M returns, respectively, for a total of 44.3 million. In 2012, when the end state design for Submission Processing is fully implemented and the e-file mandate is in effect, approximately 24 million paper returns are projected to be received, or roughly 20 million fewer returns than Fresno, Kansas City and Austin collectively processed in 2008. Based on the latest projections for individual paper returns and our ongoing analyses, we are confident that paper returns processing can be accomplished efficiently by closing Atlanta in 2011 and reaching the end-state configuration of three individual processing sites in 2012. Through these thoroughly planned and fiscally prudent paper processing consolidation efforts, we believe the projected $22.8 million in efficiency savings will be realized.

10. With regard to the $75,000,000 in assumed savings associated with improving information technology infrastructure and process improvements, please explain in more detail how the IRS believes these savings will be achieved. Is there any risk that the IRS will be unable to achieve the full $75,000,000 in savings?

Response: The IRS has already made plans to achieve the full $75,000,000 in savings by the completion of FY 2011. The IRS expects to achieve $75,000,000 in savings through improvements in information technology infrastructure and process improvements that have decreased contractual services spending. Additionally, the IRS will utilize ongoing vendor contract management practices, which have yielded approximately $20,000,000 in FY 2010 savings to date. These practices are expected to produce more savings throughout FY 2011.

11. Does the funding for the new enforcement initiatives assume that the new staffing will be onboard on October 1, 2010? In the case of a delay in enactment of the appropriations bill, would it become difficult for the IRS to spend, prior to the end of fiscal year 2011, all of the fiscal year 2011 funding for new enforcement initiatives?

Response: Yes, the FY 2011 request assumes that the new staffing is on board on October 1, 2010. In the case of a delay, the IRS nevertheless would be able to spend all fiscal year funding for new enforcement initiatives. As an example, in FY 2009, although the budget was not passed until March 2009, the IRS obligated 99.7 percent of its FY 2009 Enforcement funds, including hiring the additional employees funded by the substantial investment in new enforcement initiatives.

12. The IRS budget justification notes that one of the key objectives for the IRS in fiscal year 2011 is to "design new processes to simplify the hiring experience." What is the IRS planning in this regard, and does the IRS expect to gain efficiencies and reduce costs associated with recruiting and hiring new employees?

Response: The IRS continues to take steps to simplify the hiring experience. Our plan is to expand the use of our current automated applicant management system, which is fully integrated with the Office of Personnel Management's USAJOBS, to be used for both internal and external hiring. Additional tools are in development to quickly assess, evaluate, and refer applicants with the competencies necessary for successful performance in the job. Full implementation of this system will provide for a totally automated application process, eliminate the processing of paper, streamline the applicant screening process, automate the ranking and selection processes, and provide ongoing communications with viable candidates throughout the hiring process.

While the IRS will continue to use traditional outreach methods, we will also expand the use of various media tools such as Facebook, Twitter, LinkedIn, FedSoup and GovLoop allowing us to reach a larger pool of job seekers and maintain relationships with them at a minimal cost. We recently developed standardized recruitment marketing materials that target a diverse pool of applicants (to include entry level and midcareer audiences as well as individuals with disabilities, students and veterans) and promote a common IRS employer brand. With the initial materials being printed, future cost savings will be realized by eliminating the need for individual business areas to develop their own separate materials.

These initiatives are expected to result in both cost and time savings by standardizing hiring practices across employment offices; eliminating the manual qualification and ranking of applicants; eliminating the copying and mailing of packages between employment offices and selecting managers; and eliminating the mailing of hard copy letters to the majority of job applicants.

13. The budget request includes $5,500,000 to maintain staffing associated with implementing the Recovery Act. Does the IRS intend this funding to be a permanent addition to the funding base?

Response: The $5.5 million is comprised of $5.1 million in funds that represent a permanent addition to the funding base, and $.4 million in funding that will non-recur in FY 2012.

14. Why does the requested increase for Business Systems Modernization include a corresponding increase of $45,463,000 in the Operations Support account? What costs will be covered with these Operations Support funds?

Response: Of the $45.5 million, $42 million in the FY 2011 budget is to pay for the necessary support of previously deployed Business Systems Modernization systems that are in the Operation and Maintenance (O&M) phase. In the past, IRS has absorbed these costs by reducing expenditures on all non-BSM projects, savings from process improvements and other realized technological efficiencies. However, as a result of the overall size of the BSM program and the number of deployed systems, additional resources are critical for the IRS to fund its increasing BSM O&M costs. Since FY 2007, the IRS Operation Support appropriation has covered over $100 million of operations and maintenance (O&M) requirements for these deployed BSM systems. The IRS Operation Support appropriation can no longer absorb any further BSM O&M.

The remaining $3.5 million is the overhead costs related to new hires for the BSM program.

Questions for the Record
Submitted by Ranking Member Emerson

Roadmap for Audits

1. You recently noted that the IRS spends up to 25% of its time searching for issues of concern in large corporate audits, and noted that having a straightforward discussion with such taxpayers would cut down on the time it takes to complete an audit because it would help the IRS prioritize the examination of taxpayers. While I can understand the value of having corporations provide more information in their tax returns, I have to admit that I am skeptical of their willingness to comply with this given that it may result in a tax audit.

- To what degree do you believe this will actually encourage large corporations to highlight their tax vulnerabilities?
- Is there any way to enforce this, or is it simply a voluntary measure?

Response: Announcement 2010-9 described the IRS proposal to require certain business taxpayers to report information regarding their uncertain tax positions with their tax return and requested public comments on the proposal. The IRS also recently released a draft schedule and accompanying instructions for public comment. The comment period will end June 1, 2010, and we will take these comments into consideration as we work to implement the proposal and complete the new schedule.

We believe the proposed reporting would be beneficial to both taxpayers and to the IRS by identifying issues early in the compliance process and reducing the time and resources required to identify, develop and resolve audit issues. Although we expect the level of specificity provided by the affected taxpayers will vary, we are encouraging concise descriptions of these positions, and believe that most large corporations will comply by adequately reporting their uncertain tax positions.

As proposed, the new reporting requirement would not be voluntary, and the existing penalties for failure to report required tax return information would apply. As we continue to develop the proposal, we will consider whether additional penalties might be needed, particularly with respect to intentional reporting violations.

Questions for the Record
Submitted by Congresswoman Lee

Electronic filing and pre-populated tax returns for low income filers:

My home state of California has a program called Ready Return, where the state sends a pre-populated or pre-filled tax return for tax filers with very simple returns. Tax payers then simply review the form for errors and if everything is correct, they just sign it and mail it in.

I also support the increased funding that IRS requests for Business Systems Modernization. It is my hope that strategic investment in these systems will make tax time more efficient for the IRS and the American taxpayer.

The President has supported the possibility of pre-populated returns as well.

1. As the IRS completes modernizing and completes the new information technology systems, will the IRS's new systems be compatible with the data and IT systems of the other federal agencies, like Social Security, so that we can be certain that IRS will be in a position to begin working with the other relevant agencies and regulatory bodies to begin work on a plan to create a National Ready Return Program?

Response: The IRS is focused on delivering high quality taxpayer service to the approximately 140 million individuals who file tax returns every year. We currently offer many levels of assistance, from free tax return preparation through our volunteer partners and IRS Taxpayer Assistance Centers (TACs), to free electronic filing through the FreeFile Alliance. The IRS is currently updating its core taxpayer account database, which will deliver faster refund processing, improved customer service, and will position the agency for future enhanced online services. The IRS is following all applicable government standards, as well as industry best practices in developing its new data-centric approach. This approach will allow for maximal flexibility as the IRS looks to leverage its ongoing technology investments for enhanced taxpayer service and compliance programs.

2. When the new database system is fully functional, would it be possible for the to help taxpayers from all states and territories identify all of the need based tax credits and social services programs that they qualify for based on data collected by the IRS?

Response: The IRS currently provides taxpayers with IRS.gov-based tools for credits such as the Earned Income Tax Credit Assistant. Currently, GovBenefits has the lead for the US Government in providing America's citizens with an integrated view of the benefits available to them. In the past, IRS has worked with GovBenefits (http://www.govbenefits.gov/govbenefits_en.portal) around linkages from GovBenefits to IRS's web tools.

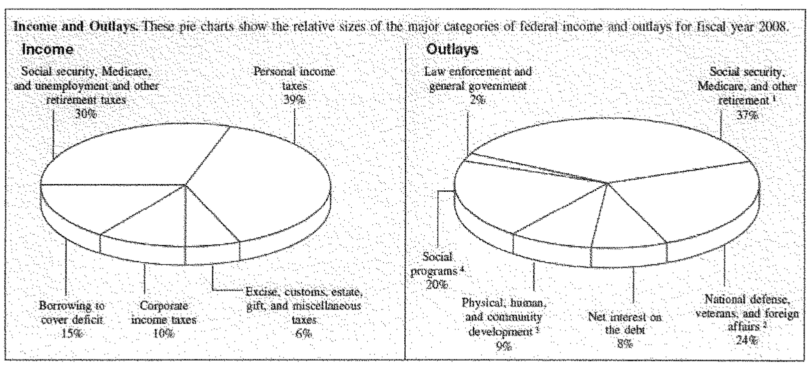
Tax payer budget transparency

I believe that it would be a very important public service to provide to the American taxpayer a breakdown of how much of their dollars on programs like housing, education, science and technology, transportation infrastructure, healthcare, or national defense.

1. Would you consider including a detailed graph or chart of how the United States spends their taxpayers dollars with each tax form distributed by the IRS?

   Response: The IRS already includes information such as you describe in the instructions for the Form 1040 (Individual Income Tax Return), 1040A and 1040EZ, which approximately 140 million individual taxpayers use to file returns each year. The chart below is included in the package.

Major Categories of Federal Income and Outlays for Fiscal Year 2008



Income and Outlays. These pie charts show the relative sizes of the major categories of federal income and outlays for fiscal year 2008.

TAX LIABILITIES OF TARP/TALF BENEFICIARIES

Commissioner Shulman, you responded that many of financial services firms that received TARP and TALF bailout funds are in a near constant state of being audited by the IRS and that they routinely have outstanding tax cases against them.

1. Can you tell the subcommittee if any of the firms' continuing tax issues rise to criminal levels? Have any of these firms or their officers been indicted on tax fraud or similar charges?

Response: The IRS can neither confirm nor deny any open criminal investigations. As of this writing, there have been no criminal indictments filed on tax or related charges responsive to this question.

RATE OF AUDIT EXAMINATIONS

1. Will IRS report back to this committee, the rate at which the largest companies in America are audited each year?

Response: The measure used to represent the number of returns examined in a given fiscal year as a percentage of total returns with a filing requirement in the previous calendar year is referred to as the coverage rate. This rate should provide a reasonable measure of the rate at which a given category of taxpayers are audited for a given year.

Additionally, the asset size indicated on the filed return is a reliable indicator of the size of the taxpayer. In response to the question, the category of largest companies would therefore encompass a portion of the large corporate return filing population. We acknowledge that "company" does not always equate to a corporate return. However, in terms of the question, we believe corporate return filings and audits will provide the best description of audit rate consistent with our available data.

The large corporate filing population is generally defined as corporations with assets $10 million and greater. The largest could be those with either $1 billion or more in assets or potentially those with $5 billion or more in assets reported.

The table below presents relevant coverage rate data for the large corporations plus data for the two sub-categories that could potentially be defined as "largest corporations."

Returns Filed and Examined for Large Corporations Categorized by Asset Size 03/29/10

	All Returns Filed	Returns Examined	Percentage Covered
➢ Corporations with Assets $10 Million and over			
FY 2009 Returns Filed and Examined	65,546	9,536	14.5%
FY 2008 Returns Filed and Examined	61,641	9,406	15.3%
FY 2007 Returns Filed and Examined	57,357	9,644	16.8%
➢ Corporations with Assets $1 Billion and over			
FY 2009 Returns Filed and Examined	6,135	2,336	38.1%
FY 2008 Returns Filed and Examined	5,375	2,378	44.2%
FY 2007 Returns Filed and Examined	4,983	2,206	44.3%
➢ Corporations with Assets $5 Billion and over			
FY 2009 Returns Filed and Examined	1,708	1,128	66.0%
FY 2008 Returns Filed and Examined	1,425	1,147	80.5%
FY 2007 Returns Filed and Examined	1,339	1,054	78.7%

Notes
1. Data is extracted from IRS Data Book Table 9a. Examination Coverage: Recommended and Average Recommended Additional Tax After Examination, by Type and Size of Return, Fiscal Years 2007, 2008, 2009
2. Corporations include Forms 1120, 1120-A, 1120-H, 1120-L, 1120-M, 1120-ND, 1120-PC, 1120-POL, 1120-REIT, 1120-RIC, and 1120-SF

2. Will IRS report to this committee the rates of examination for both individuals and businesses by income levels currently and the rates that IRS hopes to achieve under the President's refocusing of IRS's enforcement efforts?

Response: Below is the rate of examinations for individual returns (with and without businesses) at various income levels:

Individual Returns Over $200K (Includes data for $1M and over)

	FY 09 Filings**	Examined	Coverage	FY 08 Filings	Examined	Coverage
Returns with Total Positive Income of at least $200,000 and under $1,000,000						
• NonBusiness returns	3,138,198	71,544		2,741,555	72,006	
• Business Returns	1,444,801	45,260		1,307,825	36,871	
Returns with Total Positive Income of $1,000,000 or more	441,715	28,349		392,776	21,874	
Total individual returns with total positive Income over $200K	**5,024,714**	**145,153**	**2.89%**	**4,442,156**	**130,751**	**2.94%**

Individual Returns Under $200K						
	FY 09 Filings**	Examined	Coverage	FY 08 Filings	Examined	Coverage
International returns (1040PR/1040SS)	234,733	5,475		124,311	1,581	
Business and Nonbusiness returns with earned income tax credit (EITC) by size of total gross receipts						
• Under $25,000	20,518,519	457,082		21,028,686	410,889	
• $25,000 or more	1,452,041	26,743		1,470,688	51,368	
Nonbusiness returns without EITC						
• Without Schedule C, E, F or Form 2106	79,950,759	343,952		78,608,856	342,958	
• With Schedule E or Form 2106	15,094,220	201,943		15,409,542	205,432	
Business returns without EITC						
• Nonfarm with gross receipts under $25,000	10,284,637	114,849		10,496,414	122,321	
• Nonfarm with gross receipts $25,000 under $100,000	3,308,171	62,946		3,228,160	59,739	
• Nonfarm with gross receipts $100,000 under $200,000	949,650	39,496		943,174	36,131	
• Nonfarm with gross receipts $200,000 or more	736,479	23,632		730,815	22,869	
• Farm Returns	1,395,747	4,617		1,366,833	7,542	
Total individual returns with total positive Income under $200K	**133,924,956**	**1,280,735**	**0.96%**	**133,407,479**	**1,260,830**	**0.95%**

Note: **Filings from 2009 DO NOT include returns filed due to Economic Stimulus Act of 2008

The total coverage rates of examination the IRS achieved in FY 2009 and plans to achieve in FY 2010 and FY 2011 are provided below.

IRS Examination Coverage Performance Measures

Performance Measures	Type of Measure	FY 2009 Target	FY 2009 Actual	FY 2010 Planned	FY 2011 Planned
Examination Coverage - Individual	Oe, L	1.0%	1.0%	1.1%	1.1%
Examination Coverage - Business	Oe, L	5.8%	5.6%	5.1%	5.0%

Key: Oe - Outcome Measure, E - Efficiency Measure, Ot - Output/Workload Measure, L - Long-Term Goal

WEDNESDAY, MARCH 10, 2010.

FY2011 BUDGET FOR DEPARTMENT OF THE TREASURY

WITNESS

HON. TIMOTHY F. GEITHNER, SECRETARY

Mr. SERRANO. The subcommittee will come to order.

Mr. Secretary, before we go on, I join Mrs. Emerson in having you convey to the folks at the IRS our deepest sympathies and our condolences. That was a tragic situation and one that can never be tolerated regardless of how anybody feels about anyone in government.

And so, please let them know, as we told Commissioner Shulman, that our thoughts are with them, our prayers are with them and, personally—and I know Jo Ann feels the same way—that we respect and admire the work that they do on a daily basis.

Secretary GEITHNER. Mr. Chairman, could I say before we start, thank you for that. And I wanted to begin my remarks today, actually, by thanking you for what you said at Commissioner Shulman's hearing.

And I agree with everything you said, that we owe them our support, our gratitude, our respect. They are a remarkably dedicated group of public servants. They take great pride in their work. And nobody in that position should have to face what they faced. And they showed great bravery in evacuating that building quickly. They saved tens and tens of lives by how they acquitted themselves in that moment of panic and attack. And when I went out there with Commissioner Shulman, they were very strong and very brave and remarkably dedicated and committed to the work of the Service.

Mrs. EMERSON. Let me also say, Mr. Secretary, that all of the families and employees are in our deepest prayers and our thoughts every day. And they showed a remarkable resilience, in my opinion, as well. And oftentimes bureaucrats are not treated, perhaps, with the respect that they are due. But, in this particular case, I think it just points out to how many hardworking people there are really working for all of us on a daily basis.

Mr. SERRANO. Thank you.

Today the subcommittee meets to consider the budget request and conduct oversight over the Department of the Treasury. We welcome the Secretary of the Treasury, Timothy Geithner, back for his second appearance before the subcommittee.

For fiscal year 2011, the Treasury Department is requesting authority to spend $14.1 billion, an increase of $551 million, or 4 percent, above 2010.

I welcome the second straight requested increase for IRS enforcement efforts to prevent offshore tax evasion. While most Americans rely on salaries from employment that are taxed before they receive their paycheck, many wealthy individuals and businesses continue to use offshore accounts to hide billions of dollars in income generated by investments and income from abroad.

I note that Treasury's budget request also proposes to reform our taxes on international activity and to counter the use of offshore tax havens. These proposals would increase revenue by more than $120 billion over the next 10 years. These are good initiatives.

I also welcome your proposed increase in funding for financial and technical assistance by the CDFI Fund and look forward to learning more about the proposed new CDFI initiatives on healthy food and banking the unbanked. I believe that the CDFI has done some of the most important work in lifting up disadvantaged communities and look forward to discussing this work with you today.

The Treasury budget request has other notable increases, including a 13 percent increase for Treasury's departmental offices after a 9 percent boost for this year.

I am concerned, however, that the Treasury budget proposes to reduce grants for low-income taxpayer clinics, tax counseling for the elderly, and the Volunteer Income Tax Assistance Grant Program. All three programs assist low- and moderate-income taxpayers. I believe that supporting these taxpayers is of paramount importance and have made them a priority in my years as chairman of this subcommittee.

In addition, I am dismayed that the administration has once again included a $106 million proposal to tax all stores selling alcohol and tobacco the same amount regardless of their size. I am opposed to charging my neighborhood bodega the same flat fee as big suburban mall liquor stores, and Congress under both parties has repeatedly rejected it. As a practical matter under the current budget circumstances, I would probably have no choice but to consider budget cuts elsewhere to make up for this unrealistic proposal.

Mr. Secretary, you may have come here to defend your budget, but, as you know, we never allow you to leave without a discussion of economic policy. You are the highest administration official with a major role in economic policy who is required to testify before Congress. From the outset, you have been at the center of the debate over how to respond to the financial crisis, first as president of the New York Fed and then as Treasury Secretary. Much of that debate here in Congress has been concerning the Troubled Asset Relief Program, TARP, which continues to be a point of great interest among Members on both sides of the aisle.

Thankfully, it seems that perhaps the worst of the economic crisis is behind us, and yet we still have plenty more to do to get the economy back on its feet again. To that end, over the course of the last year, you have announced initiatives to respond to the concerns of everyday Americans: small business credit, mortgage relief, and limits on executive compensation at firms rescued by the taxpayers.

Many of the next steps for these issues remain in the hands of Congress, but, as a matter of practice, we must trust that you are looking out for the American people on a day-to-day basis. I feel confident that you are doing so and look forward to discussing the administration's efforts on behalf of the American people with you today.

And, with that, I turn to my colleague and sister, Mrs. Emerson.

[The information follows:]

Congressman José E. Serrano

Chairman, House Appropriations Subcommittee on Financial Services and General Government

<u>For Immediate Release</u>: March 10, 2010
Contact: Philip Schmidt, (202) 225-4361

Opening Statement of Chairman José E. Serrano
Hearing on the Treasury Department
Fiscal Year 2011 Budget Request
March 10, 2010

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Congressman José E. Serrano has represented the Bronx in Congress since 1990. He is the Chairman of the House Appropriations Subcommittee on Financial Services and General Government.

Mrs. EMERSON. Thank you, Mr. Chairman.

Secretary Geithner, thank you so much for being here with us this afternoon. And I know, as Treasury Secretary, you are facing many daunting challenges, including the attempts to reinvigorate bank lending to consumers and small business; trying to stabilize housing and commercial real estate markets; and, most important, protecting the American taxpayer, their investments, and preserving the long-term financial health of the Federal Government. And I know that you and your staff have been working extraordinarily hard on these issues, and we appreciate your dedication.

Regarding the financial condition of the Federal Government, I am very concerned that there does not appear to be a short- or a long-term plan to address deficit spending. The administration's budget estimates that the fiscal year 2010 deficit will be $1.6 trillion, with deficit spending continuing to exceed $700 billion per year through fiscal year 2020 when it increases back up to $1 trillion.

This level of spending will increase our debt-to-GDP ratio to almost 80 percent, the highest level since 1950. How is this level of debt sustainable, especially as more and more of the baby boomers, like Joe and I, reach retirement age? And are we on the same fiscal path as Greece? Are we irrevocably damaging the economic opportunities for future generations?

Regarding the economy and unemployment, I am concerned with the administration's sometimes confusing message with regard to job creation. On the one hand, the Federal Government is running up enormous debts in an effort to stimulate the economy and create jobs; however, on the other, the administration is pushing for massive new regulations on health care, greenhouse gasses, and the financial industry. These new regulatory policies don't stimulate growth or small-business lending. In fact, they are creating a lot of uncertainty among lenders, among the many, many small businesses with whom I speak on a daily basis, and consumers.

While I agree that there are some commonsense reforms needed in all of these areas, massive new government intervention in these areas will hinder short-term economic growth. So I am concerned that, while the administration is trying to spend our way out of the recession and high unemployment at the cost of future generations, that you all are also advocating policies that will hurt short-term job growth, not stimulate it.

So, as I said to begin, you face a lot of challenges in managing the Federal Government's finances and in attempting to reinvigorate the economy. I hope to be able to work closely and collaboratively with you, the chairman, and the rest of our committee to address these matters. So, thank you.

Thanks, Mr. Chairman.

Mr. SERRANO. Thank you.

Well, Mr. Secretary, you know the routine. We hope you stay within 5 minutes. Your full text presentation will go in the record, and that will give us time to grill you as the time goes on.

Secretary GEITHNER. Thank you, Chairman Serrano and Ranking Member Emerson, members of the committee. It is a pleasure to be back up here today. I want to thank you for all the support you have given Treasury and the IRS in the past. And I am very committed to, of course, working with you closely as we go forward meeting the many challenges the country faces.

I want to begin, Mr. Chairman, just with a few remarks on financial reform. Many of you may have read today in the paper that we saw another of the Nation's large banks today decide to sharply limit the practice of charging customers outsized fees for overdrafts. And I just want to say we welcome these efforts by banks to try to begin the process of restoring trust and confidence of their customers. And we welcome the fact we are seeing banks now try to get ahead of the President's financial reform effort that is now working its way through the Congress.

After years in which we saw many financial companies competing to exploit vulnerable borrowers, it is good to see banks once again competing to benefit their customers. And I want to urge other large banks that have not acted to follow the lead of some of their competitors.

But voluntary action is not enough. Progress today can too easily erode, as memories of the crisis fade. And that is why the President has proposed a very strong set of reforms for Wall Street, including an independent consumer agency charged with making sure that customers get better access to information, better choices, with clear rules enforced across banks and nonbanks. The House has acted, and we hope that the Senate will support Chairman Dodd's efforts to move ahead now. We can't afford to go through another period where we see a race to the bottom across our financial system.

Now, a little over a year ago, when President Obama took office, the urgent challenge facing the country was preventing a second Great Depression. At that time, as you know, the American economy was shrinking at an annual rate of 6 percent. Now, in the fourth quarter of last year, we saw the economy grow again at about that rate, about 6 percent. And this was a result, of course, of forceful action by the President and Congress under the Recovery Act and the result, also, of the steps we took to prevent the collapse of our financial system.

But we still face enormous challenges as a country. The recession caused enormous damage. Millions of Americans are still out of work. Many are still facing foreclosure. Many are still struggling to keep businesses open. They are still living with the consequences of the worst recession in many decades.

Now, that is why job creation remains our principal focus. Working with Congress, we propose to expand and extend tax cuts for job creation and investment, a $30 billion small-business lending fund, and expansion of the SBA's programs. The President's budget also proposes investments in American innovation and education, in exports and infrastructure that will help lay a foundation for stronger future economic growth.

And we are proposing to make these investments and reforms in a fiscally responsible way. As part of this commitment, the President proposed to freeze nonsecurity discretionary government funding for 3 years starting next fiscal year. And this, along with other steps to restore fairness to the tax system and what we hope will be the recommendations of the bipartisan fiscal commission, will help limit the growth of government spending in the future and reduce our deficits over time.

Now, as you know, the Treasury Department plays a central role in this agenda of spurring job creation, encouraging innovation and investment, promoting strong economic growth, and restoring responsibility to our Nation's finances. And I just want to highlight briefly some of the key features of the Treasury Department's budget request for fiscal year 2011.

At the start of this budget process, I asked Treasury senior staff to identify efficiency gains, program cuts and reforms. And, as a result of this process, you have before you today program cuts and new reforms that would generate nearly a half a billion dollars in savings and revenues for the Department. Just to cite two examples, we propose to cut $100 million by not funding the CDFI Capital Magnet Fund and Bank Enterprise Award funds. And we identified savings that would generate for the IRS nearly $43 million through more electronic filing and by eliminating the automatic mailing of tax booklets to taxpayers.

Now, we are proposing to use these savings to fund a series of targeted, modest investments in the Internal Revenue Service; the Community Development Financial Institutions Fund, the CDFI Fund; our global economic and national security priorities; and rebuilding the Treasury Department's professional staff. The resulting budget amounts to a modest but significant 3.5 percent increase over last year.

Just very briefly, Mr. Chairman, for the IRS, we proposed to strengthen IRS enforcement with a $250 million investment to increase voluntary compliance, an effort that would produce as much as $2 billion in additional tax revenues; other targeted investments to improve IRS customer services; and technology to enable the IRS to process tax returns more quickly.

We have proposed to expand the CDFI Fund, which has a long record of leveraging private money to help attract private investment to some of the country's most hardest-hit, distressed communities.

On the international side, as you know, Treasury plays a very key role in advancing U.S. economic interests abroad and protecting our national security interests. And our budget request would provide funding for the Department's efforts to improve international cooperation on economic recovery and financial reform and to make sure that we have adequate resources put into our national financial sanctions program, which is designed to deprive terrorists, nuclear proliferators, and other illicit actors of access to financing.

Now, Treasury entered this economic crisis with its professional ranks seriously depleted. We entered the worst economic downturn in generations with, just as an example, only 25 economist in the Office of Economic Policy, which is a third fewer than in 2000, about a decade ago. Just to give you a comparison, similar offices at the Departments of Housing and Urban Development, Agriculture have 140 and 330 economists, respectively. The Federal Reserve system has over 500 Ph.D. Economists. Another example, our two key offices, Domestic Finance and Tax Policy, had very modest levels of staffing coming into this crisis, significantly below the levels that prevailed in the past.

We have a long tradition in Treasury of operating with a very lean staff, and we are proud of that tradition. We have no intention of changing it, especially given the severe financial constraints the country faces as a whole. But we are going to have to make some targeted investments in rebuilding that institutional capacity at Treasury if we are going to have an adequate capacity to respond to future economic challenges. So we have proposed a modest additional investment to try to rebuild and strengthen in a very targeted way those three offices in the Treasury: Domestic Finance presides over the financial system, Tax Policy, and our Economic Policy division.

Now, I have the honor of leading a team of very smart, dedicated individuals who are working every day to make our government more effective, make our economy stronger and more fair. Treasury officials work every day in critical, important priorities, from helping restart small-business lending to working to contain the nuclear ambitions of Iran, from promoting job creation and investments to supporting debt relief for Haiti, from extending the benefits of growth to the hardest-hit communities in our country to promoting American exports around the world, from cracking down on mortgage scams to providing technical assistance to the Governments of Afghanistan and Pakistan, for example.

We have accomplished a lot over this year, but we have a lot of challenges ahead. And the investments we proposed in this budget will give us the tools to meet those challenges more effectively in the future.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Geithner follows:]

EMBARGOED UNTIL DELIVERY
2:00 p.m., Wednesday, March 10, 2010

Treasury Secretary Timothy F. Geithner
Treasury Budget Written Testimony
House Committee on Appropriations
Subcommittee on General Government and Financial Services
March 10, 2010

Introduction
Chairman Serrano, Ranking Member Emerson, members of the Subcommittee, thank you for the chance to testify about the President's Fiscal Year FY 2011 Budget for the Department of the Treasury.

Treasury plays a critical role in the day-to-day lives of Americans. We disburse social security checks, distribute tax credits to stimulate the economy and manage the finances of the United States Government. Under the leadership of President Obama, we have used authority provided by Congress to help responsible homeowners, promote investment in underserved communities, and stimulate lending for the small businesses that create jobs across the country. As we emerge from the worst financial crisis in generations, Treasury's role in both protecting the financial security of Americans and our efforts to stimulate the economy will be essential to the nation's recovery.

Treasury's FY 2011 Budget seeks to invest in four areas: repairing and reforming the financial system to make it safer and help assure that its benefits are broadly shared; boosting voluntary compliance with our tax code to pay for vital government functions; advancing our global economic interests and national security; and rebuilding the Treasury's professional staff.

The focused investments in Treasury's Budget request will support our key goals of spurring job creation and private investment, stabilizing the housing market and financial sector, and reinforcing strong, broad-based economic growth. I look forward to discussing some of the details of our Budget Request with you today.

Economic Recovery and Crisis Response
While substantial challenges remain for the economy and financial system, the broad strategy that this Administration has adopted to address a historic recession and contain the financial crisis has been effective.

A year ago, the American economy was shrinking at an annualized rate of six percent. Now, due in large part to the American Recovery and Reinvestment Act ("Recovery Act"), the economy grew at an annual rate of six percent last quarter. Further, the consensus amongst private economists is that the Recovery Act has saved or created more than two million jobs thus far. As part of the Recovery Act, Treasury has provided more than 95 percent of American families with tax cuts, $85 billion in credit for cash-strapped states, and provided billions of dollars more in targeted investments for clean energy and infrastructure.

In February of last year, I announced a strategy to encourage private capital to replace the Troubled Asset Relief Program (TARP) investment in our financial system. The stress tests of

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2:00 p.m., Wednesday, March 10, 2010

our largest financial institutions provided the transparency and confidence necessary for those institutions to raise substantial capital in private markets. Since the results of the stress tests were announced, these institutions have raised over $140 billion in high-quality capital and over $60 billion in non-guaranteed unsecured debt. Treasury has already recovered two-thirds of TARP investments in banks, earning over $17 billion on those investments through dividends and warrants. Today, the American government has a dramatically smaller stake in banks than a year ago because of this Administration's policies.

The expected cost of our financial stabilization efforts has also fallen sharply since last year. In President Obama's FY 2010 Budget, as transmitted in May 2009, the projected impact of financial stabilization efforts on the deficit was over $550 billion, including TARP and a reserve in case of continued instability. Today, the Treasury expects that impact will be less than $120 billion. And, if Congress adopts the President's proposed Financial Responsibility Fee, American taxpayers will not have to pay one penny for the cost of TARP. Treasury will continue its efforts in these areas until recovery is firmly established and the financial system is repaired and reformed.

Treasury's Budget
As the steward of the nation's finances, Treasury is well aware of the fiscal constraints America is facing. As we put together this year's Budget request, we placed a priority on identifying potential savings.

We made a series of tough choices. In some cases, we decided that it was necessary to terminate well-intentioned and sometimes popular programs because they aren't working or are duplicative. In others, we concluded that programs are worthwhile, but only if funding is accompanied by fundamental reform. In still others, we chose to seek your approval to shift the cost of programs from all taxpayers to those who benefit directly from the programs.

In the end, Treasury came up with nearly a half billion dollars in savings and revenues from bureaus and offices throughout the Department. Among the proposals:

- Fund the Alcohol and Tobacco Tax and Trade Bureau (TTB) in the same way as most other regulatory agencies —through fees on the regulated industries—at a savings to taxpayers of $106 million;
- Save the Community Development Financial Institutions (CDFI) Fund $105 million by not funding its Capital Magnet Fund and Bank Enterprise Award in the coming year;
- Save the IRS nearly $23 million through increased e-filing and another $20 million by eliminating the automatic mailing of tax booklets to taxpayers;
- Save $10.6 million in the Department's Headquarters Offices budget through efficiencies such as improved technology contracting and space utilization; and
- Cancel $62 million in unobligated balances from the Treasury Forfeiture Fund.

The result of our efforts is the targeted, constrained Budget that you have before you, a $13.9 billion request for the Department's 10 appropriated bureaus.

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2:00 p.m., Wednesday, March 10, 2010

Our Budget request includes a $474 million, or 3.5 percent, increase over FY 2010 enacted levels. This Budget includes targeted investments in the Internal Revenue Service (IRS), the Community Development Financial Institutions (CDFI) Fund, global economic and national security efforts, and institutional capacity. These key areas of investment in the FY 2011 Budget will be crucial to addressing the challenges our nation faces, and I would like to turn to how each will help us meet our increased responsibilities, achieve our immediate goals, and perform our core missions.

Improving the IRS
The Internal Revenue Service (IRS) is vital to the financial well-being of the nation. As the government's revenue collector, it raises the money that builds our roads, improves our health, and secures our nation.

Treasury's Budget request for the IRS reflects our understanding that in a dynamic society and open economy such as ours, administering a tax code is about more than simply collecting payments and keeping records. It also means increasing compliance with our tax laws.

To increase tax compliance we will bolster international enforcement, regulate tax preparers and improve the services that the IRS provides. To work effectively, all of these will depend on completing a long-running effort to modernize IRS technology.

Our Budget request provides nearly $250 million for new enforcement initiatives aimed at reducing international tax evasion and noncompliance by businesses and high net worth filers. By the time these measures are fully in place, we estimate that they will produce additional tax revenues of nearly $2 billion a year. This will mean $9 in additional revenue for every additional enforcement dollar spent.

The Budget request includes a number of legislative proposals that would, for example, repeal a requirement that indebted taxpayers make partial payments before starting negotiations with the IRS over how to handle their past due bills, and getting third parties to report more about payment to businesses. These adjustments would be relatively inexpensive to implement, impose little additional burden on taxpayers, and increase collections by an average of $2.6 billion a year.

We also are working to begin regulating tax return preparers. Given that the IRS estimates there are between 900,000 and 1.2 million preparers operating in the U.S., with many handling hundreds of individual filers, rules limiting fraud and errors by preparers would have a multiplier effect of improving compliance by millions of taxpayers, and would do so at minimal additional cost.

To get taxpayers to voluntarily comply with our tax laws requires more than tougher enforcement; it requires improved service. The Budget request includes a targeted investment of $46 million to improve taxpayer services. The IRS now receives more than 100 million service calls a year, so we propose $21 million to improve the answer rate for the IRS's 1-800 telephone lines.

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2:00 p.m., Wednesday, March 10, 2010

Additionally, we propose $25 million to upgrade the agency's website, IRS.gov. This will improve the agency's telephone service levels by encouraging taxpayers to turn to the web for services. It will also work in tandem with a multi-year effort by the IRS to encourage taxpayers to file electronically. Treasury estimates that e-filings will save the agency almost $23 million in the coming fiscal year, effectively paying for the new investment in the website.

To improve enforcement and service, the IRS must complete a decade-long upgrade of its technology. That's why our Budget request includes a $168 million investment to finish a new centralized database that we believe will double the speed of refunds to taxpayers, speed resolution of taxpayer issues, and allow for steadier mailing of tax notices to smooth out service-damaging spikes in telephone call volumes.

Reform and Investment
As we recover from the financial crisis, it is important that we put in place financial reforms that will protect consumers, investors, taxpayers and the entire economy from the risk-taking that produced the financial crisis. The House of Representatives has already passed a financial reform package, and we look forward to continue working with Congress to produce a package for the President's signature. But as we work to repair the financial system, it is important that we address the economic needs of the hardest hit communities.

The FY 2011 Budget provides the CDFI Fund with $250 million for the coming fiscal year. This includes $140 million for its flagship financial assistance awards to CDFIs, an increase of $32 million, or 30 percent, from the current fiscal year. This funding level is expected to leverage private sector capital by CDFIs and result in loans, investments, financial services and technical assistance to underserved populations and low-income communities. This translates into significantly more lending to support small businesses and microenterprises, first time homeowners, and the development and rehabilitation of low-income housing and community facilities, such as charter schools and child care centers.

The CDFI Fund reports that recent award recipients helped finance over 10,000 businesses and over 1,600 commercial real estate properties in 2008. CDFIs also reported that they helped create or maintain over 70,000 full-time jobs in that period.

While we have made additional funding available for the CDFI Fund's financial and technical assistance awards to CDFIs, we have also refocused our priorities to support two critical new areas: (1) expanding access to financial products and services through the Bank on USA initiative; and (2) a program that is part of the First Lady's campaign against childhood obesity, the Healthy Food Financing Initiative (HFFI).

In order to make funding available for these initiatives and for the Fund's core financial and technical awards, we propose to save $105 million by not funding the Capital Magnet Fund or Bank Enterprise Awards programs in FY 2011.

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2:00 p.m., Wednesday, March 10, 2010

The Bank on USA initiative would help expand access to mainstream financial services to help families avoid predatory lending traps and high fees for check-cashing and other alternative financial services. The initiative will promote broader access to bank accounts, basic credit products, and other financial services to help these families build savings and solid credit histories.

I recently joined the First Lady in Philadelphia to highlight the HFFI program. HFFI is a partnership between Treasury, the Department of Agriculture, and the Department of Health and Human Services that will provide over $400 million in financial assistance to expand access to nutritious foods in urban and rural communities that have limited access to healthy foods, sometimes called "food deserts." This initiative will help to promote a range of financing to expand access to nutritious foods, including developing grocery stores and other small businesses selling healthy options in "food desert" communities.

A key component of HFFI is the New Markets Tax Credit (NMTC) program. The NMTC is another critical tool administered by the CDFI Fund which helps extend the benefits of recovery to hard-hit communities. This tax credit helps attract investment to these communities by reducing the risks investors must take in putting their capital into them. It does so by letting investors claim a 39 percent credit against their federal income taxes in return for making equity investments in Treasury-certified Community Development Entities (CDEs). CDEs, in turn, invest in small businesses and other projects that serve hard-hit communities.

To date, NMTC recipients have invested over $15.6 billion in distressed communities across the country. That financing has helped small businesses, manufacturers, grocery stores and retail centers, alternative energy projects, healthcare centers, charter schools and job-training sites. It has helped create, save or support hundreds of thousands of local jobs. The Budget requests $5 billion in NMTC authority in 2010, and another $5 billion of authority in 2011.

We are proposing reforms to make the credit more effective, such as expanding the types of taxes against which the credit can be used. As is the case for many types of investments, investor capacity to use NMTCs has fallen since the recent crisis. To help attract a broader array of investors, our Budget Request would change the credit so that it can be used to offset not only investors' regular federal income taxes, but also the taxes they owe under the Alternative Minimum Tax (AMT).

In addition, Treasury is working to simplify rules for the NMTC to improve the overall attractiveness and effectiveness of the credit as well as to make the credit work better for small businesses. Treasury and the IRS are actively pursuing reforms that would make it easier for CDEs to provide more working capital loans and other investments in small businesses in distressed communities. In all of these efforts, our aim is to strengthen the NMTC's ability to attract investments and jobs to hard hit communities.

EMBARGOED UNTIL DELIVERY
2:00 p.m., Wednesday, March 10, 2010

Global Economic Interest and National Security
Treasury also advances U.S. economic interests abroad, advocates international policies that help create American jobs and domestic economic growth, and protects against foreign threats to our economic and financial well-being. The recent crisis elevated the importance of these tasks.

The Budget provides $44.4 million to support the Office of International Affairs. This includes a $6.7 million increase to support our international coordination efforts in forums like the G-20. Although not directly under the jurisdiction of this Subcommittee, the Treasury's Budget request includes approximately $3 billion to meet our obligations to the International Financial Institutions, which support the President's recent commitments in Copenhagen to help combat climate change, contribute to a multi-donor trust fund to combat global hunger, and meet our international obligations.

Treasury plays a critical role in protecting our national security through the Office of Terrorism and Financial Intelligence (TFI). The Budget provides $203.1 million for TFI, which includes the Financial Crimes Enforcement Network (FinCEN). This includes $4.7 million in new investments to improve TFI's ability to target proliferation networks and expand Treasury's role in coordinating financial intelligence across the nation's overall intelligence community. The TFI budget represents less than two percent of Treasury's overall Budget, and, given the important results that it has produced, is an immensely cost-effective program.

TFI works to deprive proliferators, terrorists, narcotics traffickers, corrupt foreign officials and other illicit actors of the money and financial access they need to carry out or profit from their activities.

To do this, TFI uses financial information to map out the support networks of these dangerous actors, works to educate financial institutions worldwide about the risks of doing business with them, administers and enforces financial regulatory authorities that protect the integrity of our financial system, and collaborates with our foreign partners to set standards to help the international financial system avoid illicit activity.

For example, TFI's efforts to crack down on the financing of the proliferation of weapons of mass destruction have led to financial institutions worldwide cutting off the banks, companies, and individuals that are integral to Iranian, North Korean and Syrian nuclear ambitions. In the case of Iran, all U.S. banks, nearly every major European bank, as well as large banks in Asia and Middle East, have cut or severely limited their ties to that country.

TFI's efforts have also helped to put Al-Qaida in its worst financial position in years. Its core leadership is struggling to raise and sustain funds.

In pursuing all of these efforts, protecting the integrity of our own financial system is key. That is why, even as we continue our international efforts, Treasury is marshaling state, federal and private sector resources to crack down on mortgage fraud and loan modification scams, and is working to address emerging threats and vulnerabilities in new technologies and financial products.

EMBARGOED UNTIL DELIVERY
2:00 p.m., Wednesday, March 10, 2010

Rebuilding Treasury's Institutional Capacity
Treasury entered the recent financial and economic crisis with the professional ranks of many of its key policy offices seriously depleted. Responding to the crisis has put a severe strain on these units and made clear the need to rebuild our professional ranks to assure that Treasury can deal effectively with the issues that it must tackle.

We entered the worst economic downturn in generations with only 25 economists working in the Office of Economic Policy, a third fewer than in 2000. To put this in some prospective, the comparable office in the Department of Housing and Urban Development has 140 economists, the Department of Agriculture has 330 economists, and the Federal Reserve system has over 500 economists.

We arrived on the doorstep of the worst financial crisis since the Great Depression with our Financial Markets and Financial Institutions units within Domestic Finance each staffed by about 20 people, and a Tax Policy office whose staff had dropped by a fourth since 2000.

Treasury has a tradition of operating with a lean staff. We are proud of this fact, and have no intention to change it, especially given the severe fiscal constraints that the nation faces. But we must reverse the erosion of the Treasury's basic intellectual capital or we will be unable to meet the nation's economic challenges. We began the process of making targeted investments in upgrading professional staff this fiscal year, and we need to continue it in the coming year.

Our Budget request for FY 2011 would provide the Office of Domestic Finance with an additional $16.7 million to expand its staff by 24, in order to build capacity to more effectively respond to the aftermath of the financial crisis; promote stronger, more equitable financial policies; and add expertise in securities market structure and housing finance.

The request would provide an extra $2.4 million to the Office of Tax Policy to hire additional specialists to analyze emerging tax issues and provide timely analysis of key fiscal and financial issues as well as broader climate change and health care policy proposals.

Finally, we propose $2 million in funding to hire additional economists for the Office of Economic Policy for swifter, more effective analysis of economic trends and proposals. This sum would also fund the creation of a data analysis unit to maintain the large economic and financial databases used for Department-wide analyses.

These investments are very modest. We propose to add only six new economists to our Office of Economic Policy, which would still leave its professional staff below where it was in 2000. We propose to add just eight new specialists to the Office of Tax Policy, which would also leave its professional staff below 2000 levels.

Let me end where I did last year, with a word about the Treasury's staff.

EMBARGOED UNTIL DELIVERY
2:00 p.m., Wednesday, March 10, 2010

I have had the honor over the past year of leading a team of smart, dedicated individuals who are working to make our government more effective and our society fairer. They debate policies on their merits; they do what is right and not simply what is expedient; and they draw from the best ideas and expertise available. They are performing an incalculable service to our country. Several weeks ago, I joined IRS Commissioner Shulman in Austin, Texas, to talk to the IRS employees who were affected by the senseless attack on them and their co-workers, like Vernon Hunter, who tragically lost his life in the attack they are a group of dedicated and committed public servants. This nation owes them a debt of gratitude, and we owe them our respect.

Treasury has accomplished great things in the past year, but we recognize that challenges still lie ahead. The targeted investments proposed in this Budget will provide the tools needed to meet those demands.

Mr. SERRANO. Thank you, Mr. Secretary.

Let me begin by stating, when they devised TARP, our friends on the authorizing committees provided an open-ended funding stream for operational expenses. Congress has an obligation to do oversight of TARP operational spending.

In the report language adopted by our committee for the fiscal year 2010 financial services bill, the committee required the Department to provide a full accounting of TARP spending and staffing to date in your projections for next year. That report was due with your budget request last month, but, unfortunately, the committee has yet to see this information.

Do you have a time frame in place for providing this information to the committee? How much have operational expenses for TARP cost to date? And how much do you anticipate operating expenses for the TARP program will cost for the rest of this fiscal year and next?

Secretary GEITHNER. Mr. Chairman, we will provide that information as quickly as we can. I assume we can do it quite quickly.

But I just want to underscore, we are now in the process of winding down TARP. We have been able to achieve this recovery in the financial system at dramatically lower costs than we expected. The costs of this program have fallen—overall costs to the government of this program have fallen by over $400 billion from the initial estimates just a year ago. We have had over, I think, $170 billion come back to the American taxpayer by forcing banks to replace the government's investments with private capital. We are seeing a very substantial return to the American taxpayer on the investments the government made in banks.

Now, even though we have seen a lot of healing in the financial system, as you both said in your opening remarks, small businesses across the country still face a very difficult time getting credit. Our housing markets are still in the process of recovery; housing and finance still overwhelmingly dependent on the government. And we are going to need to continue to make some carefully designed, targeted programs to support additional credit expansion in those areas most damaged by the crisis. But I think the administrative costs of that are going to be a fraction, going forward, of what they were at the peak of the crisis.

But I just want to underscore that the overall program has achieved a dramatic improvement in stability in the system at much, much lower costs than anybody anticipated. And if the Congress joins with the President in adopting this fee we have proposed to recoup any losses from the Nation's largest banks, then you can tell your constituents, you can tell the American people that they won't be exposed to a penny of loss in this program.

Mr. SERRANO. Let me ask you a question on that. Experts in the field tell us that consumer confidence and investor confidence are what drive our economy. If people are afraid, it doesn't work; they don't invest, they don't buy, they don't purchase. But, at the same time, there is another part to that, and it is the part that falls on Members of Congress and the administration, and that is to create consumer confidence that what we are doing is correct.

So, on one hand, it might be—and it is, in many cases—that so much of what is going on is beginning to take hold. But the public thinks that we just threw money away, in many cases, and that we bailed out people we shouldn't have.

How can you and how can we work together, how can you help us, to get a better message out, if nothing else? You know, why is there such a disconnect with what many believe to be what is really going on to what the public thinks is going on?

Secretary GEITHNER. Well, I think it is very important to recognize that, even though the economy is now growing again and even though you are seeing the pace of job losses fall from, you know, three-quarters of a million Americans losing their job last January every month to—we are just now at the verge of the economy as a whole starting to create jobs again. But the crisis caused a huge amount of damage to confidence of the average American family, of the average business. And we are going to be living with the lasting effects of that damage to confidence for a long period. It is going to take some time for that to heal.

But it is very important that we are able to demonstrate to the American people that the programs Congress authorized in the Recovery Act and to help rescue the financial system are delivering what they were supposed to do. And, again, the best measure of that is you had an economy that was shrinking at an annual rate of 6 percent a year to an economy now growing at an annual rate of 6 percent per year. You are seeing the costs of credit to municipal governments, to someone who wants to borrow to get a mortgage, to buy a car, put their kids through college, come down dramatically. Credit is much more available to an average business today than it was when we took office, when this Congress came into power about a year ago.

Those are very, very substantial returns. In highlighting those returns—and they are the direct result of the actions Congress authorized in the Recovery Act. You know, remember, the Recovery Act was a third in tax cuts that went to 95 percent of working Americans and to businesses across the country. It was about, roughly, a third in infrastructure investments, targeted investment in infrastructure and support to State and local governments. And a substantial chunk went to help the unemployed, help those people hardest hit by the recession. But those things are generating a very substantial return, and you would not have an economy that had moved this quickly from deep contraction on the edge of a Great Depression to an economy growing, as I said, at an annual rate of 6 percent a year in the fourth quarter of last year.

So we have a lot of challenges ahead, but I think the best thing we can do is, you know, just make sure we can draw people's attention to the concrete aspects of those programs.

When you ask people whether they support tax cuts for working families, whether they support targeted infrastructure investments to help rebuild schools, rebuild bridges, when you ask them if they support assistance to State and local governments so they don't have to fire teachers and firemen, the American people support and welcome those investments. And it is important to draw their attention to the specifics, because it is sort of hard to understand when you limit the debate to these broad programs out there.

And, again, just one more thing, Mr. Chairman. The efforts we took to stabilize the financial system were never going to be popular. But it is very important for people to understand that, when we came into office and when this Congress took office in January of last year, the government had very substantial investments already in the banking system, and we have brought back more than two-thirds of those investments already. We did not write a check to a major U.S. bank since we came into office. We wrote some modest additional checks to small community banks, regional banks, but we did not give another dollar of the taxpayers' money to the Nation's major banks.

Now, we had a bunch of problems we had to solve, bombs we had to defuse, problems we had to dig out of, but we have been very, very careful in managing this very, very unpopular program in ways that allowed us to get the American people's money back from the financial system, to save them, as I said, over $400 billion in potential losses. And we are in a much stronger position as a country today to come out of this stronger. We have saved dramatic amounts of money that we can use to meet the many, many challenges we face as a country today.

Mr. SERRANO. Well, I want to keep going on this subject, but I will defer now to Mrs. Emerson, because I suspect we will have many Members today and the chairman should set an example for the 5-minute rule, which I just broke.

Mrs. EMERSON. Darn it, I was hoping that you would go over, Mr. Chairman, so I could as well.

Let me switch gears to the Federal debt for a moment, and I am sure we will come back to TARP. I have no doubt about it.

As I mentioned in my opening remarks, I have great concern about where we are going to end up in 2020, where our Federal debt held by the public will be about 77.2 percent of GDP, which would be the highest percentage of Federal debt to GDP since World War II, 1950, when I was born. So I have about three questions I would like to ask with regard to this. Well, actually, it is probably four, but I know you will indulge.

Given the size of the Federal debt, number one, is Treasury crowding out investment in the private sector? You know, obviously, to what extent are investors buying Treasury bonds instead of investing in businesses?

Number two, given the trouble in the world economy, how difficult is it to attract buyers of Treasury debt? And are you increasing interest rates in order to attract those investors?

And, three, who is investing in Treasury debt? And are you concerned about our dependence on foreign investors, foreign governments, sovereign wealth funds, and the like to finance our deficit spending?

Secretary GEITHNER. Excellent questions.

Let me just start by saying, as we discussed when I was here last year, that you are right to point out that our deficits are too high. They are unsustainably high. If you just look at over the next 10 years, they are unsustainably high, and they get dramatically worse, if Congress does not act to reform our Medicare and Social Security, they get dramatically worse in the succeeding decades.

So they are too high. They are unsustainable. And if we do not act to address them, then we will face much greater challenges as a country. Growth will be weaker. America will be poorer as a country. And you are right to highlight these challenges. And, of course, we are deeply committed to make sure we start the process now of building consensus on the policies to bring those deficits down.

Now, on your specific questions: You asked, is government borrowing today crowding out public investment? No, it is not. In a financial crisis, in a recession like this, the only fiscally responsible way to act as a country is to make sure you are providing temporary, targeted support to get the economy back on track, growing again.

And the best measure of what I just said, which answers your second question, is that U.S. long-term interest rates today, the rate at which Treasury borrows today, is really remarkably low. And it reflects the fact that, for the moment, again, given the echoes of this crisis, the most responsible thing we can do as a country is try to make sure we are providing the support and the investments necessary to lay a foundation for strong, sustainable private-sector growth.

Now, these things need to be temporary and targeted. And that is why we have proposed in the President's budget to begin the process in fiscal year 2011 of bringing down these deficits over time.

One more thing that goes to your third question. Today, the American people are providing most of the financing for our deficits, for these temporary exceptionally high deficits. Over the last year or so, in particular, you have seen the savings rate of Americans start to rise again. Private savings rates have risen from a modest negative to a rate which is in the positive 4 percent territory. At the same time, our current account deficit, which is the amount of money we are borrowing from the rest of the world, has fallen very, very sharply.

So, if you just step back, generally what you are seeing so far is a very high level of confidence among foreign investors in our economy and our financial system and a willingness of Americans to provide the financing the government needs temporarily to help get through this basic crisis.

But you are absolutely right to underscore the fact that these deficits are too high. They are unsustainable. And as soon as we are confident that we have a self-sustaining recovery in place led by the private sector, then it is very important we shift at that point to bring those deficits back down to Earth.

Mrs. EMERSON. I appreciate your answers, but if we are still at a trillion-dollar deficit at 2020, when will the savings actually materialize?

Secretary GEITHNER. Thank you for raising that.

For an economy like ours—and this is the critical imperative—we need to make sure we are bringing the deficit down to a level that stabilizes our overall debt burden as a share of our economy to a level that is not going to be acceptable and not threaten future growth rates. And for an economy like ours, that requires we bring our deficits to below 3 percent of GDP. It sounds like a magic number, but it is just, given the structure of our economy, that is what it takes to stabilize the overall debt burden as a share of our economy at an acceptable level.

What we have proposed in the President's budget is a series of detailed measures on the expenditure side and the resource side that would bring our deficit down over the next 4 years to below 4 percent of GDP. That is not far enough. We are very explicit in the budget saying that is not far enough, we need to go further.

And that is one reason why the President has proposed to form a bipartisan fiscal commission and to ask a set of national statesmen to step back from politics and try to take a fresh look at measures that help get us down further over the next 5 to 10 years but also begin to propose measures to deal with the long-term deficits in the further decades, which are clearly unsustainable and will be very damaging.

Mrs. EMERSON. You have great faith that that will work.

Secretary GEITHNER. No, it is a—as you know, Congress has to enact policies that restore gravity to the Nation's fiscal position. We have proposed a series of detailed measures that begin that process. But we are, you know, following the model of President Reagan, who proposed and ran, helped establish I think the best example of a successful bipartisan commission on Social Security reform, and we are using that, proposing that model to try to build a consensus on things that will bring sustainability back to the Nation's finances.

Mrs. EMERSON. Okay. One more quick question, and then I will be finished. And it is a more philosophical question. How do you balance a desire for short-term benefits to the economy versus the long-term risk to the future generations of increasing debt? I mean, I feel like we are being greedy or something.

Secretary GEITHNER. No, I think, again, with an economy facing the risk of a Great Depression, an economy living with the echos of the worst financial crisis in generations, the only possible, the only credible response of any government and the only thing that is fiscally responsible is to temporarily provide the kind of support on the tax side and on the investment side that can help reestablish a foundation for growth. That is what we did in the Recovery Act and our financial recovery efforts. And we are still in the period now where, as an economy, the best thing for us to do right now is to provide some modest additional targeted support for job creation and investment.

But that will not work, will not be effective, unless we can make people confident, in the United States and around the world, that we are going to find the will as a country to start to bring those deficits down as we shift to growth that is going to be sustainable.

So the imperative right now is still job creation and reinforcing growth. But, once we are confident we have an economy that is growing again, led by the private sector, then the right thing for the country to do is to bring those deficits down. That is how you balance them.

And if you make sure these investments we make today, like in the Recovery Act, are temporary and targeted and they are focused on things that will help restart growth and job creation, then you are doing the responsible thing and the effective thing to help restore our Nation's finances over the longer term.

These deficits are high today, as you know, they are high today overwhelmingly because of the policy choices made by the country over the past preceding 8 years and because of the consequences of the recession. When we came in office, you know, we had a—before we did one thing, asked Congress to propose one change to policy, we had a deficit of about $1.6 trillion, more than 10 percent of GDP, and that was a legacy of the recession and the policy choices the country made over the preceding 8 years. Those choices left us with very high projected future deficits, unsustainably high debt burdens. And we are going to have to work together across the aisle, Republicans and Democrats, to dig our way out of that.

Mrs. EMERSON. Thank you.

Mr. SERRANO. Just a quick comment, not a question, but it seems to me that we never had major wars where we didn't raise taxes. So we are all guilty of the $2 trillion that it will cost us over the next generation just to pay for the last two involvements. But there is one resolution on the House floor today that we can all be fiscal conservatives about and vote to get out of Afghanistan.

Now, Mr. Fattah, the way I see this is your beloved Phillies will play Ms. Emerson's beloved Cardinals for a chance to get beaten by the Yankees in the fall.

Mr. Fattah.

Mr. FATTAH. Thank you, Mr. Secretary. I think you have done an extraordinary job in a difficult situation.

If we looked a year ago, the first 2 months of the year, we lost more than a million and a half jobs. And these 2 months we have seen job losses of 50,000 in totality. But we have seen a major increase in temporary hiring; we have seen an increase in hours worked. All of this is a prelude to what all of us, I think, expect to see: net plus in job growth next month and going forward. The stock market was at 6,000 yesterday a year ago; it is now at 10,500. Purchasing is up, manufacturing is up. I mean, if you look at all of the indicators, they are pointing in the right direction.

Now, there are still some naysayers, and there are people who principally are responsible for the conditions that we find ourselves in who are critics of the work of this administration. But I want to go through some of the details.

When the President was sworn into office a year ago January 20th, the Nation's national debt was over $10 trillion. And we had a $1.2 trillion deficit for that fiscal year. Now, 8 years before that, we had Alan Greenspan in here, and we were having a discussion about the fact that a $5 trillion surplus could take the country to be debt-free at the conclusion of the Bush administration.

A bunch of decisions were made, so rather than surpluses to erase a $5 trillion national debt and an intellectual discussion about the economics profile of a nation that was debt-free, we had doubled the debt, and as it was the case at the end of World War II, in part for national defense. I don't think anyone would suggest that we should have forfeited World War II rather than run up some debt or that we should concede to bin Laden and company, you know, and sacrifice the lives of Americans because we are afraid to spend money. So, in part, we spent it on national security. And we also did tax cuts and so on.

But the point I want to get to now is that there has been a lot of discussions, and with the ranking member, about the deficit. I want to talk about the debt. The deficit is just what the gap is year to year. I want to talk about the national debt.

Now, we have seen the President set up the debt commission with Erskine Bowles and with Senator Simpson. We have seen the Vice President say that this national debt is a national security issue. The Secretary of State last week said it is a national security issue. You have made comments about the challenges that it presents in the international framework of our dealings.

What do you—and I know that you are short a few economists in the Tax Policy Office. Previous Treasury Departments looked at broad-based tax reform. Everyone who is knowledgeable on this says we have to raise some revenue, we have to cut our long-term costs on entitlements, and we have to engage in broad-based tax reform.

Now, the Reagan Treasury Department and the Bush Treasury Department, 20 years apart, looked at the national sales tax, said it was fatally deficient, it wouldn't work. They looked at the flat tax, said it wouldn't work.

So my question to you is, as we go forward, we need to have a deficit commission, which we have in place—and I am happy to see that Leader Boehner has said he is going to make appointments, and the Republicans in the Senate are going to make appointments. So they can look at long-term entitlements, and that is great.

What I am interested to know is what you think about an idea of a dedicated revenue focused entirely on paying down the national debt, going forward, as part of a constellation of things. You know, we passed statutory PAYGO and so on. But a revenue source dedicated to debt, what do you think about that as a generality?

And then specifically, I have proposed a transaction fee on non-stock, non-financial markets activity of a penny on a dollar, dedicated entirely to the debt. I would like to know what you think about that specifically.

Secretary GEITHNER. Congressman, you are right to point out that we have an unsustainable fiscal position, and we are going to have to bring our resources and our commitments more into balance over time.

Now, what we have asked this commission to do, what the President has charged the commission with doing is to, as I said, step back from politics, take a fresh look, everything is on the table, no preconditions, and to see if they can come up with recommendations on a bipartisan basis that will help address both problems: not just the long-term problem of the next 4 decades, but the more immediate problem of how we get the budget down to a more sustainable level over the next 5 to 10 years. Both are necessary. Both are part of the commission's mandate. It is not just the very long-term problems of entitlement reform.

Now, they are going to take a look at a range of ideas. I am sure they will take a look at a range of ideas from both sides of the aisle. And, again, what we wanted to do is get a group of people together who can step back from politics, take a fresh look, no preconditions.

And, you know, I think that it is important for us to recognize that we are a very strong, resilient country. In the past when we have faced challenges like this, we have acted. The world has confidence in our ability to do that. We need to make sure we are going to earn that confidence again.

And I have no doubt that this is within our capacity to fix over time. We need to get some people together working on it now, because, you know, again, as the economy recovers, as growth gets established, it is going to be time then to start to move. We can't put this off.

Mr. FATTAH. Has Treasury looked at any new ideas, revenue-raisers?

Secretary GEITHNER. As you know, Treasury has a great tradition, a great, pragmatic, creative tradition in tax policy and elsewhere, of looking at all ideas. And, you know, we will, along with OMB, we will provide some support to the commission as it goes through this. But we are going to leave the commission the task of trying to evaluate the options and help educate the American people about the challenges ahead.

Mr. FATTAH. Well, I understand. I appreciate that. The commission, obviously, has to have ideas that have been rigorously analyzed, and your department is most capable, so that they can make an informed choice. So——

Secretary GEITHNER. And we will provide that, as we always have attempted to traditionally.

Mr. FATTAH. So my last question then is, can we get the proposal that I have made in H.R. 4646 analyzed by your department, torn apart, and looked at to see whether it can be a part of perhaps addressing some of these issues?

Secretary GEITHNER. Again, we generally try not to "tear apart" proposals made by the Appropriations Committee——

Mr. FATTAH. Well, I mean——

Secretary GEITHNER [continuing]. But we will take a careful look at anything that you all have proposed and asked us to take a look at.

Mr. FATTAH. Well, I will ask the chairman to submit it to you officially and ask for its review. Thank you.

Mr. SERRANO. Good idea. We will do that.

Mr. Kirk.

Mr. KIRK. Thank you, Mr. Chairman.

You met yesterday with the Prime Minister of Greece. And I am particularly concerned by, as The Washington Post reported, Greece's problems, critics argue, have only partially to do with speculators, more to do with false economic data, broken tax system, runaway spending. The Greeks report that only 5,000 people make over $136,000 in their whole country.

I am particularly concerned about the role of U.S. financial institutions, particularly Goldman Sachs, that as Greece got on the heroin of borrowed money, Goldman was the crack dealer and did not disclose these increasing liabilities to the EU financial system, to the IMF, or to the Fed.

Now, Papandreou asked you for money and backing. But it would seem that not only should we very carefully review any request he has, but have you had any frank discussions with Goldman about their very questionable role in this?

Secretary GEITHNER. Congressman, just to clarify one thing, the Prime Minister did not ask me or the President for financial assistance yesterday. What he did do was to outline the reforms they have enacted so far and the plans they have in prospect to help dig themselves out of a unsustainable fiscal position and restore growth and competitiveness to that economy. He has a lot of challenges to face, but he is beginning that process. And he also walked us through their discussions with the Europeans to try to make sure they are managing through this carefully.

Now, it is very important that the United States work with Europe to put in place a comprehensive set of reforms to provide oversight over the derivatives markets. It is important to us. It is important to them. It is something you have to do globally if you are going to do it effectively.

And, as you know, we proposed in the House a sweeping set of reforms that would bring oversight to all participants in those markets, move the standardized parts of those markets on to clearinghouses, bring transparency to those markets, make sure that our enforcement authorities, the SEC and the CFTC in particular, have the ability to police, to go after, to deter fraud and manipulation.

And that is very important to us. We are going to work very closely with the Europeans to help support those reforms. Part of the imperative here is to bring as much transparency as we can to those markets now.

Mr. KIRK. Let's go to the question.

Secretary GEITHNER. I am coming to your question, which is that, you know, I can't comment on any ongoing investigations, but, of course, as you have heard the Federal Reserve chairman say, the responsible people in the U.S. are taking a careful look at these things, as you would expect them to do.

Mr. KIRK. And so you have called Goldman and said, "What is up?"

Secretary GEITHNER. I am not going to comment on anything we have done specifically, but I just will draw your attention to the statements made by the chairman of the Federal Reserve Board and by the SEC, who are the competent authorities in this case, that they are going to take a careful look at this stuff, again, as you would expect them to do.

Mr. KIRK. Okay. Yeah.

As Treasury Secretary, you oversee much of the enforcement of the sanctions regime of the United States. We passed legislation in 1996, in the Clinton administration, to sanction any entity which invests more than $20 million in the energy sector of Iran. The Congressional Research Service has identified 25 companies that appear to have violated this.

We now learn that the U.S. Government has provided $107 billion to companies who are in direct violation, it appears, of the Iran Sanctions Act. We also understand that the Ex-Im Bank has extended $4.5 billion to entities which have directly violated the Iran Sanctions Act. Of the companies that have violated the act, 49 of them have no plans to suspend any activities in Iran.

Also, just a few blocks from your office, the World Bank is about to send $258 million to the finance ministry of the Islamic Republic of Iran. Since we own about 20 percent of the IBRD, that is 50 million U.S. Taxpayer dollars under the Obama administration that would be paid to the Ahmadinejad treasury.

We understand that Dalian Industrial made a $700 million investment in Iran oil refineries in direct violation of the act; that in 2009 the U.S. Army contracted $111 million with Dalian. Petrobras invested over $100 million in Iran oil. That is five times the trigger level of the act. Ex-Im Bank provided recently a $2 billion credit to Petrobras.

Mazda is in business with the Iranian Revolutionary Guard Corps and yet still is winning U.S. Government contracts using U.S. taxpayer dollars. Any updates on that?

Secretary GEITHNER. Congressman, let me just start by commending you for the support you provided for a more aggressive approach to implement existing sanctions, to strengthen those sanctions. I think you are right on that issue. And we are committed to working with countries around the world to put in place a stronger, more effective enforcement regime globally.

As you know, the activities of the Iranian Government on the nuclear front to support terrorists in the region and around the world are a substantial threat to our national security interests, to the interests of the countries around the region. And we are working very hard, the President is working very hard with the Secretary of State to build support for a stronger U.N. Resolution. We are working with countries to encourage them to more aggressively enforce the existing sanctions regimes. The United States is running a very effective program now to tighten those existing sanctions using the authority we have. And we are going to work to build on that record.

And, as you know, the Treasury plays a very important role on the financial side. And we have had remarkable success in making it much harder for those entities to get access to finance around the world because of the successful work with other countries to tighten up those sanctions——

Mr. KIRK. But no success in stopping U.S. taxpayer money going from companies who are directly violating, no success whatsoever. And I have raised this with you before: no success, no effort whatsoever to stop World Bank payments——

Secretary GEITHNER. No, no. Let me—I want to address—you know a lot about this, Congressman. And I know you have written to the Secretary of State about the concerns you began with, which are enforcement of the——

Mr. KIRK. Iran Sanctions Act.

Secretary GEITHNER [continuing]. Iran Sanctions Act. But let me just address the World Bank concerns directly.

As you know, the World Bank has approved no new loans to Iran since, I believe, 1985. There are only——

Mr. KIRK. No, that is not the issue. The issue is——

Secretary GEITHNER. You are right, you are right. I am coming to it.

There are only two loans outstanding where the World Bank is still disbursing. Those are two loans that go to water projects that are consistent with the humanitarian exemption that is under the U.N. resolution, permitted under the U.N. Resolution. These are modest——

Mr. KIRK. I am running out of time, but are you naive enough to think that the money paid——

Secretary GEITHNER. I don't have a naive bone in my body, Congressman, not a naive bone.

Mr. KIRK. Okay. Okay.

Mr. SERRANO. Can we let the man respond?

Secretary GEITHNER. I am saying that, as you know——

Mr. KIRK. Are you naive enough to think that $258 million paid from the World Bank to the Ahmadinejad treasury actually goes to those projects? Do you actually think that?

Secretary GEITHNER. No, what I am saying is that the U.S. has worked very effectively across administrations to make sure the World Bank was not authorizing any new loans. That has been successful policy of the government for a long period of time. The only two loans outstanding are these two loans permitted under the U.N. Resolution that go to support humanitarian and development projects.

Now, I just want you to know that we agree with you and share your objective of making sure we are working around the world, as we have been doing, to tighten the effectiveness of this existing enforcement regime. And you are right to point out that it is an ongoing challenge. You can't stay still. If you don't keep intensifying the sanctions regime, people will get around these existing regimes. They will be able to find new opportunities to exploit it.

But for us to be effective, we have to work with countries around the world to tighten up this net. And we are committed to that, and we are going to do it.

Mr. KIRK. I just would hope that this is—right now, given the New York Times article, it is less to do about what is happening with other governments and more that the U.S. Government stops contracting with companies that do business with Iran.

Secretary GEITHNER. That I wouldn't agree with. But I think, again, we have more in common on this than we may have on many other issues——

Mr. KIRK. Okay.

Secretary GEITHNER [continuing]. Which is, you are right to underscore the importance to our national security.

Mr. KIRK. Yep.

Secretary GEITHNER. But the critical thing for us to do is to make sure we are not just using our authority that Congress has provided to tighten up these sanctions, to make sure we get other countries to move with us, as they are doing on a—I would say we are having some impact now, and it is get getting some traction.

Mr. KIRK. Thank you, Mr. Chairman.

Mr. SERRANO. Thank you.

There is no way—no reflection on you, Mr. Secretary—there is no way that Mrs. Emerson and I can pass up this moment just to note that, if any of those folks had invested $2 in Cuba, it would be a major scandal throughout the country.

Mr. Schiff.

Mr. SCHIFF. Thank you, Mr. Chairman.

Thank you for being here, Mr. Secretary.

I have questions, really, on two different areas. The first is the proposal of the President to use some of the TARP funding to encourage small banks, community banks to lend to small businesses. I would like to know what the status of that is and what conditions or measures can be put in place to make sure that the small banks don't simply hold on to the money.

I have heard—well, we have all gotten unstoppable feedback from small businesses in our districts that institutions they have had long relationships with, where they have perfect credit history, won't lend to them. They are arguing that the regulators—the banks will tell them the regulators won't let them lend. I don't know whether that is an excuse the banks are using or whether regulators really are putting on that kind of pressure.

I am also hearing feedback, though, that the small banks are saying, "Hey, you know, if we get the money, we will keep it, and we are not going to necessarily use it to lend." So in order to avoid some of the pitfalls that characterize the support for the big banks that didn't always turn around and lend it, what precautions have been put in place?

And the second question is on the jobs issue. This recovery so far looks different than prior recoveries. It has not been as robust, even though the GDP growth last quarter was encouraging. Still, the job numbers are sluggish. And I am interested to know your both sense of why the jobs aren't bouncing back as quickly as in prior recessions and what are the most significant things that we can do to stimulate that job growth.

Secretary GEITHNER. Excellent questions.

First, on small-business lending, we are proposing, really, four separate things to help address this problem. One is we have a series of well-designed, targeted tax measures that go directly to small businesses: expensing, depreciation, zero capital gains on new investments in small businesses, new jobs tax credit. The second is to expand substantially SBA's existing guarantee programs. A variety of specific proposals in the President's plan, and we think those would be very effective.

Those are important, but they are not sufficient. We are encouraging the supervisors—they are independent of the Treasury, but we are encouraging them to try to make sure they are providing a more balanced amount of guidance to examiners across the country so the examiners don't overcorrect and contribute unnecessarily to tightening of credit conditions that would hurt viable businesses.

In addition to that, we propose, as you said, a $30 billion small-business lending fund that would give capital to small community banks that commit to use that capital to expand lending. We designed this in a way that gives pretty powerful incentives to lend the money out. So if you increase lending to small businesses above a certain baseline, then we have reduced the dividend you pay the Treasury over time.

Now, our view is that is a pretty powerful package, set of proposals. And you can't be certain that small banks will take a dollar of capital and increase lending. But if small banks who could otherwise raise capital in a normal market can't raise capital, don't have access to capital, then they will cut lending. And that has a pretty negative effect on business access to credit. So capital is a very effective way of helping mitigate this problem.

Mr. SCHIFF. On that last point, though, what baseline are you using to measure whether they increase lending? And, also, do you buy what the banks are saying about the kind of regulatory strait-jacket they are in, or do you think they are using that as a fall guy?

Secretary GEITHNER. I think you said it right. You know, think of it this way: A bank has been doing business with a customer for 30 years. The bank made a bunch of other decisions with a bunch of other clients in the real estate area that cost it a lot of money, left it very exposed, not enough capital. It is going to have to cut back on assets and lending to survive. What do you say to your customer that has been a good customer for 30 years? It is easier to say that the supervisor is making me do it than to explain that I made a bunch of judgments that got me too exposed to commercial real estate. So I think there is a lot going on.

But, on the other hand, in every recession what happens is that there is a risk that examiners, after a period where in hindsight they look like they were too easy, tend to overcorrect. And so I think it is good that the leaders of our supervisors, bank supervisors across the country—and this is the FDIC, the Fed, the OCC, and the OTS—they need to make sure they are leaning against that tendency to overcorrect in a recession, because that can cause a lot of damage too.

Just briefly on the job front——

Mr. SCHIFF. Before you go, what is the baseline?

Secretary GEITHNER. Oh, I am sorry, the baseline. I believe—but I have to check and make sure I say this correctly—I think we leave it at the level in 2009. We have designed that in a way—we think that is a realistic baseline.

You know, the pipes, the parts of this financial system are still clogged. You can't force money through those pipes. We can't force banks to lend without taking a risk that the government ends up with too much loss and risk. But we think we have designed this in a way that would substantially increase the odds that we are really helping mitigate the small business credit problem, where it remains.

On the jobs front, you know, you won't have jobs without growth. Growth has to come first. There is always a lag. But I think most economists across the country would say we are on the verge now of seeing a sustained level of positive job growth for the country as a whole.

And I think the best story, looking back, of why unemployment increased so much and why job losses were so steep was just that you saw just shattering damage to business confidence across the country. People were just too scared to do anything, and they cut back just dramatically because of the fear that they faced a very long period of no demand for their products. And that is going to take some time to heal, but it is beginning to heal. As your colleague said, you are seeing the early signs now: hours increasing, temp employment increasing. And that should——

Mr. SCHIFF. One last short question, Mr. Chairman.

Does this recovery look different to you? GDP growth was greater than expected but still smaller than in prior recoveries, and the commensurate job situation has improved. Why do you think this looks different?

Secretary GEITHNER. I think, in many ways, growth came more quickly, stronger, and more broad-based than many people expected. In that sense, it is encouraging.

But because this is a recession caused by a long period of excessive borrowing, a huge overinvestment in real estate, a huge increase in leverage in the financial sector, there was no way that recovery was not going to be dampened by those basic forces. So, as households across the country save more, start to deduce their debt burdens, as the financial sector digs out of this terrible mess it was in, any recovery was going to face significant headwinds in that context.

So we are seeing, I think, the necessary, inevitable consequence of a recession that is borne in part of a very damaging financial real estate boom that was fed by excessive borrowing and lending.

Mr. SCHIFF. Thank you, Mr. Secretary.

Thank you, Mr. Chairman.

Mr. SERRANO. Thank you.

Mr. Culberson.

Mr. CULBERSON. Thank you, Mr. Chairman.

Thank you, Mr. Secretary. I heard you talk a lot this afternoon about the importance of bringing down the deficit, controlling spending, and I appreciate your saying those things. I wondered if you would tell for the record, could you explain how the creation of the Obama health care entitlement will help bring down deficits?

Secretary GEITHNER. I will be happy to do that. That is not the way I would describe the health reform plan, but I will be happy to describe and answer the question.

The CBO estimates, and they are the independent scorekeeper of the Congress, they estimate that the reforms that are in prospect now would reduce the long-term deficits, the 10-year deficit, and would substantially reduce the rate of growth in health care expenditures over the succeeding decades.

Mr. CULBERSON. Are you talking about the Senate bill?

Secretary GEITHNER. Well, I would say that you can take the Senate bill as with suggested changes that the administration put out a few weeks ago, but they are all in the same basic ballpark. You say a meaningful reduction in the 10 years numbers and a very substantial reduction in succeeding decades. And that is because, as you know, that the biggest driver of the long-term deficit is the rate of growth in health care expenditures. It is more important than, for example, the fact that our population is aging. So there is no path of fiscal responsibility that does not go through health care reform that reduces the rate of growth in costs.

Mr. CULBERSON. But the reductions they see in the future are all based on assumed reductions in health care expenditures in later years.

Secretary GEITHNER. Well, again, they are doing what they always do is they take proposals Congress is considering, and they quantify those estimates on future spending by the Congress. They are just doing what they always do.

Mr. CULBERSON. Right. And you recognize that those proposals entail 6 years of spending with 10 years of revenue.

Secretary GEITHNER. Again, I am not trying to characterize their proposal. What I said is accurate in their estimates of the——

Mr. CULBERSON. You are talking about the CBO?

Secretary GEITHNER. Yes, CBO. But again, the most important thing to point out, which I know you understand, is that if you care about the fiscal position of the United States, you are worried about those long-term deficits, there is no way to deal with that without reforming the health care system in a way that reduces the rate of grown in costs.

Mr. CULBERSON. Well, those of us on the fiscal conservative side are approaching it from the perspective of focusing on making health care affordable and portable so you can buy it across State lines and shop. I want to be able to buy coverage from my carrier in Arizona or Texas. That law needs to be changed. We need to focus on that, on medical malpractice reform to protect doctors from frivolous lawsuits has worked so successfully in Texas, on allowing small businesses to pool their ability to negotiate better rates together. We could do those things without—and bring down the cost of health insurance to make it affordable and portable. That is where, from our perspective as fiscal conservatives, the focus needs to be.

But I just have to tell you the credibility of the administration is not very high when you or the administration attempts to persuade taxpayers who are—you know, they pay attention, and they—it just defies common sense to believe that we can, as your proposals do, expand coverage to 20 to 30 million new people that will be brought into this new entitlement, which is clearly the mother—this is the mother of all entitlement programs.

Secretary GEITHNER. Congressman.

Mr. CULBERSON. You are going to bring in 20- to 30-million new people, and you are going to reduce deficits, and this is just not credible.

Secretary GEITHNER. All I am citing——

Mr. CULBERSON. It is just not credible.

Secretary GEITHNER. All I am citing is the estimates of CBO.

Mr. CULBERSON. Of CBO. Do you believe those estimates are accurate?

Secretary GEITHNER. Well, I think they are the best estimates we have. And again, they have the virtue of being a fair and independent arbiter, nonpartisan arbiter, of the proposals now working their way through Congress. So you can challenge those things, but those are the ones Congress will rely on to score your proposals as well as the administration's.

Mr. CULBERSON. We are, as you have said, in an unsustainable fiscal position, and I am as concerned as I know every one on this committee is, no doubt, that we would become Greece.

Secretary GEITHNER. There is no risk of that. That will not happen in the United States.

Mr. CULBERSON. We are spending money—as of June 1st we are running on the Nation's credit card. My office has calculated, and if you look at the available revenue as of June 1st this year, everything we spend beyond that point is borrowed money.

And it is a fact, and I have to say also in your opening remarks earlier, Mr. Chairman, if I could very quickly, we are kicking the

Bush administration. You can't just blame others for the scale of the deficit. The deficits that you inherited were way too high. I voted against virtually all of those major Bush spending issues. But this, Nancy Pelosi and Barack Obama have managed to spend over $2.5 trillion in about 1 year. That is just the big-ticket items. You spent more money in less time than any administration in the history of the United States. You have created more debt than any other administration in your budgets than any other administration in the history of the country, so it just isn't credible. You damage your own——

Secretary GEITHNER. I would be happy to measure our record on fiscal responsibility with the record of the previous 8 years. I will just give you one example. I was a career civil servant in the Treasury Department. I left the Treasury Department in 2001. At that point the CBO projected future surpluses of $5 trillion. Eight years later those surpluses turned into $8 trillion in projected future deficits.

I would be happy to compare the basic records of what we achieved in that period of time on fiscal responsibility with the record of the succeeding 8 years, and I will say, not to make a political point, it is just a fair thing. And I think the important thing to recognize is over that period of time, when we demonstrated as a country that we were able to produce surpluses, we saw a record of trong private investment growth, strong productivity growth——

Mr. CULBERSON. Because of tax cuts.

Secretary GEITHNER [continuing]. Strong growth in incomes.

No. In the——

Mr. CULBERSON. In the Bush administration.

Secretary GEITHNER. No, no. I was comparing the growth record of the previous 8 years. The growth record of the 8 years under the Bush administration did not compare favorably to the preceding 8 years. It was worse on growth, worse on any basic measure of basic returns, and, again, worse on the thing you care about a lot, which is on basic tests of fiscal responsibility.

Mr. CULBERSON. I am exceeding my time. The Chairman is being very gracious.

Secretary GEITHNER. We can't change the past. I know you voted against a lot of those proposals, but we can't change the past. And right now we need to stand together and admit that deficits matter, tax cuts aren't free. We have to pay for stuff we propose to enact, and we need to bring our fiscal deficits back down to a point where they are sustainable over time, and I look forward to working with you in how to do that.

Mr. CULBERSON. Thank you. We want to you live up to those words, that is all.

Mr. SERRANO. Mr. Crenshaw.

Mr. CRENSHAW. Thank you, Mr. Chairman.

Welcome back. I have two questions. One kind of has to do with philosophy of managing these assets, and the other is kind of a quick question about the tax collections.

You mention the TARP funds are being repaid quicker and in a greater amount than first thought. I think that is good news. I think we ought to do everything we can to maximize those dollars. But when you look at AIG, it seems to be, again, we are a majority shareholder, and so I guess we are involved in their decisions. And it seems to me I read they sold two life companies last week, $51 billion, which will go back to American taxpayers. That is good news.

But if the philosophy there is to sell off these assets, it seems to me sooner or later you will kind of run out of assets to sell. You will have a company that has kind of been downsized, and you wonder what kind of capability it will have to make any further payments. I think they have over $100 billion, and I think they paid back $15 billion maybe. So we are still on the hook.

On the other hand, when I look at General Motors, as I understand it, if you take General Motors, Chrysler and GMAC, we maybe gave them $80 billion, and I think maybe General Motors was about $50 billion of that. And then I read where you said we are probably going to lose $30 billion on General Motors' deal. But I guess it seems like if the philosophy there is to—GM has kind of reinstated some of the dealerships, they are increasing their sales, maybe their market share is going to increase. So you would think that is one way to deal with the situation. You would think if they become an ongoing entity, and grow, and increase sales, and increase market share, they will be even in a better position to pay back—you know, of the $50 billion, maybe they end up paying it all back.

So just help me understand the two different philosophies, because we must be involved in those decisions. Is it short-sighted on AIG? I am not asking whether we should have just broken it up early on, but we own it, and we want to get paid back as much as we can. And those are two different kind of case studies. Explain to me how it is working, how you think that works in the long run.

Secretary GEITHNER. Excellent question. It is a difficult judgment. The two basic objectives we try to balance are to maximize the returns to the taxpayer, minimize the risk of the loss to the taxpayer. And we want to, frankly, get out as quick as we can. Those two objectives will sometimes be in conflict, as you said. So we are going to try to balance them.

These companies where we are reluctant shareholders in these companies are dramatically in different positions, and the precise strategy is going to differ because of differing conditions. We are going to try to make sure we manage these in a way to minimize any risk of loss, maximize the achievable return, but we want to get out as quickly as we can, because we don't want to have the American Government involved in these companies a day longer than is necessary. So we will do it as quickly as we can, subject to that constraint that we don't want to leave the American taxpayer exposed to the risk of unnecessary loss in that case.

You are right to point out that we are making really remarkable progress. I would say the board of AIG is making remarkable progress in reducing the risk and restructuring the company in a way that is going to reduce the expected loss to the taxpayer very, very dramatically. They have come down dramatically in that period of time. We are still exposed to substantial risk of loss, as we are in the other companies. But we are going to be very careful in managing those in a way to balance those two basic objectives.

Again, I think we are being consistent in applying them, but where they differ is just because of inherent differences in the position of those companies and the opportunities we have to get out earlier.

Mr. CRENSHAW. Thank you. And the same question, just a brief question, I read in your testimony where there are going to be some new initiatives in terms of tax collection. You spend $250 million, which will—according to your testimony, that is going to bring in another $2 billion. Every time I read that, I can't help but kind of ask the question, how do know; how do you determine that spending $250 million on compliance is going to end up bringing you $2 billion? And then based on that, how do you decide, well, instead of spending $500 million, we get $400 billion, or up and down the scales.

I am just curious, because my colleagues know that from time to time Members of Congress use the so-called tax gap as like a piggy bank and say all you have to do, if you spend a billion, you get this. And I have always wondered are there any facts and figures to kind of verify that? And how do you decide to limit to $250 billion—$250 million to say that will get us $2 billion? And somebody says, well, gee, four times that would get you four times the money.

Secretary GEITHNER. I asked the same questions when we had an initial discussion with Commissioner Shulman about what makes sense in this area. I think what he will tell you, I think he told you when he was up here before, and I will be happy to provide in more detail in writing and answer that question, but what he said is that those are pretty conservative estimates based on experience over in the past of putting more enforcement resources in targeted areas to generate better compliance. I think they are pretty conservative. I have seen much higher estimates than that.

On the question which I asked, the same question, why not more? If the return is that high, then why not more? Part of it is just their judgment about this pace at which they can really bring on capable people to do this. There are some constraints on how quickly you can scale up those operations. We are trying to be relatively careful, given that we don't live in a world of unlimited resources, to do it in ways where we are confident you are going to see a high return. That is the best answer I can give, but I would be happy to follow up.

Mr. CRENSHAW. I appreciate that. You have stolen the ideas of all the Members of Congress, so we can't go talking about spending an extra $250 million to get another $4 billion. You kind of maxed out on that.

Secretary GEITHNER. The virtue of what your colleague just pointed out, which is CBO is the arbiter of the extent to which you can actually justify investments on some return like that. We don't get to decide; you guys get to decide based on those estimates.

Mr. CRENSHAW. Thank you.

Thank you, Mr. Chairman.

Mr. SERRANO. Ms. Wasserman Schultz.

Ms. WASSERMAN SCHULTZ. Thank you, Mr. Chairman.

Mr. Secretary, the work that you have been doing with the TARP funds and the Recovery Act funds is obviously starting to take hold. And we have that little pinhole of a light at the end of tunnel that we are going to hopefully, as the recovery funds continue to get out there in the next couple of quarters, we will blow a wider hole into the tunnel.

That having been said, I come from the State of Florida where the foreclosure crisis definitely puts a brake on the progress that we have been able to make, even with those TARP and stimulus funds out there. The data that I have seen nationwide is about 25 percent of all homeowners are upside down. In my State it is 46 percent, and in south Florida in particular it is 46 percent of all homeowners being under water. So the HAMP program, the Home Affordable Modification Program, is struggling because you have so many upside-down homeowners.

So can you talk about the hardest hit fund and how that is going to start to address the problem in a more effective manner? But specifically I mean, just to give you an example of the foreclosure crisis in south Florida, we have more than 97,000 foreclosures filed just in my 3-county area in the last year. I mean, we have got to get that turned around. And one of the most frustrating experiences that people will have is both with the HAMP program—and I hope that the hardest hit fund is going to fix this—is the banks just refuse to work with homeowners. They won't modify loans. They give them the runaround. I have dealt with constituents who spent months and months, willing constituents who can afford to make mortgage payments, but who the bank will absolutely not work with. So why not walk away? What is the point of continuing upside down?

Secretary GEITHNER. You are exactly right, and I agree with, I think, everything you said.

It is important to step back for a second and look back at what has happened over the past year. It is important to emphasize this before I respond directly to your question. When I think a year ago today, if you looked at expectations of what is happening in house prices in the future, people thought house prices might decline another 30 percent across the country. Instead we have seen more than 6 months of relative stability in house prices across the country on average for the first time. And that is very, very important to confidence, because houses are such an important source of economic security to many Americans.

The HAMP program, as you know, has provided very, very substantial cash flow relief to now 1 million Americans; 1 million Americans are now getting an average of $500 more a month in their pockets because of this program. It is not just that they are able to stay in their homes, but have very substantial reduction in their size of the mortgage obligations. This is a very large, very substantial tax cut. We are seeing very substantial increases in convergence to permanence, not as much as we would like still.

But you are right to emphasize that there is just a huge amount of pain and damage still across the country, not just in Florida. In Florida and the other States targeted by this initiative, it is still just devastating damage. Again, it is just fundamentally people who did not borrow too much, who are very responsible, just the victims of the broader collapse, irresponsibility of everyone else. And we have an obligation as a government and a country to do everything we can to help those people who we can legitimately help stay in their homes.

Now, this program targets five States where the problems are most acute, the combination of house price declines and high unemployment are most acute. We are providing substantial resources to help reinforce State efforts to experiment in assistance for the unemployed, for people who are under water, modifying mortgage programs, who want to support innovations at a State level, and maybe there are some lessons for that for other States nationally.

We are also looking at, and we are looking carefully at, a series of other enhancements to the existing program to try to reach more people who are unemployed, and to help deal with the substantial number of Americans still who are—because they are under water, as you put it, they have negative equity, can't refinance, can't sell their homes.

So we are looking at ways to try to reach more people, but it is very terrible out there still in the housing market, and it is very important that we keep working at trying to make sure we are reaching more people.

And I want to end which is to say that it is very important for the servicers across the country to do a better job at helping these people get help.

Ms. WASSERMAN SCHULTZ. But they are not.

Secretary GEITHNER. And again, the one thing we do that is very important is you can see now in the public domain every month very, very detailed numbers on how servicers are doing reaching these people. You can see how one bank is doing with another bank. And so they can look and see if their bank and their servicer is doing well or poorly. But I will just say my view is none of them are doing enough. They need to put substantially more resources in this program, and they need to do a better job of making sure they are reaching the people that we can legitimately reach with these programs.

Ms. WASSERMAN SCHULTZ. But mechanically how can we ensure that that happens, because I tell you, I stand in front of town hall meeting after town hall meeting where I have constituents legitimately stand up and say—we all do—legitimately stand up and say, we bailed them out; my bank wouldn't be in business anymore if it were not for the United States Government.

Secretary GEITHNER. Absolutely. That is why people are so angry about it. So we have a variety of things. We have a detailed second look to make sure people who are eligible are not being denied. We make sure that we have got teams of people to go into these servicers and take a look at how they are doing. We are trying to put enormous pressure on them to do it. And we are going to keep at that, because we have a long way to go, and they can do it dramatically better.

Ms. WASSERMAN SCHULTZ. Just one more question, Mr. Chairman.

I know you are going to be shocked I am asking a question about Cuba, but I feel a sense of obligation. In the last week or so, we had the tragic death of Orlando Zapata Tamayo, who was on an 85-day hunger strike, and who, along with the other dissidents, continued to protest the abuses of the Castro regime. I am particularly concerned about the prodemocracy efforts on the island and getting the funds that we have appropriated for the last 2 fiscal years to them.

What is being done to expedite the licensing process to ensure that direct assistance and aid is being sent quickly to those prodemocracy organizations? The money is sort of being sat on right now for the last 2 fiscal years, and I realize that we need to be careful, and that we need to make sure that they are going to legitimate dissident organizations and ensuring that there is a vibrant prodemocracy movement, but sitting in the Treasury in Washington isn't going to accomplish that.

Secretary GEITHNER. Congresswoman, I share your concern and would be happy to try to respond in more detail as to what we can do to be responsive to that concern. I would be happy to come talk to you and walk through that with you.

Ms. WASSERMAN SCHULTZ. That would be great.

Secretary GEITHNER. I know there are strong feelings on both sides of the debate.

Ms. WASSERMAN SCHULTZ. Especially in this room.

Secretary GEITHNER. Especially in this room. And we are doing our best to make sure we are enforcing the laws as written and we are meeting the objectives of the Congress.

Ms. WASSERMAN SCHULTZ. So you can follow up with me in more detail?

Secretary GEITHNER. Of course. As on the issue raised by any of your colleagues I will be happy to listen more carefully and make sure that we understand your concerns and see if we can meet them.

Ms. WASSERMAN SCHULTZ. I want to press you a little bit more, though, because there are funds that we have appropriated for the last 2 fiscal years that aren't being spent and——

Secretary GEITHNER. I am not trying to be unresponsive. I have to talk to my colleagues a little more to understand exactly what it is.

Ms. WASSERMAN SCHULTZ. The article that I just read the other day talked about how your Department is making sure that there are safeguards put in place and that we have the accountability measures, but it is an extraordinarily long time to be examining that.

Secretary GEITHNER. We have careful people, and their obligation is to make sure they are implementing the law and following the intent of Congress. I am sure that is what they are doing, but I will take a careful look at it.

Ms. WASSERMAN SCHULTZ. Thank you very much.

I yield back, Mr. Chairman.

Mr. SERRANO. Thank you.

Mr. Secretary, as I noted in my hearing with IRS Commissioner Shulman a couple of weeks ago, I am concerned by several proposed cuts to programs that provide important services for low-income and working families, including the Volunteer Income Tax Assistant Grant program and Tax Counseling for the Elderly program. Do you believe that these cuts reflect the appropriate priorities as we struggle to recover from the economic downturn?

Let me just say, the IRS, similar to the immigration department, it seems that some of those agencies, not that they have bad reputations, but they have a lot of people complaining about this all the time. And so when I saw the IRS begin to move in this direction, I said, what a wonderful way not only of helping people, but also helping the image of the agency, because now you are going to assist those who need help with those forms and everything else. So in terms of is it a real savings, in that budget, because of the message that it sends out that the people who need help the most are going to be cut out.

Secretary GEITHNER. Mr. Chairman, I understand your concerns, and I would be happy to listen to those concerns in more detail. The Commissioner and I both believe that these are sensible proposals because they help us to increase resources we are providing to improve taxpayer servicers more generally. And we think that will help the same people that these programs help.

But I would be happy to talk to you about it in more about detail. We are making difficult choices trying to make sure how we are using scarce resources as effectively against these things, and we are proposing very substantial increases in programs to improve taxpayer services generally, and we think that will help reach some of the same people that these programs you refer to are designed to reach.

Mr. SERRANO. Right. But these programs were created with the intent of both helping and showing that there was a desire to help. One is not necessarily the same as the other, but they both can work towards the same goal. So aren't you concerned about the message you are sending at the very time that the IRS was beginning to gain, I think, more respect from the public?

Secretary GEITHNER. The IRS is going to continue to work very hard to do the right thing and earn the respect and confidence of the American people. One way they can do that is to make sure they are working very hard, and we are giving them the resources they need to improve service, to make it easier for Americans to meet their obligations. That is an objective that the Commissioner and I both share. And the Commissioner has done a very, very good job in helping improve the record of service IRS employees do.

But again, Mr. Chairman, I respect your concerns and understand your concerns. I appreciate your support for those programs, highlighting their benefits, and we will work with you to make sure we come up with the right balance.

Mr. SERRANO. Okay. Because, you know, if this was a course in legislative politics 101, the professor would say, you shouldn't come before Serrano cutting these programs; it is not going to do well. And I suspect there are other folks on this panel who feel the same way, because this is one statement we can make on behalf of a community that needs help.

Let us talk about the tax gap. How big do you think the overall tax gap currently is, and how much do international activities account for that? Where are the best opportunities for closing the tax gap?

Secretary GEITHNER. We put out a very detailed report last year that went through the latest estimates of the size of the gap and the sources of that gap. As you highlight in your opening statement, the President in his budget has proposed a variety of ways to help make some progress reducing that gap. One of those proposals is to reform the tax treatment of overseas earnings of American companies. And the basic premise that underlies that proposal, just to make one specific example, is if you have two companies in your district, one invests overseas, one invests in your district, you don't want them facing different tax treatment. You don't want the Tax Code to create incentives to shift investment of jobs overseas. So we propose some changes to the program that would help address that issue.

There is a range of proposals to the President's budget that we think are making headway. We are making a lot of progress, not just with Switzerland, but a range of countries around the world, to reduce opportunities for evasion, and we are committed, and we are going to keep at it. But the report that we laid out last year we have to provide the committee again is a very good, detailed analysis of the sources, principal drivers of the gap and the policies that we think would have the highest return in starting to close that gap.

Mr. SERRANO. Well, before I turn it over to Mrs. Emerson, let me ask my question—she will ask one, too—and make my one comment that you don't have to respond to.

So much of what we discussed around Cuba is helping people inside Cuba oppose the government. For all intents and purposes, that is what it is. I often wonder how would we react to a foreign government funding groups here to oppose our government. Even during a government I didn't like, I would be a little upset, but anyway that is another issue.

Last year the Department followed the lead of this subcommittee and allowed travel to Cuba by Cuban Americans visiting their families. The Department is also implementing an appropriations provision that partially relaxes the terms under which payment may be received on exports of agricultural and medical goods to Cuba. Mr. Secretary, please update us as to how implementation is proceeding with respect to these two areas of U.S. transactions with Cuba.

Secretary GEITHNER. I can't do that justice in the hearing today, but I am happy to do it in writing. My sense is that it is going reasonably well, but, of course, open to other perspectives, and happy to try to respond to any specific concerns you have about how we are implementing. I would be happy to respond in detail in writing.

Mr. SERRANO. Then we will hold you to that, and we will ask you to write to us and tell us what is going on.

And with that I turn to Mrs. Emerson.

Mrs. EMERSON. Thank you, Mr. Chairman.

Mr. Secretary, looking back at the financial crisis, I, like all my colleagues and many Americans, are very upset with the lack of regulatory oversight that led to the climate in which our entire financial system was undermined. Our small banks in Missouri survived pretty well, we are tough and have got some good people, but life still isn't getting a lot easier for them.

The burden of bank foreclosures falls entirely on the banks that survive this crisis, and as surviving banks continue to do their best to serve their customers, I do hope the Treasury and FDIC will give every consideration to fair descriptions of the risks they face and the Deposit Insurance Fund assessments that are based on those measurements of risk.

And I also hope that, looking at the ultimate analysis of the financial crisis, something would be done in the future to perhaps allow FDIC to get more involved with or perhaps offer guidance to American banks who they identify as actually facing increasing risks. Perhaps by putting the bank back on the right track, we could limit the number of banks that must close their doors. Obviously the number of customers who have to turn to the Deposit Insurance Fund to be made whole, and a very obvious lack of consumer confidence in financial products.

My real question focuses on one enforcement aspect of this matter. Do you all look at the financial statements of failed banks to see if they misrepresented their financial conditions, if executives took unreasonable compensation or bonuses out right before the bank failed? Can you all at Treasury claw back excessive compensation from such a bank? Because obviously the alternative is the Deposit Insurance Fund ends up making up the difference when they try to make depositors whole. And I think there is a Senate effort on this, but I am just curious if, in fact, you can claw back under those certain circumstances.

Secretary GEITHNER. Congresswoman, I think I am correct in saying that—I will correct this if I get it slightly wrong—which is in the Recovery Act I believe that Congress passed a series of provisions to provide greater constraints, encourage reforms in executive compensation in institutions that took financial resources from the government. As part of that, if I am not mistaken, the government was given the authority to claw back compensation if there was clear misrepresentation of financial data.

But I will take a more careful look at the way the law is written and will be happy to respond in more detail in writing. It is a sensible provision, and I will fully support that basic objective.

We are trying to make sure we are bringing about fundamental reform and compensation practices across the finance industry because we want to make sure in the future that we don't see a repeat of the set of compensation practices that provided huge returns for taking lots of risks and no exposure to the downside.

Mrs. EMERSON. I appreciate that, and I will be grateful to get a written response from you.

Let me ask you about too big to fail. Five banks control 80 percent of U.S. deposits, and I guess that wins them the moniker of too big to fail.

Secretary GEITHNER. Well, not—okay, keep going. I am sorry.

Mrs. EMERSON. No. Am I incorrect that five banks control about 80 percent of U.S. Deposits?

Secretary GEITHNER. No, keep going. I will be happy to give the details. I think that is a little high, but it may not be. I am going to support your concern so——

Mrs. EMERSON. So the financial crisis pretty well proved that "too big to fail" is a misnomer without the guarantee of huge amounts of capital from the U.S. Government. If we keep borrowing money at the present rate, we may even test the hypothesis of whether the U.S. Treasury is too big to fail.

Let me ask you, is it good to have institutions like these dominating the American market for savings? It makes me think about the old Ma Bell, if you will, which was disassembled in 1984. Could you unwind those big banks that are too big to fail without government taxpayer assistance?

Secretary GEITHNER. Critical issue, critical test of the financial reform plan and whether we fix what is broken, whether we address this problem of too big to fail, you can't have a financial system where the management of the firm, the boards of directors and the equity holders expect the government to come in and save them from their mistakes in the event that that they manage themselves to the edge of the cliff, as we saw happen for so many institutions in this crisis. So that is something that we have to fix and end.

The only way to do it is to make sure first that you have the ability and the authority to constrain risk taking by those institutions ahead of the fall. That means much more conservative capital requirements; constraints on risk taking applied more effectively, more evenly across those institutions. That is necessary; it is not sufficient. You also want to make sure that if they get themselves to the point where, again, they can't survive without government assistance, you want to make sure the government has the ability, and the tools, and the authority to take them over temporarily, break them up, wind them down, sell the businesses off, and make sure the taxpayer is not exposed to risk of loss.

This is the third thing that is important as we proposed this just to make sure that if the government is exposed to any risk of loss in doing that, they will recoup that loss in the form of a fee applied to the financial system over time, as we have proposed in the President's proposed fee on banks.

So you need the ability to limit risk taking ahead of the crash, you need to prevent the future crisis, but in the event that companies are able to still mismanage themselves, in addition the ability to step in and put them through a kind of quasi bankruptcy regime and do that in a way that doesn't leave the taxpayer exposed to any risk of loss. Those are the kind of things. We cannot do that today with the existing authority the executive branch has. We need financial reform do that.

Mrs. EMERSON. No, I understand that, and I appreciate that. I guess what I am saying is—and perhaps you don't want to directly answer my question, and I won't be offended if you don't, which is if we had to take apart those banks today, would we have to use taxpayer funds to do so?

Secretary GEITHNER. Well, I don't—I am not trying to——

Mrs. EMERSON. If we had to unwind those big banks.

Secretary GEITHNER. I may say it differently, but I am being responsive to your question, which is right now—and this is a tragic failure of the Government of the United States. We still do not have the authority to deal with the potential failure of a major firm, a future AIG. We don't have that today. And we can't fix that without legislation to give us the authority to do that. So if we get that legislation, then we can meet your test, and we have the ability to manage its failure safely without leaving the taxpayer exposed to risk of loss or a bunch of innocent victims across the country exposed to the collateral damage caused by their failure.

Mrs. EMERSON. The analogy with Ma Bell just to me rings pretty true, because back in 1984 the Congress said, hey, this is anti-competitive, and let us just go ahead and break it apart. So, to me, five banks having—you know, even if it is close to 80 percent to me is a monopoly, and I obviously don't think it is healthy for this country.

And I say that, too, because I don't even know if one of these banks failed, I don't know even if the FDIC would be able to handle the enormous liabilities of deposit insurance. I don't think they could.

Secretary GEITHNER. Again, I am agreeing with you, which is that a critical imperative of financial reform is to make sure we have the tools and authority to do it, just what you said, manage failure safely without the taxpayer being exposed or a bunch of innocent businesses, families across the country being exposed to the collateral damage of their failure.

Mrs. EMERSON. Well, instead of even allowing banks to become too big to fail, perhaps we should give someone the authority to——

Secretary GEITHNER. To limit their risk taking, that is right. You read this in January. Right now we have a cap on the share of the Nation's deposits any individual bank can hold. That is a necessary constraint, it is a good idea, it is a good thing for just the reasons you said. But it has this following effect which is unfortunate, which is you can become bigger over time as long as you fund yourselves with other sources, nondeposits, more risky sources of funding. It is a well-designed constraint, but it has the effect of still allowing size and concentration, but in more risky forms. So we propose to complement that cap with an additional cap on total size so you don't have a level of excessive concentration, consolidation in the industry over time.

Again, just for some perspective, we have a system of 9,000 banks in this country, and a great strength of our system is that not only do we have a set of large institutions operate globally, much stronger position today than they were 2 years, 3 years, 4 years ago, but we have 9,000 banks across the country meeting needs in their communities, and that provides a great source of competition, resilience. We very much want to preserve that.

Mrs. EMERSON. I appreciate that.

Mr. Chairman, I have to leave for about 20, 30 minutes, so I will be back. Thanks.

Mr. SERRANO. Mr. Fattah.

Mr. FATTAH. Thank you, Mr. Chairman.

Mr. Secretary, I just want to deal with some issues that have been raised. First of all, I heard the Greece Finance Minister yesterday on CNBC. He was asked about this question about Goldman Sachs, and what he said was that the activities that Goldman Sachs was involved in were perfectly legal at the time, and were part of the interactions that were taking place on behalf of a number of countries. And I don't want to have on the record allegations without any opportunity for a response, because I am actually appreciative of Goldman's efforts in another regard which I am moving to now, which is on the small business lending side. They have taken some $500 million and created a fund to try to aid in providing credit to small businesses. And I appreciate along with the point that you made earlier about Bank of America's decision on the debit card overdraft charges.

You know, I think we ought to be careful as we go forward that we delineate where appropriate criticism should be levied and where it shouldn't be.

But I wanted to get to a couple of points. One is we have had a number of dialogues over mortgage foreclosure. The program that I created in Pennsylvania, the HEMAP program, the Housing Emergency Mortgage Foreclosure Program, which is run through our housing and finance agency, which provides actual relief in terms of payment of mortgage payments for people who are unemployed by no fault of their own, it has helped over a couple of decades tens of thousands of families in our State, and you know as well, just putting it on the record, at no loss to the taxpayers because it then tags onto the back end of the mortgage, you know, those payments or as a small percentage of ongoing mortgages. So there has been no loss, it has worked very well, and we have had a moment in time in which many of these mortgage foreclosures were because of lending practices.

The vast majority of foreclosures that we face now are related to unemployment, and there is no ability for someone who is unemployed to pay mortgages. And if we want to keep them in their home, there has to be some effort. That is why I am so happy that the House agreed with me and we passed some $3 billion in the reform bill that you complimented us on earlier in your statement, and you urged the Senate to act.

I hope you are also urging the Senate to keep the 3 billion in place. I was very pleased to see the billion and a half provided to what were determined to be the hardest-hit States. Now, States are a geographical place, but they are hardest-hit ZIP codes, and there a lot of ways we could delineate where people need the most help.

But I am for helping taxpayers who have been law abiding, and who have been hard working, and who saved enough money to buy a home and were making their mortgage payment. They lost a job because of a recession that they have had no fault in. For us to take, on the other hand, tens of thousands—I think it is close to $90,000 it costs the taxpayers—to foreclose on their home when we could intercede to help, and we have a record of doing that in Pennsylvania to the tune of an average of about $6,000 a family, we would have been able to maintain people in their homes, not ruin their credit rating, not destabilize neighborhoods.

So I just wanted to mention again and put it in the record and ask you both to comment on that, and to comment on in this new lending effort for small businesses, whether or not credit unions and CDFIs are quasi public entities in cities like Philadelphia may also be involved, because there you will get actual lending. You won't have to worry about the question of how much they keep for capital and how much they lend out. They are in the business of lending. So I would like to have your comment on that.

Secretary GEITHNER. I have heard great things about the program you described, and everybody who has talked about it——

Mr. FATTAH. It is all true.

Secretary GEITHNER [continuing]. Says what you say, which is that it has a very good record, very good experience. And I compliment you for the design of it, and it is a good example of how initiative at the State and local level is a good thing for us to encourage and incent and reinforce. We have supported, will support the efforts you described in the House bill to provide a little bit more oxygen resources for those programs.

You were actually right that one of the most effective ways you can get small business lending to increase in communities where credit was still starved for credit is through the CDFI program. And we have, as you know, not just put substantial additional budget resources into that program, into the New Market Tax Credit program, but we announced recently that we would give capital to—we would provide a program for CDFIs to get capital from the Treasury at very attractive dividend rates, and I think it is going to be a very effective program. And we are putting that in place right away. That is under the TARP for them to come. And we think that would have a very good return in communities where typically what happens is investment dries up quickest, credit flees most quickly, it comes back latest.

It is a very good economic case, I think, for trying to make sure that we are getting resources targeted to those community institutions that can do a good job. You and I were in Philadelphia together, I think, just a couple of weeks ago highlighting one example of that kind of program. We are very committed to that.

Mr. FATTAH. Yes. Last question on commercial real estate, which is not new, but the challenge of the greatest, I think, concern in the horizon now. And I know of instances in Philadelphia, I assume they are not isolated, where you have commercial real estate mortgages that have been paid, that are vanilla deals that have, you know, no issues versus hardship cases. I am not talking about hardship cases—but where you have vanilla deals, and these deals are still being yanked. Is there any thought yet about how we might go about not having a run of foreclosures where we don't have to have them on the commercial side?

Secretary GEITHNER. It will still be a big challenge, I think, the commercial real estate challenge. It is going to take a while to work through this problem. We have put in place a series of programs that I hear you are familiar with to help ease that adjustment process, but it will still be very difficult.

Again, one of the reasons why we proposed this Small Business Lending Fund is to make sure we are getting capital to small community banks that are still the most hardest hit by what is happening in commercial real estate. But we think that mix of programs to get capital to banks who need it and to support efforts to get the securities markets more liquid again is the best thing we can do to ease that transition. I would be happy to talk to you in detail.

Mr. FATTAH. I have an idea, and I would be interested in dialogue in what we might be able to do in that area.

Secretary GEITHNER. Mr. Chairman, I want to end where the Congressman began, which is that I think it is very important to recognize that, of course, banks are different, not all institutions were the same, but I would say across the American financial system you saw banks and finance companies doing things that caused a dramatic loss of trust, of confidence in the American financial system. And I think that they all need to work much harder to earn back the trust and confidence of their customers, of the American investors, and of people around the world in the American financial system. I think they have got a long way to go, and I would like to see them all doing more to help restore basic trust and confidence in their customers, in the American people.

You highlighted some examples of things people have done, but we can see a lot more of it. They have a lot more to do. One thing they can do is try to help make sure that we get financial reform passed that puts in place a level playing field of strong protections, deals with the too big to fail problem. That is a good thing for the country and, I think, a good thing for the future of the American economy. And I think it is a fair thing to ask them to support, and we are hopeful they will work with us to get a strong package of reforms in place as the House has already passed.

Mr. FATTAH. With my $3 billion emergency mortgage foreclosure intact.

Mr. SERRANO. So far you have proposed seven bills. I like it.

Mr. FATTAH. This is already passed by the House, the Wall Street reform bill.

Mr. SERRANO. The other one is already on the way.

Mr. FATTAH. And the Secretary promised a rigorous examination of this idea, pros and cons.

Secretary GEITHNER. You said to tear apart, but we will do a careful balance.

Mr. FATTAH. I think any idea should be able to withstand analysis.

Mr. SERRANO. Thank you.

Mr. Culberson.

Mr. CULBERSON. Thank you, Mr. Chairman.

Mr. Secretary, the bailout bill which passed in the last months of the Bush administration, which I voted against and strenuously opposed, did contain language that had a requirement that TARP money repaid to the Treasury be used for deficit reduction, which I wanted to ask, do you agree that is important?

Secretary GEITHNER. Oh, absolutely. Again, the important thing to recognize is that we have now taken back, replaced with private money, more than two-thirds of the investments that my predecessor had to make, and he did the right thing. They were the necessary things to do, but we have now gotten back more than two-thirds of that, I think more than $170 billion of the American people's money, and that, under the law as written, that goes to reduce our deficits and our debt.

Mr. CULBERSON. And should not be reallocated?

Secretary GEITHNER. Again, Congress, under the laws of the land, can decide what it does with the resource here, but we saved substantial resources for the American people and would like to work with you and make sure we are devoting those to the right priorities for the country. And, of course, we face these two priorities now, which is getting this economy back on track and digging out of that fiscal hole we inherited.

Mr. CULBERSON. Oh, wait, wait, wait, no. You inherited somewhat—you inherited a fiscal hole.

Secretary GEITHNER. That is right.

Mr. CULBERSON. But I want to go back to that, but you dug the whole three times deeper.

Secretary GEITHNER. No, no, no. That is absolutely not true, Congressman. You know the facts in this is that when we came into office——

Mr. CULBERSON. You dug the hole much deeper.

Secretary GEITHNER. No, no, no. All we did was try to rescue an economy that was in collapse, a financial system at the edge of failure. We did that in the most careful, effective way we could, and those actions, as you have seen, have had a very substantial effect in restoring growth.

Mr. CULBERSON. Set aside whatever your intent was in spending the money, it is a fact that the annual budget of the United States in 2007 with about 1 trillion, in 2008 was 1.1 trillion, in 2009 was 1.2 trillion. And yet in a little over 12 months, 13 months that the Obama administration has been in office, your administration and the Pelosi-Reid-led Congress has managed to spend—in the course of a single year, you signed $3.3 trillion worth of new spending into law. You spent more money.

Secretary GEITHNER. I would be happy to go through it.

Mr. CULBERSON. More than any Congress in the history of the United States, and it just defies common sense for this administration to pretend that you are paying any attention at all to deficit reduction.

Secretary GEITHNER. No, no. Again——

Mr. CULBERSON. In any way it just doesn't square with reality.

Secretary GEITHNER. Congressman, faced with the worst economy in generations, the President and Congress acted. If we had not acted, the economy would have fallen off the cliff. Growth would still be declining. Our deficits would be larger. If you care about fiscal responsibility, there is no way you could have argued that the response for the government should have been to stand back, let this economy collapse, let it collapse. That would have been far more costly not just to the fiscal position of the United States, but to the fortunes of average Americans and businesses across the country. There is no fiscally responsible strategy in a crisis that would have justified standing back and not acting in that context.

Mr. CULBERSON. Let us set aside the bailout, because that happened under the Bush watch, and that is the principal mechanism I am sure you are referring to.

Secretary GEITHNER. No, no. I'm referring——

Mr. CULBERSON. The stimulus bill, $787 billion; the omnibus, $439 billion; the supplemental, $105 billion; consolidated appropriations bill, $446 billion. The level of spending is unprecedented. The level of debt that you have asked our kids to pay off is unprecedented.

Secretary GEITHNER. No.

Mr. CULBERSON. The level of deficits is unprecedented.

Secretary GEITHNER. Again, Congressman——

Mr. CULBERSON. And it is really important that we want you to live up to what your words are——

Secretary GEITHNER. The great thing about this country, Congressman——

Mr. CULBERSON [continuing]. And we have not seen it.

Secretary GEITHNER. The great thing about this country is we get to debate what makes sense for the American people. And you can look at the actions that we proposed, Congress enacted, and said you would have preferred we do nothing, or preferred that more of it come in the form of tax cuts or other things. But we put in place a set of well-designed, targeted measures that were absolutely essential to break the back of the worst economic crisis in generations, and we are at the beginning of the process of healing the damage it has done.

But I completely agree with you that we have to recognize, make sure the American people understand is we are going to have to dig our way out of this hole.

Mr. CULBERSON. By spending more money.

Secretary GEITHNER. No.

Mr. CULBERSON. But that is what your approach has been.

Secretary GEITHNER. Again, in this budget, the President's budget proposes specific measures on the tax side and the expenditure side to bring our deficits down dramatically as a share of our economy over the next 4 years.

Mr. CULBERSON. You agree all the Bush tax cuts should be allowed to expire and therefore——

Secretary GEITHNER. No, that is not true. We propose to allow——

Mr. CULBERSON. Your budget proposes.

Secretary GEITHNER. As Congress legislated, we propose to allow that tax cuts on the most fortunate 2 to 3 percent of Americans to expire as scheduled in 2011. Now, we have also proposed a freeze on nondefense discretionary expenditures for 3 years. We have also proposed some other measures to cut spending over that period of time. And again, some of those proposals will cut our deficits to below 4 percent GDP in 4 years.

Now, you may propose different ways to do it, you may propose more aggressive ways to do it at a period of time, but the basic imperative we all share is to recognize, as I think you do, that deficits matter.

Mr. CULBERSON. Yeah. I appreciate your vigorous defense of the administration's proposals, but this is why the country is so upset, because what you say doesn't square with your actions.

Secretary GEITHNER. No. You can measure it by exactly what we are proposing.

Mr. CULBERSON. You have spent more money and less time than any Congress in any administration in history, you have driven the deficits to unprecedented levels, and you are trying to sell a bill of goods to the country claiming that you are going to create the mother of all entitlements, insure 30 million more Americans, and we are going to save you money. No one believes that.

Secretary GEITHNER. Again, I don't expect you to agree. Again, the great thing about our country is we get to have a national debate on what makes sense for the country.

Mr. CULBERSON. That is true, and that is why the November election is going to be a tidal wave.

Mr. SERRANO. Thank you. And everything that went wrong started on January 20th of last year.

Mr. CULBERSON. Oh, no. I voted against——

Mr. SERRANO. You are going to get a chance on the House floor to pull us out of Afghanistan, which is going to cost a couple of trillion dollars. Let us see how fiscal conservatives vote on that.

But I must take issue with something, you threw into the package the omnibus bill.

Mr. CULBERSON. Yes.

Mr. SERRANO. Well, if I recall, that was the regular appropriations bills that we have to constitutionally pass every year.

Mr. CULBERSON. That is right.

Mr. SERRANO. I guess you were saying that we should have shut down government.

Mr. CULBERSON. I had a problem, Mr. Chairman, with the 85 percent increase in nondefense discretionary spending over the course of the last 2 years. That is what worried me.

Secretary GEITHNER. Mr. Chairman, could I just say one thing? This is fun for both of us.

Mr. CULBERSON. It is. And we are enjoying this. And my Chairman and I, we get along very well. That is what makes it a great country, friendly debate.

Mr. CULBERSON. I agree.

Mr. SERRANO. But actually in all honesty, with all due respect to both of you, this is quite an accomplishment. He did not blame anything on immigrants today.

Secretary GEITHNER. Congressman, I want to point out one thing about this, because I think it is important for you to recognize. In the President's budget we proposed to leave nondefense discretionary expenditures—this is sort of the measure of the discretionary government—4 years out at the same level in real terms that we inherited at the last year of the Bush administration. So we are proposing enough restraint to make sure these temporary things we did to save the economy from collapse go away, and that we bring ourselves down to a size of government, taking out defense and security, that is where it was in real terms when we came into office.

Mr. CULBERSON. Four years from now.

Secretary GEITHNER. Yeah. But we are going to get there. If you would like to get there overnight, I would be happy to work with you on that. But we are going to try to get there in a—by restraining expenditures in a way that is careful and balanced and allows us to come out and heal the damage caused by this crisis.

But anyway, I respect you, I am glad you are here. You are making the rigorous case for fiscal responsibility. We need to have more people do it. It is a good thing for the country.

Mr. CULBERSON. Mr. Chairman, you will enjoy this. May I ask one quick follow-up, with your permission?

Mr. SERRANO. Yes, in your 11th minute.

Mr. CULBERSON. Do you still have the Zimbabwe bank note in your wallet you showed me?

Secretary GEITHNER. No, I don't carry my wallet anymore, but I am glad you raised that again, because I remember that exchange from last year. But I remember, as you recall, you showed me the pink version, but I had a better one.

Mr. CULBERSON. I had a $50 billion bank note, Mr. Chairman, from Zimbabwe, and I was very impressed the Secretary a trillion, I think, dollar.

Secretary GEITHNER. Ten trillion.

Mr. CULBERSON. Ten trillion dollar bank note from Zimbabwe. And we are ready to help you get those deficits under control and balanced.

Secretary GEITHNER. We welcome that. And again, it is good for people like you to try to make the case for the country that deficits matter, and I am glad to hear you say it.

Mr. CULBERSON. Thank you.

Thank you, Mr. Chairman.

Mr. SERRANO. What I know about capitalism, what I learned about capitalism is that every so often you have to invest to make things happen. And banks and other folks were not investing, and so government invested some. I think at the end of the day we will get a good return.

Mr. Secretary, on March 4th of last year, you stated that the administration had laid out a clear path forward to helping up to 9 million families restructure or refinance their mortgages to a payment that is affordable now and into the future. Unfortunately the latest Treasury report on this program showed that only 116,000 homeowners have received permanent mortgage relief. The result has been that millions of homeowners have been forced out of their homes through foreclosures on short sales.

Can you take a moment to please explain what happened between your optimistic forecast and the reality of what has instead occurred?

Secretary GEITHNER. The program we announced initially to help modify mortgages for a set of Americans facing the risk of losing their house, we thought over time it would reach perhaps up to 3½ million Americans. Now, that program in its initial 8-month life has now provided very substantial cash flow relief to a million families across the country, as I said, on average $500 less, almost $600 in lower monthly payments to reduce their mortgage obligations.

Now, we are seeing a substantial number of those, less than we would like, converted to permanent modifications. But the number that matters now is a million. The million is growing. We are going to reach as many as we can.

Mr. SERRANO. So what was the 116,000?

Secretary GEITHNER. That is the number of permanent today. But remember, when you get a temporary modification, your mortgage obligations get reduced substantially right from that point. Now, of course, we want to see people eligible for permanent modifications get permanent modifications. And it is now a million families across the country, they are seeing an immediate, substantial, sustained reduction in their mortgage obligations so that they have a chance of staying in their homes. And, of course, we are going to make sure we are reaching as many people as we can. That number is still growing, and we are going to make sure that as many of those temporary modifications are converted into permanent as possible. We are committed to doing that. We are seeing those numbers start to increase dramatically. They are not getting there fast enough, but we are going to keep working on that.

Mr. SERRANO. Okay. Then can I make a suggestion and ask you to issue yet another report that tells us what you just told us so people don't rely on the other one that they know.

Secretary GEITHNER. Absolutely.

Mr. SERRANO. Because I am asking my question based on that information.

Secretary GEITHNER. Absolutely. Well, we did not claim, Mr. Chairman, that we would reach 9 million Americans through that program. We thought as it was originally designed, it would reach up to 3½. We may not reach that target, but that was going to be over a 3-year period of time. And so the architects of this program say we are on track to hit those original objectives, but we are going to do as much as we can to make sure we again reach as many people as we can.

Mr. SERRANO. Okay. In the 2011 budget proposal for the CDFI fund, you propose zeroing out two existing programs, the Bank Enterprise Award Program, which provides assistance to banks that have demonstrated increased lending activity in low-income neighborhoods, and the Capital Magnet Fund, which provides competitive grants for constructing, preserving and rehabilitating or acquiring affordable housing in low-income neighborhoods, as well as other economic development projects in communities where the housing in question is located. Would you please explain why the administration made the decision not to request funding for these two programs?

Secretary GEITHNER. As you know, as appropriators know, governing requires making choices among competing priorities with scarce resources. So what we did, which I think you need to expect us to do, is to take a careful look at all these programs and make sure we are allocating resources where they have the highest return. And we, after careful reflection, with the knowledge that many people like these two programs we proposed to cut funding on, we decided we thought those resources would be better used in supporting the signature CDFI program which has so much support across the country. It has such a good record of success. So the simplest way to say it is we took a careful look, and we thought those resources would be better used in support of the signature CDFI program.

I think that I am confident that is the right judgment. But again, we are making choices and trying to demonstrate to you that we are going to use the resources you allocate to us carefully, and we are prepared to take a careful look at programs that, even if they help, may not provide high enough return for the resources we are providing.

Mr. SERRANO. Okay. But just for the record, it doesn't sit well with me and, I am sure, with other Members of the Congress that on the first page of my questions to you, I ask why are there cuts in the program serving low-income taxpayers, and on this one I am asking you similar questions. So it would seem either that I am asking all the questions that are leaning on one side, or we are taking hits again, directing hits, at the low-income homeowners of this country.

Secretary GEITHNER. But on balance, we have proposed a significant expansion in these two signature programs, which are the CFI program and New Market Tax Credit program. For reasons that we both agree, these programs have a great record of reaching some of the hardest-hit communities in our country, with a very good record of success leveraging private money to help make sure that our taxpayer dollars are used effectively. They go to institutions who have a good record of lending in their communities.

So my own view is that we are increasing our investments, and we are reforming how we use them in ways that make them more effective.

Mr. SERRANO. I have one last question, and then I will submit the others. I know Mrs. Emerson wanted to come back, Mr. Culberson, but it is getting to that crunch time here.

In the last year banks have reduced their credit outstanding to commercial and industrial businesses by almost 20 percent, or $300 billion. When businesses lose access to credit, they cut back jobs and prolong our efforts at economic recovery.

Recently the Financial Press has reported that the financial services sector has paid out more than $100 billion in bonuses in the last couple of months.

What do you think will be required to resume business lending in this country? Do you agree that the obscene amount of money handed out for bonuses could have been retained and used to increase credit in our struggling economy by hundreds of billions of dollars?

Secretary GEITHNER. Mr. Chairman, what you have seen happen in terms of credit is a mix of two different things. One is you saw demand for credit fall very, very sharply as the economy growth slowed, the economy contracted; and then you have seen a substantial reduction in credit bank supply banks who are short capital. Both those two things were happening, but it is starting to ease.

The best measure of whether credit is getting easier or tighter is the price of a loan, and the cost of credit has come down very, very dramatically across the country for a business, for a family, for a municipal government, and that is a measure of progress we have achieved in trying to heal the damage caused by the financial system.

Now, I completely agree that what you have seen happen in compensation practices across the financial industry is unacceptable. It is outrageous. And we are working very hard using the authority Congress provided us trying to make sure we are bringing about durable reforms in how financial executives are compensated so they don't have the incentives again to take a bunch of risks and leave the American people holding the bag. And it is very important. We have seen some progress, but not enough, and we are going to keep working, making sure that we encourage reforms that will make sure we don't get in this kind of mess again.

Mr. SERRANO. I know you do realize that part of the lack of public confidence in what we are doing is when they continue to see this happen.

Secretary GEITHNER. Of course. Absolutely.

Mr. SERRANO. And then one last point here, and I won't ask— I won't make all the comments that go before the question, but with the whole issue of TARP and the public feeling that the money is not going to the right place, with 20/20 hindsight, what more do you think could have been done from the onset of TARP to ensure greater transparency and accountability in the way that TARP dollars were being used?

Secretary GEITHNER. Mr. Chairman, it is a little hard for me to say that even with the benefit of hindsight now, but let me tell you what we did and what we are committed to.

We made sure that we put the precise financial terms of all the investments we made in the public domain on our Web site for everybody to see right from the beginning. We have adopted a whole range of proposals by the various overseers Congress put in place over this program to try to improve transparency of this basic program.

We have put in place a dramatic improvement in the basic access to information the American public have about these programs, where their resources went, what they were for, the terms in which they were provided, and we will continue to work on ways to do that.

But the important thing to take, just to reflect on as you look at how this program was run, is that we have now again got back more than $170 billion from the financial system. We have reduced expected losses by more than $400 billion from where they were just a year ago. We have saved substantial resources for the American people to devote to our long-term fiscal challenges, not just our near-term priorities. We have done this at much lower cost than people expected, and we have seen a very dramatic improvement in credit conditions across the country.

So I think the American people can look at that record, and they can see the detailed numbers on the return, on the risk of losses still where that is concentrated, and they can see the benefits where they are.

Now, but we all recognize that there are a lot of challenges ahead of us still, in small business credit, in housing markets, in commercial real estate. And this is not over yet, and we are not going to make the mistake many countries have made across history over time, which is to pull back too quickly, to stop before we have actually healed the damage caused by—and this crisis caused a huge amount of damage. We have made a lot of progress. We have a lot of challenges left, though.

Mr. CULBERSON. I would like to ask about Freddie and Fannie.

Mr. SERRANO. One more, and then we will wrap it up. He has to leave. I have to speak against the war, save some money.

Mr. CULBERSON. That is always good to save money.

Thank you, Mr. Secretary. I wanted to ask about Fannie and Freddie in particular. I know that the Congress had put limits on the liability of the taxpayers, and that Treasury had the authority to do so and lifted, I think, those caps on the amount of the exposure. But we have not yet seen a reform proposal out of the administration, and the scale of the losses, of course, at Freddie and Fannie are both immense. This is a very scary situation, and as a fiscal conservative, I certainly don't like to see the taxpayers put on the hook for this, particularly in an unlimited way.

Would you, if you could, tell us what the administration's time frame is? Why are we still waiting to see reform of Freddie and Fannie, and what will it entail to help provide protection for your kids and my kids?

Secretary GEITHNER. What we have suggested, Congressman, is that we are going to put out on the public domain—I am going to testify in a few weeks on this—some broad objectives and principles to guide reform. We are going to put out a set of broad questions on the strategy for public comment.

This is a very complicated issue, as you know. It doesn't just involve Fannie and Freddie. We want to take a careful look at the entire set of government agencies that act in the housing market now and the set of policies that helped contribute to this terrible crisis. And our expectation now is that as we go through that process of public hearing and comment, we will put together some proposals for reform that we present to the Congress next year.

Now, you have asked a legitimate question, which is why not now? And I will just be honest with you. We are doing a lot of things. We just have got a lot going on, and we thought to do it well, do it carefully, do it right, we wanted to go through a process of more careful reflection. If we rushed it, the risk is we would not achieve enough and not get consensus, something sweeping enough.

But my personal commitment is we are going to need fundamental reform of the government's role in the housing market, not just in Fannie and Freddie in their future, but looking across a whole range of other policies and instruments. And what we allowed happen was, again, a national tragedy, it was avoidable, and we should never have let those institutions get themselves in a position where they took on that much risk without capital to back them, without credible oversight. With that degree of moral hazard, it is a terrible thing, and it is going to require comprehensive reform to change it.

Mr. CULBERSON. The sooner the better. The unlimited liabilities are a real concern.

And also, Mr. Chairman, it is important to ask about—we haven't touched on this yet—the commercial market. We are about to see a tremendous number of resets of commercial mortgages, and a lot of those properties have been dramatically devalued. The valuations have plummeted for a lot of those properties, you get a lot of vacancies, businesses that have left, and the banks are being—are so spooky, of course, about real estate loans. And we have got potentially another tidal wave coming.

What is the administration doing? And forgive me for throwing this in at the end, Mr. Chairman, it is an important question. What is the administration doing to attempt to mitigate the size of the commercial reset tsunami which we see coming, which is conceivably as big, if not bigger than the residential mortgage problem?

Secretary GEITHNER. You are right to say it is still a challenge. A big part is still ahead of us. It is going be to a challenge for the country to work through.

Again, as I said to your colleague earlier, the two things we think are most effective are to make sure we are getting capital to the banks, to the small community banks, which still face substantial exposure to commercial real estate losses. That will help at the margin, but we want to make sure that we are helping to provide more liquidity to the securitization markets that are helpful in this context. The programs we have put in place in that area have been quite helpful so far, they have made some impact so far, but there is a lot of challenge still ahead. I would be happy to hear suggestions from you on what would be helpful.

Mr. CULBERSON. One I would like, a suggestion that I will pass, the Chairman has been very gracious in indulging me and giving me extra time, is that the regulators—I am hearing this consistently from the smaller banks—the regulators are being unnecessarily aggressive in attempting to force banks to get real estate off their portfolios, and it is not a good idea. The regulators, I think, are a part of the problem. Obviously, you want to make sure that the loans are prudent, that they are going to be repaid. In Houston, for example, I know of a tremendous number of these are blue-chip borrowers with very long, stable credit histories that have never missed a payment, and banks are turning down loans just because the banks are being hammered by the regulators to get real estate off of their—do you know what I am talking about?

Secretary GEITHNER. I have heard this concern, too.

Mr. CULBERSON. What can you do about that, that right there, just giving a little breathing room to the banks on the regulation side? If it is a safe investment in real estate, the guy has always paid his bills, you have seen some reduction in the valuation, but come on, you know, keep loaning money. What can you do there?

Secretary GEITHNER. It is a serious concern. I hear it across the country, as do you. But this is a matter for the FDIC, for the OCC, the OTS, and the Fed, and what we are doing is encouraging them to continue to provide a little bit more care and balance in the guidance they give examiners across the country so they are not overdoing it, overdoing the tightening, not contributing to it. They put out some guidance in November that would help clarify how examiners should treat loans backed by commercial real estate to avoid some of the risk you said, but I will certainly carry that message to them.

Mr. CULBERSON. Thank you, Mr. Chairman.

Mr. SERRANO. Mrs. Emerson and I and other Members will be submitting questions for the record.

We thank you, Mr. Secretary, for your time. We thank you for your direct answers. We want to work closely with you to make sure that the recovery is strong, and that the things you inherited January of last year are dealt with properly. But we thank you for your time. Thank you.

Secretary GEITHNER. Thank you very much.

Mr. SERRANO. Meeting is adjourned.

HOUSE APPROPRIATIONS SUBCOMMITTEE ON FINANCIAL SERVICES AND GENERAL GOVERNMENT

HEARING

ON

THE FY 2011 BUDGET REQUEST OF THE DEPARTMENT OF THE TREASURY

Questions for the Record

Treasury Secretary Timothy F. Geithner

March 10, 2010

Questions from Chairman Serrano

1. **The IRS announced with much fanfare last year an agreement with several Swiss banks to reveal the names and records of more than 4,000 Americans suspected of evading US taxes by parking their money in Swiss bank accounts. However, the Swiss courts recently undermined an agreement that would have allowed better enforcement of taxes on Americans with Swiss bank accounts. What are the prospects of restoring that agreement in the Swiss Parliament? Are similar agreements being pursued with other tax haven countries?**

   The August 19, 2009, agreement reached between the United States and the Swiss Confederation involved a request for information from the IRS regarding UBS AG. On March 31, 2010, the respective Competent Authorities for the United States and the Swiss Confederation signed a protocol amending certain provisions of the August 2009 agreement for the purpose of submitting the amended agreement to the Swiss Parliament for approval. Although we expect the Swiss Parliament to deliberate and act on the protocol in its June 2010 session, we are not in a position to predict the outcome. The United States government continues to explore its options to assure this agreement is implemented and is exploring other information exchange opportunities involving offshore accounts on a global basis.

2. **Last year, the Department followed the lead of this subcommittee and allowed travel to Cuba by Cuban-Americans visiting their families. The Department is also implementing an appropriations provision that partially relaxes the terms under which payment may be received for exports of agricultural and medical goods to Cuba. Please provide an update as to how implementation is proceeding with respect to these two areas of U.S. transactions with Cuba.**

   Treasury's Office of Foreign Assets Control ("OFAC") issued amendments to the Cuban Assets Control Regulations (the "CACR"), effective September 3, 2009, to implement measures announced by the President on April 13, 2009. The changes were designed, among other things, to promote greater contact between separated family members in the United States and Cuba and to implement certain provisions of the Omnibus Appropriations Act, 2009. Earlier, OFAC had issued a general license to liberalize certain family travel consistent with a provision of the Omnibus Appropriations Act, 2009 immediately after its passage. Pursuant to the Consolidated Appropriations Act, 2010, OFAC further amended the CACR, effective March 9, 2010, to implement the provision of that Act related to the interpretation of the term "payment of cash in advance" as it applies to U.S. sales of agricultural and medical products to Cuba.

3. **The budget request contains two new initiatives for the Community Development Financial Institutions Fund: $50 million for the Bank On USA Initiative to promote affordable financial services and credit for those without bank accounts, and $25 million to increase availability of healthy, affordable foods in underserved urban and rural communities. Please describe how these new programs will be run and how they will differ from existing programs at Treasury and other agencies. Has a sufficient amount of funding been allocated to allow for their successful implementation? I am especially interested in the Healthy Food Financing Initiative**

because a recent study released by the Food Research and Action Center showed that my Congressional District had the highest rate of hunger in the nation. I would like to get a better understanding of the role that the CDFI fund will play in the implementation of this program.

Bank On USA Initiative

Bank on USA is a new initiative that seeks to address the many problems faced by unbanked and underbanked households in America who lack access to the basic financial products and services they need to build more secure financial futures for themselves and their families. According to the FDIC, unbanked households, those who lack a checking or savings account, make up 7.7 percent of American households (approximately 17 million adults), and underbanked households, those who have a checking or savings account but rely on alternative financial services, make up 17.9 percent of American households (approximately 43 million adults). For minority groups these figures are even higher with 54 percent of Black households and 43.3 percent of Hispanic households being either un- or underbanked.

Treasury has requested $50 million for Bank on USA to promote:

- Financial education;
- Broader access to safe and affordable bank accounts; and
- Private sector innovation to serve low and moderate income households.

The program will promote financial services that help families meet their financial needs and build savings and solid credit histories. The program will build on community-based efforts involving CDFIs, state and local governments, non-profits, and a wide array of financial institutions.

Bank on USA will have several distinct components including:

1. A grant program to support local initiatives to bank the unbanked and increase the availability of appropriate financial products and services to unbanked and underbanked low- and moderate-income people;
2. Outreach and technical assistance, including the development of partnerships, education tools, and the maintenance of a web-based toolkit for practitioners; and
3. Research and development on expanding access to bank accounts, including the development of model banking products and the development of model implementation and outreach strategies, which will integrate financial access and financial education.

The Healthy Food Financing Initiative

The Healthy Food Financing Initiative (HFFI) is a new multi-year effort that will increase the availability of affordable, healthy foods in underserved urban and rural communities, particularly through the development or equipping of grocery stores and other healthy food retailers. To support this initiative, the Departments of Agriculture, Health and Human Services, and Treasury have partnered to make available over $400 million in financial and technical assistance to community development financial institutions, other nonprofits, public agencies and businesses with sound strategies for addressing the healthy food needs of communities. These organizations will use federal grants, loans, loan guarantees and tax credits to attract private sector capital to invest in projects that increase access to fresh produce and other healthy foods. The goal is to substantially reduce the number of "food deserts" in our nation over the next several years.

"Food deserts" are communities in which residents do not have access to affordable and healthy food options. Instead of supermarkets and grocery stores, these communities are typically served by fast food restaurants and convenience stores that offer little, if any, healthy options. This lack of access contributes to a poor diet and can lead to higher levels of obesity and other diet-related diseases, such as diabetes and heart disease. Nationwide, the USDA estimates that 23.5 million people, including 6.5 million children, live in low-income areas that are more than a mile from a supermarket. Of the 23.5 million, 11.5 million are low-income individuals in households with incomes at or below 200 percent of the poverty line. Of the 2.3 million people living in low-income rural areas that are more than 10 miles from a supermarket, 1.1 million are low-income.

However, effective local programs have demonstrated that well-targeted financing and technical assistance can create viable business outcomes and access to healthier food options. Targeting federal financial assistance to these areas will not only increase the supply of healthy foods and create new markets for farmers, but also create jobs and support broader development efforts to revitalize distressed communities.

Of the total Federal assistance requested for HFFI in the President's FY 2011 Budget, $250 million is for New Markets Tax Credit authority and $25 million is for grant funding to CDFIs. CDFIs are specialized financing institutions that provide financial services to underserved communities, and have developed innovative and successful models to respond to local needs, including the need for healthier food options. Grants and technical assistance to CDFIs, along with New Markets Tax Credits, will spur private sector investment, which will increase affordable financing for grocery store development, supplies and equipment to improve food production technology, improvements and modernization of food distribution mechanisms and infrastructure, and the development of outreach and training programs to bring healthy food options to even more communities.

4. **Both the Recovery Act and this year's appropriations bill waived the requirement for CDFI Fund applicants to have matching funds. This year's budget request, however, would end the waiver. Although the economy is showing some signs of improving, the communities served by CDFIs will likely be the last to recover from the economic woes this country faces. The new fiscal year starts in seven months. Please explain why the decision was made to reinstate the matching funds requirement so soon.**

Treasury believes that CDFIs will be able to honor the matching funds requirement for FY 2011. In 2009, before Congress waived the matching funds requirement for the FY 2009 round, the CDFI Fund had received 260 applications for the CDFI Program, up 16 percent from the FY 2008 round (225 total applications). The ability of CDFIs to obtain those matching funds in the midst of the finical crisis demonstrates the capacity of the CDFIs to leverage private sector resources.

Treasury does recognize that many CDFIs are still managing a tighter credit environment, which could make it challenging for some CDFIs to obtain matching funds. The FY 2010 award round, which had a waiver for the matching funds requirement, received 408 applications requesting $467 million in Financial Assistance awards - almost double the number of applications and funding requested from the FY 2009 round. This demonstrates the current strong demand for capital by the CDFI industry.

5. **With regard to the Department's Making Home Affordable Program, at the current time how many homeowners do you expect will be helped with a 'restructured mortgage that is affordable into the future' and how many others do you anticipate will be forced to give up their homes through foreclosures and short sales?**

Because participation numbers are dependent upon a number of changing variables in the housing market, we have not made such projections beyond our expectation that the Obama Administration programs will provide 3-4 million homeowners the opportunity to stay in their homes over the life of the program.

As the largest and most complex mortgage modification program of its kind, there was little historical precedent and limited data for estimating potential performance when the Home Affordable Modification Program (HAMP) was launched in March 2009. The projection of three to four million homeowners helped is based on our best estimate of the number of HAMP-eligible households that are likely to require assistance during the four-year program (2009-2012). Even then, the number of households that actually require assistance from HAMP during the remaining three years may diverge from our expectations if economic conditions or home prices evolve differently than projected.

For instance, the process of converting trial modifications to permanent has been more challenging than originally anticipated. This is due to several factors, including insufficient capacity and execution at most servicers, a lack of willingness or ability to provide necessary documentation on the part of some borrowers, frequent inconsistencies between verbal and verified income that result in a borrower being deemed ineligible for the program, and a process that has proven more complex administratively than originally conceived. Drawing on these lessons, we have implemented program changes that will help address these challenges. Foremost among those changes is the requirement for a servicer to offer a trial modification based on verified income only, which should help eliminate any conversion or process delays resulting from discrepancies between stated income and verified income.

Any such projection is further complicated by the enhancements to HAMP announced on March 26, 2010. These changes will provide temporary mortgage assistance to some unemployed homeowners; encourage servicers to write-down mortgage debt as part of a HAMP modification; allow more borrowers to qualify for modification through HAMP;

and help borrowers move to more affordable housing when modification is not possible. Additionally, the Administration announced enhancements to Federal Housing Administration (FHA) programs that will permit lenders to provide additional refinancing options to homeowners who owe more than their home is worth because of large falls in home prices in their local markets. TARP funds will be made available up to a total of $14 billion to provide incentives to support writedowns of second liens and encourage participation by servicers, and to provide additional coverage for a share of potential losses on these loans.

As these changes are implemented over the coming months, they will improve assist homeowners affected by the economic downturn. However, the precise impact of these changes on program participation is still uncertain as they too arrive with little precedent and will largely vary based on economic or housing market conditions going forward.

HAMP is just one part of the Obama Administration's multi-faceted approach to assisting homeowners and stabilizing the housing market, which also includes state and local housing agency initiatives, tax credits for homebuyers, neighborhood stabilization and community development programs, mortgage refinancing, and support for Fannie Mae and Freddie Mac. We are confident that these combined efforts will help a significant number of American families avoid foreclosure in the coming years and preserve home values for many more.

6. **In answering a question for the record regarding executive compensation, following last year's hearing, Secretary Geithner laid out certain principles for bank compensation. He noted that, "First, compensation plans should properly measure and reward performance. Second, compensation should be structured to account for the time horizon of risks. Third, compensation practices should be aligned with sound risk management. Fourth, we should reexamine whether golden parachutes and supplemental retirement packages align with the interests of shareholders." Does the Department believe that the latest round of enormous bank bonuses meet those standards?**

We have seen some early evidence that the process of changing the compensation practices that contributed to the financial crisis has begun[1]. However, as we indicated last June—when Treasury released compensation regulations applicable to all recipients of TARP funds and appointed a special master to oversee compensation at recipients of exceptional taxpayer assistance—to achieve long-term, substantive reform we need to equip independent directors, shareholders, and regulators with the tools they need to ensure that compensation structures provide appropriate incentives to executives.

That is why we proposed, and both the House and Senate versions of financial reform include, legislation that will require all public companies to give shareholders a "say on

[1] As an example, in December 2009, Goldman Sachs announced that its 30-person management committee would receive all their discretionary compensation for 2009 in the form of restricted shares that cannot be sold for five years and that shareholders would have an advisory vote on executive compensation in 2010. Moreover, JPMorgan Chase CEO Jamie Dimon received his bonus for 2009 entirely in equity rather than cash.

pay" and compensation committees real independence. We have also worked with our G-20 partners to reform compensation practices to appropriately align incentives at financial institutions around the world. Following those initiatives, the Federal Reserve has proposed guidance on executive compensation that will be incorporated into the supervisory process, and launched a comprehensive review of the relationship between risk and pay at our banks. These reforms will help make certain that we do not return to the executive compensation practices that contributed to the financial crisis.

7. **In the wake of the savings and loan fiasco in the 1980s, over 1,000 insiders were convicted. In the banking fiasco of recent years, no insider has even been indicted, much less convicted. Executives have not only escaped punishment, they have gone back to reaping record bonuses as if nothing had happened. They also seem to have had considerable success in preventing Congress from passing legislation to rein in their risk-taking, leverage and gouging of consumers. Does the Department believe that banking executives have begun to change their behavior as a result of this banking fiasco- that is, have they learned any lessons from their behavior? Is the Treasury Department working with the Department of Justice to investigate and prosecute any illegalities that occurred during the recent crisis? Does the Treasury Department think that absent large scale regulatory reform, banking and Wall Street executives will change their behavior in a way that will help us avoid future crises?**

   In November 2009, President Obama established the Financial Fraud Enforcement Task Force (FFETF) to hold accountable those who helped bring about the last financial crisis, and to prevent another crisis from happening. The task force is improving efforts across the government and with state and local partners to investigate and prosecute significant financial crimes, to ensure just and effective punishment for those who perpetrate financial crimes, to recover proceeds for victims, and to address financial discrimination in the lending and financial markets.

   To make sure that we avoid future crises, we need comprehensive financial reform: we must close loopholes so no major firm escapes serious oversight; we must have comprehensive reform of our financial markets, including derivatives transactions and securitization of mortgages; we must consolidate federal consumer financial protection in an accountable, independent body with the resources to maintain standards in every corner of the market; and we must end the perception of "too big to fail."

8. **The budget request once again repeats a budget gimmick first proposed by the Bush Administration that assumes that the entire budget of Treasury's Alcohol and Tobacco Tax and Trade Bureau will be funded through a fee on all sellers, distributors, and manufacturers of alcohol and tobacco products. I would very much like to get a commitment from the Department that this will be the last budget that includes this proposal. Does the Department have any thoughts on this?**

   The proposal to fund TTB with fees levied on alcohol and tobacco businesses was developed with regard to our current fiscal challenges and the federal government's need to make the most effective use of finite resources. These proposals were intended to assign the Bureau's cost to those who profit from the sale of alcoholic beverages and tobacco. We are aware, however, of the concerns that any such fee must not be levied on small businesses or businesses that are already paying alcohol or tobacco excise taxes. The Department will ensure that the Chairman's concerns are taken into consideration in the FY 2012 budget formulation process.

Questions from Ranking Member Emerson

Gold Bullion

1. **It has been the practice of the United States Government since the American Eagle program was started in the early 1980s to sell gold, silver and platinum "bullion" coinage to the public through a network of approved purchasers – rather than directly to the public itself. Many constituents are questioning this practice in this period of high demand for bullion coinage and wondering why they cannot purchase bullion coinage directly from the United States Mint at near market prices. What are the pros and cons of allowing the United States Mint to sell "bullion" coins directly to the public?**

The United States Mint currently has the statutory authority, and is therefore already allowed, to sell gold, silver, and platinum bullion coins directly to the public. As the question implies, the sale of bullion coinage through a network of Authorized Purchasers is merely a business practice, not a legislative requirement that the United States Mint has followed in order to ensure that members of the public can readily buy and sell these coins on the precious metals investment market.

The principal advantage of retailing these coins to individual members of the public is that it would fulfill constituents' desire to acquire them directly from the Government, without a so-called "middleman."

The principal disadvantages of retailing these coins to individual members of the public are that the United States Mint would have to establish a new sales channel by which it sells the coins at prevailing market prices, and that the United States Mint does not have the authority to buy the coins back when a customer wishes to liquidate his or her holdings. Moreover, if the United States Mint were to sell bullion directly to the public, it might not be able to sell at near-market prices. The United States Mint would have to fully recover any added costs of minting, packaging, selling and distributing bullion coins directly to the public.

Community Development Financial Institutions - Healthy Food Financing Initiative

2. **Your budget request proposes $25 million for grants and technical assistance for CDFIs to develop approaches for financing businesses that provide affordable healthy foods in underserved markets. I appreciate that the Administration is trying to address this very serious problem but I would like to know more about how you plan to implement this program.**

    - **How will CDFIs attract investors to open grocery stores in underserved areas?**

As part of the Healthy Food Financing Initiative (HFFI), the Treasury Department will support private sector financing of healthy food options in distressed urban and rural communities. Through the New Markets Tax Credit (NMTC) and Financial Assistance to Treasury-certified CDFIs, Treasury has a proven track record in expanding access to nutritious foods by catalyzing private sector investment.

Through HFFI, the CDFI Fund will provide competitively awarded grants and tax credits to CDFIs and Community Development Entities (CDEs) that are improving access to fresh food in low-income and underserved communities. The actual investment decisions will be made by certified CDEs and CDFIs which demonstrate, through their applications, the capacity to finance healthy food activities.

- **How will you determine what communities receive assistance?**

  As with other awards administered by the CDFI Fund, the Healthy Foods Financing Initiative will be a competitive application, peer reviewed process. Three external reviewers are assigned to each New Markets Tax Credit application as well as each Financial and Technical Assistance award application and are responsible for providing independent analysis of each application. They are charged with applying the CDFI Fund's scoring guidance impartially and consistently.

- **How many grocery stores do you think this initiative can open?**

  The Healthy Food Financing Initiative will promote a range of financing vehicles that will expand access to nutritious foods, including developing and equipping grocery stores and other small businesses and retailers selling healthy food in communities that currently lack these options. The Initiative will not just support grocery stores; other innovative food supply strategies such as local farmers markets, food co-ops, and fisheries may also be financed.

- **Will you make funding opportunities available to both urban and rural communities?**

  The Healthy Foods Financing Initiative is dedicated to helping both urban and rural communities. CDFIs have a wealth of experience in a variety of healthy foods efforts in all low-income communities, both rural and urban. CDFI examples in both urban and rural communities include grocery stores (which often include a requirement that the store must purchase locally-grown fresh food), wholesale farming, fisheries, local food processors and distributors, farmers' markets, and food co-ops. Each program is based on the individual community's needs.

Alcohol User Fee

3. **The budget proposes a new $106 million user fee on the alcohol and tobacco industries that would be used to offset the cost of the Alcohol and Tobacco Trade and Tax Bureau.**
   - **Are you working with Ways and Means or the Energy and Commerce Committees to enact the necessary authorizing language to implement this fee?**
   - **Do you expect those Committees to mark-up your proposed legislation soon?**
   - **If those Committees do not advance this proposed user fee, will the Administration submit a budget amendment requesting the $106 million reduction be restored to this Bureau and propose a funding reduction in another account?**

The House Ways and Means Committee and the Senate Finance Committee are the authorizing committees that would decide on the fee proposal. The Administration included the proposal in the President's Budget rather than in standalone legislation. We have discussed the proposals with committee staff. We do not expect a markup of legislation including our proposal.

In previous years, no budget amendments have been submitted regarding this issue, and we don't anticipate submitting a budget amendment in FY 2011.

Questions from Congresswoman Lee

Questions regarding minority and women owned firms' access to TARP and TALF:
Last year, I and many of my colleagues expressed concern about the structure of the TARP and TALF programs and how that structure would prevent minority and women owned businesses from participating in the management of the programs.

1. **Can you update the subcommittee on what Treasury is doing to ensure access to contracting and sub-contracting opportunities for minority and women owned firms?**

   Treasury believes it is essential that the TARP be structured in a manner that encourages participation of small businesses, veteran-owned businesses, and minority and women-owned businesses. We encourage the participation by and a level playing field for small, minority, veteran, and women-owned businesses. Our small business strategy for federal contracts put in place last spring is showing tangible returns, such as:

   - Our Financial Services solicitation, issued to obtain multiple contracts estimated at $185 million over five years, reserves at least two prime contract awards for small business, and includes a target of 20% of total contract and subcontract dollars to small business, including minority, veteran, and women-owned businesses, increasing to 30% over the life of the contracts.

   - Our Web Portal support contract awards, valued at approximately $100 million over five years, have been issued to three small businesses.

   - Our Freedom of Information Act (FOIA) support contract, valued at approximately $14 million over four years, was awarded to a Service Disabled Veteran Owned Small Business.

   Where small business set aside contracts have proven infeasible, and where subcontracting opportunities exist, we have required small business subcontracting plans containing specific performance goals. We evaluate proposed small business subcontracting plans during proposal evaluation, and assess their commitment to providing meaningful opportunities to small businesses in various socioeconomic categories. Our contractors are required to submit performance data against those goals directly to the Small Business Administration's electronic subcontracting system website. Small business subcontracting performance is integral to our contract performance management and reporting process. Prime contractors that fail to make a good faith effort to achieve their subcontracting goals may be rated poorly in the government-wide Past Performance Information Retrieval System and subject to liquidated damages penalties.

   In addition to federal contracts, the Office of Financial Stability (OFS) has the authority to designate financial agents to perform work related to the custody and management of TARP assets and the execution of TARP programs. The OFS has designated ten asset managers as financial agents to monitor the Treasury's portfolio positions. Of those ten, six managers are minority- or woman-owned businesses. Our financial agents have also contracted with an additional 19 minority- and woman-owned businesses to provide necessary services in support of TARP programs.

More recently, on April 26th the Treasury announced that Treasury's financial agent Morgan Stanley is providing opportunities for small, minority and women-owned broker-dealers to participate in the sale of our common stock position in Citigroup (www.financialstability.gov/latest/tg_04262010.html).

Treasury recognizes the importance of engaging a diverse pool of talent. Accordingly, we continue to seek to ensure equal opportunity for minority- and woman-owned firms as financial agents, and to encourage our existing financial agents to identify opportunities to engage small business contractors, including those that are minority- and woman-owned businesses (MWOBs).

Specifically, The Term Asset Backed Securities Loan Facility (TALF) is a $200 billion joint- Federal Reserve and Treasury- program to restart the asset backed securities market. The Federal Reserve provides term non-recourse loans collateralized by AAA-rated ABS. The U.S. Treasury provides a $20 billion first loss credit protection. Day to day operations, including MWOB selection, is managed by the Federal Reserve Bank of New York (FRBNY). The TALF program has been actively engaging MWOB participation with the following:

- *TALF Agent expansion.* FRBNY designated four minority-owned broker-dealers to serve as TALF agents, with them to play the same role as primary dealers to represent borrowers in their interactions with the FRBNY.

- *Collateral Monitor RFP.* FRBNY cast a wide net in identifying firms that might provide analytical services to support the TALF. Collateral Monitor RFP was sent to 62 firms of all sizes and ownership structures.

- *Investor Guide.* FRBNY published a user-friendly investor guide on its website with smaller investors in mind, intended to explain the program and how to access it to potential borrowers.

- *Outreach.* Senior officials and staff from the Board and FRBNY had an ongoing dialogue with leadership and members of the Congressional Black Caucus and National Association of Securities Professionals (NASP, an industry association for minorities) to explain the program, discuss opportunities for members to become involved, and identify likely participants.

1. **Will you give us a breakdown of minority and women owned participation rates in the operations of TARP and TALF?**

   Please see response to Question #12 above.

<u>Questions regarding CDFI's:</u>
I was pleased to hear the announcement by the President of increased support for our Community Development Financial Institutions. CDFI's that provide investment and services to our lower income and most economically disadvantaged communities are more critical than ever. But I have some concerns about the ability of small minority owned depository institutions being able to compete for the new funding for CDFI's.

1. **What can Treasury do to proactively reach out to minority and women owned financial firms to ensure their access to CDFI funds and improve the participation of the communities that they serve in the nation's economic recovery?**

   CDFIs serve a critical role in distressed communities as they offer affordable loan products and technical assistance to borrowers who may not be reached by mainstream financial institutions. CDFI customers are 70 percent low income, 60 percent minority and 52 percent female.

   The CDFI Fund is dedicated to certifying more minority and women-owned financial institutions as CDFIs. The CDFI Fund is involved in a variety of outreach initiatives designed to increase the number of certified minority CDFIs and CDEs. These efforts include a recent workshop for Minority Depository Institutions (MDIs) with the FDIC and IRS participating. Representatives from approximately 30 MDIs around the country attended the event. The CDFI Fund is also working with the FDIC to develop a strategic plan to determine the opportunities and constraints associated with MDI participation with the New Markets Tax Credit.

   The CDFI Fund is also working with Partnership for Progress; a Federal Reserve Bank System program created to preserve and promote MDIs and enhance their ability to thrive in an increasingly competitive banking environment. The CDFI Fund has participated in three Partnership for Progress events since February 2010.

   To increase outreach and awareness of programmatic activities that may be beneficial to MDIs, the CDFI Fund has requested inclusion of its news alerts in the events section and newsletters of the Federal Reserve Bank System Partnership for Progress, Office of Thrift Supervision, Office of the Comptroller of the Currency, Federal Deposit Insurance Corporation, and the White House Office of Urban Affairs.

   Moreover, Treasury launched the Community Development Capital Initiative in February, to offer low-cost capital to depository CDFIs so the CDFIs in turn can provide credit and financial services to underserved communities and businesses, including minority and women owned firms.

<u>Executive Compensation:</u>
The Administration has limited the executive compensation of companies that have received the most aid from the TARP funds.

1. **Can you tell the committee if the limits on the pay for some companies have caused the companies to fail or underperform?**

   As noted in your question, last June we appointed Kenneth Feinberg to be Special Master for TARP Executive Compensation, and charged him with determining appropriate compensation for the top earners at TARP recipients that received exceptional help from taxpayers. The Treasury regulations that give the Special Master this authority include a clear set of principles that the Special Master must apply when making those decisions. These principles require, among other things, that the Special Master make certain that compensation structures reflect the need for each TARP recipient to remain a competitive enterprise—and, ultimately, to repay the taxpayer.

   The Special Master's decisions have applied these principles carefully and consistently, striking the difficult balance needed to bring compensation practices at these companies into line with long-term financial stability and taxpayer interests. It is too soon to tell exactly how these decisions will affect the performance of these companies over the long term. We are encouraged, however, that two of the seven firms that were initially subject to the Special Master's jurisdiction have since repaid the exceptional assistance that taxpayers provided during the crisis, and that overall TARP repayments stand at $194 billion, well ahead of last year's projections, and now an amount that exceeds the amount of TARP assistance outstanding.

2. **Would reigning in just some of the most extreme examples of excessive pay of the highest paid executives cause companies to fail?**

   Our goal is to bring compensation practices into line with long-term value creation and financial stability. To do so, we will need to equip independent directors, shareholders, and regulators with the tools they need to ensure that compensation structures provide appropriate incentives to executives. Limiting that effort to just a few specific examples could lead to unintended consequences—and leave in place many unacceptable compensation practices that contributed to the crisis.

   Instead, since last February we have worked with Congress, the Federal Reserve, and others to reform the compensation practices that undermined trust and confidence in our financial system. We proposed, and both the House and Senate versions of regulatory reform include, legislation that will require all public companies to give shareholders a "say on pay" and compensation committees real independence. We forged an agreement with the other G-20 nations to reform compensation practices at financial institutions around the world to, among other things, eliminate practices that encourage excessive risk-taking. Following that agreement, the Federal Reserve has launched a comprehensive review of the relationship between risk and pay at our banks, and has proposed guidance on compensation that will be incorporated into the supervisory process. We believe that these reforms will help directors, shareholders, and regulators make certain that all compensation practices—rather than just a few extreme examples—are brought into line with financial stability and long-term growth.

Company Owned Life Insurance policies:
Many companies use life insurance policies taken out on their rank and file employees, often without their knowledge or consent, to pay out deferred compensation for some of their top executives.

1. **Do you believe that the positive tax treatment of life insurance that Congress enacted was meant to allow corporations to shield executive pay from taxation and benefit from the deaths of their employees or should that positive tax treatment be reserved for the families and loved ones of the deceased, which is what I believe Congress intended?**

   The beneficial tax treatment of employer-owned life insurance reflects the acknowledgement under state insurable interest laws that an employer has an economic interest in the lives of its employees. For example, death benefits under a life insurance contract may offset losses incurred as the result of the death of a key employee, or may be used to provide funds to redeem a deceased owner's interest in the business. Life insurance contracts also may be used to fund death benefits that are owed to a deceased employee's beneficiaries, or to fund other employee benefits.

   However, existing law includes limitations on the availability of the tax benefits associated with employer-owned life insurance that are intended to prevent abuse. Specifically, the Pension Protection Act of 2006 imposed significant limitations on the income tax benefits that otherwise would apply to amounts received by an employee by reason of an employee's death. As a result of these limitations, death benefits received under such a contract are not excluded from the employer's gross income unless the employee is notified in writing that the employer intends to purchase life insurance, and the employee consents in writing to being insured. In addition, the insurance must either (1) cover the life of someone who was an employee within 12 months of death or was a director or highly compensated employee or individual, or (2) be used to make a payment to the employee's beneficiaries or to purchase the employee's equity interest in the business.

   The Administration's FY 2011 Budget proposes an additional change in the treatment of employer-owned life insurance. Specifically, the proposal would further limit the ability of a business taxpayer to deduct interest expense allocable to tax-free inside buildup on life insurance contracts, thereby limiting opportunities for tax arbitrage through employer-owned life insurance.

Diversity in Hiring and Contracting at Treasury:

1. **Will you provide the Subcommittee with information regarding the diversity of the professional full time employees at the Treasury Department?**

The following table shows the participation rate of Treasury's permanent employees by Gender, Ethnicity, and Race as compared to the Civilian Labor Force (CLF) as of March 31, 2010. (For all tables, the numbers may not total exactly 100% due to rounding.)

Participation Rate in Treasury's Permanent Workforce by Gender, Ethnicity and Race

		Men	Women	Hispanics	Whites	Blacks	Asian	NHOPI*	AIAN**	2+Races
Permanent Workforce	#	43991	77428	12067	72872	29409	5820	67	992	192
Permanent Workforce	%	36.2%	63.8%	9.9%	60.0%	24.2%	4.8%	0.1%	0.8%	0.2%
CLF	%	53.2%	46.8%	10.7%	72.7%	10.5%	3.6%	0.2%	0.6%	1.6%

Native Hawaiian/Other Pacific Islander
* American Indian/Alaska Native

The following table shows the participation rate of Treasury's permanent employees within the professional occupational category as compared to the overall permanent workforce participation rate. There is no relevant CLF comparator for professionals.

Participation Rate of Professionals in Treasury's Permanent Workforce by Gender, Ethnicity and Race

		Men	Women	Hispanics	Whites	Blacks	Asian	NHOPI	AIAN	2+Races
Professional Workforce	#	6046	6094	578	8036	2548	878	6	80	14
Professional Workforce	%	49.8%	50.2%	4.8%	66.2%	21.0%	7.2%	0.1%	0.7%	0.1%

The following tables show the participation rates of Treasury's permanent employees within selected highly populated occupations within Treasury: Tax Examiner (592), Attorney (905), Program Manager (340), Revenue Officer (1169), and Information Technology Specialist (2210) as compared to each series' Relevant Occupational CLF (RCLF).

Participation Rate of Tax Examiners in the Treasury Permanent Workforce by Gender, Ethnicity and Race

592		Men	Women	Hispanics	Whites	Blacks	Asian	NHOPI	AIAN	2+Races
Workforce	#	3914	11406	1846	9199	3409	687	4	144	31
Workforce	%	25.5%	74.5%	12.1%	60.1%	22.3%	4.5%	0.0%	0.9%	0.2%
RCLF	%	38.1%	61.9%	7.6%	69.8%	17.1%	3.4%	0.0%	0.5%	0.6%

Participation Rate of Attorneys in Treasury 's Permanent Workforce by ERI and Gender

905		Men	Women	Hispanics	Whites	Blacks	Asian	NHOPI	AIAN	2+Races
Workforce	#	1266	1028	61	1992	102	126	1	10	2
Workforce	%	55.2%	44.8%	2.7%	86.8%	4.5%	5.5%	0.0%	0.4%	0.1%
RCLF	%	71.3%	28.7%	3.5%	89.1%	3.9%	2.2%	0.0%	0.2%	0.5%

Participation Rate of Program Managers in Treasury's Permanent Workforce by Gender, Ethnicity and Race

340		Men	Women	Hispanics	Whites	Blacks	Asian	NHOPI	AIAN	2+Races
Workforce	#	687	917	97	1087	358	46	0	16	0
Workforce	%	42.8%	57.2%	6.1%	67.8%	22.3%	2.9%	0.0%	1.0%	0.0%
RCLF	%	43.4%	56.6%	10.0%	69.9%	12.7%	4.9%	0.2%	0.6%	0.7%

Participation Rate of Revenue Officers in Treasury's Permanent Workforce by Gender, Ethnicity and Race

1169		Men	Women	Hispanics	Whites	Blacks	Asian	NHOPI	AIAN	2+Races
Workforce	#	2758	3526	670	3791	1556	204	2	53	8
Workforce	%	43.9%	56.1%	10.7%	60.3%	24.8%	3.3%	0.0%	0.9%	0.1%
RCLF	%	38.1%	61.9%	7.6%	69.8%	17.1%	3.4%	0.0%	0.5%	0.6%

Participation Rate of Information Technology Specialists in Treasury's Permanent Workforce by Gender, Ethnicity and Race

2210		Men	Women	Hispanics	Whites	Blacks	Asian	NHOPI	AIAN	2+Races
Workforce	#	3542	2874	317	3840	1669	532	1	53	4
Workforce	%	55.2%	44.8%	4.9%	59.9%	26.0%	8.3%	0.0%	0.8%	0.1%
RCLF	%	66.8%	33.2%	4.7%	75.1%	7.8%	10.3%	0.1%	0.3%	0.9%

2. What is Treasury doing to ensure that it is recruiting and hiring a diverse staff including from different race and ethnicities?

The Department's recruiting and hiring activities include:

- Our vacancy announcements are distributed to a wide variety of professional groups and community based organizations to ensure a broad applicant pool.

- In an effort to promote the Department of the Treasury as an employer of choice, the Department either contacted (via mailings, emails or phone) or participated in on-site recruitment activities at the following minority serving colleges and universities:

  - Historically Black Colleges and Universities: University of Maryland Eastern Shore, Howard University, Kentucky State University, University of District of Columbia, Morgan State University, Norfolk State University, Virginia State University, Hampton University, Virginia Union University, Central State University, Wilberforce University, Jackson State University, Bluefield State University, Alabama A & M University, Clark Atlanta University, Dillard University, Elizabeth City State University, Morehouse College, Paul Quinn College, Prairie View A & M University, Shaw University, Coppin State College, Bowie State University, Grambling State University, Philander Smith College, Edward Waters College, Bethune-Cookman College, University of Arkansas - Pine Bluff, Huston-Tillotson University, Wiley College, Tennessee

State University, Florida A&M University, Virginia State University, University of Alabama at Birmingham, North Carolina AT&T, North Carolina Central University, North Carolina State University at Raleigh, Texas Southern University, and Winston-Salem State University.

  - Hispanic Serving Colleges and Universities: University of Texas-El Paso, California State University-San Bernadino, California State University-Dominguez Hills, California State University-Fullerton, California State University-Los Angeles, and California State University-Northridge, Northeastern Illinois University, Florida International University, University of Texas-Pan American, University of New Mexico, New Mexico State University, and California State University-Long Beach.

  - Tribal Colleges and Universities: Dine College, Haskell Indian Nation University, Saginaw Chippewa Tribal College, Blackfeet Community College, Navajo Technical College Bay Mills Community College, Stone Child College, Fort Belknap College, Fort Big Horn College, Chief Dull Knife College, Leech Lake Tribal College, Sisseton Wahpeton College, College of Menominee Nation, and Lac Courte Oreilles Ojibwa Community College.

- The Department worked closely with the following groups in order to attract disabled veterans to apply for Treasury vacancies: the Veterans Administration, Vocational Rehabilitation Agencies, Disabled American Veterans, G.I. Forum, Paralyzed Veterans of America, Blinded Veterans Association, Black Veterans Association, Non-Commissioned Officers Association of America, state and local employment agencies, Department of Defense, Department of Veteran Affairs, Cuban American Veterans Association and the Employee Assistance and Recruitment Network (EARN).

- The Department held its Second Annual DisABILITY and IT Accessibility Summit on October 8 and 9, 2009, which included a career fair for individuals with disabilities. The Summit provided Treasury managers, supervisors, HR/EEO and IT professionals the opportunity to learn about and share best practices in outreach, recruitment, retention, and accessibility for individuals with disabilities. Through a partnership with EARN (Employer Assistance Referral Network), the Department was able to review resumes of potential new hires and invite those individuals who met vacancy qualifications to interview for open positions. On April 26, 2010, the Department participated in the government-wide Federal Hiring Expo, jointly sponsored by the Office of Personnel Management and the Department of Labor; the Department accounted for the bulk of the interviews held during the Expo.

- The Department continued to support the recruitment of disabled veterans by partnering with the Department of Defense's Operation Warfighter Program (OWF). Operation Warfighter provides Service members, who are undergoing treatment or rehabilitation at Walter Reed Army Medical Center, with a formal means of transitioning back into the workforce. Two OWF candidates were placed with the Department while they were rehabilitating.

- Treasury uses diversity focused internship programs to create a diverse pipeline of potential permanent employees. For example, Treasury continued its Hispanic Serving Institutions National Internship Program (HSINIP) by partnering with the Hispanic Association of Colleges and Universities (HACU) Internship Program to place high quality interns. Treasury hired 52 HACU interns in FY 2009. The Department also participated in the USDA HACU Career Fair, which allowed bureaus to interview interns for available positions. By using student employment hiring flexibilities, the Department was able to hire 581 students under the Student Temporary Employment Program (STEP), 59 students under the Student Career Experience Program (SCEP) and 651 students under the Federal Career Internship Program (FCIP).

3. **Will you submit to the subcommittee any outreach efforts that Treasury is conducting?**

- Treasury tries to have a presence in many diverse communities, minority serving institutions and professional groups' events in order to make them aware of the opportunities available at Treasury, including outreach to the institutions and organizations identified in the answer to the previous question. In addition:
    - On March 12, 2010, Treasury hosted a *Latinos in Finance Summit,* which provided a forum for Treasury senior officials and representatives for other economic agencies within the Administration to meet with Hispanics pursuing careers in finance, banking and related careers. Participants learned about the policy formulation process and management of Treasury and other economic agencies.
    - The Department served as a sponsor and active planning partner in the development of the Second Annual Hispanic Career Advancement Summit program. Of the 56 Federal agencies represented at this event, Treasury had the ninth largest number of registered employees. Three of the Department's Hispanic Senior Executives participated in one-on-one mentoring sessions for GS-14s and GS-15s who attended the summit.
    - For the fourth consecutive year, the Department served as a sponsor of the Virginia Hispanic Youth Symposium. Two-hundred 11th and 12th grade high school students from the DC metro area attended this event. Through our participation, Treasury is able to reach Hispanic high school students who are about to enter college and make career field choices.
    - The Department participated in the following conference and career expos:
        - Hispanic Communities: Association of Latino Professionals in Finance and Accounting (ALPFA) National Conference; HIRE-Hispanic Internal Revenue Service Employees National Conference; National Society for Hispanic Professionals; National Society of Hispanic MBAs; Hispanic Youth Symposium; Hispanic Women's Conference; LULAC -League of United Latin American Citizens National Conference; Second Annual Hispanic Career Advancement Summit; Latinos for Hire; Latino Career Expo; and Hispanic Association of Colleges and Universities (HACU) Conference.

- Tribal Communities: Symposium for American Indian Science & Engineering Society (AISES); National Indian Gaming Annual Trade Show and Convention; Sycuan Gaming Commission Seminar; National Indian Gaming Association 10th Annual Regulatory Certification Training; National Indian Gaming Commission (NIGC) Indian Gaming Regulatory Conference; Native American Finance Officer Association Winter Conference; Interagency Native American Financial Access Working Group; National Congress of American Indians Annual Convention; National Indian and Native American Training & Employment Conference; American Indian Business Leaders Conference; Society of American Indian Government Employees (SAIGE) Conference.

- Disabled Veterans: Military Stars; Salute Our Heroes; Department of Defense Hiring Heroes; Hire a Hero; Hire a Veteran; Veterans Career and Resource Fair; Recruit Military; Military World Expo; Corporate Gray; Paralyzed Veterans of America; Veterans of Foreign Wars; American Legion; Stars and Stripes; and the Military Officers Association of America.

- Black Communities: National Association of Black Accountants (NABA); Black Accountants and Latino Professionals; Black College Expo (Sponsor); Blacks in Government (BIG) Annual Conference; National Association of Black Accountants (NABA) Eastern Conference; and National Association of Black MBAs Conference.

- Asian Communities: Asian Society of Internal Revenue Service Employees (ASPIRE) Conference and National Association of Asian American Professionals Conference (NAAAP).

4. On the procurement and contracting side, can you also provide us with information regarding the amount and percent of contracts that Treasury makes with small and disadvantaged business enterprises, particularly women and minority owned firms?

This Fiscal Year, the Department of the Treasury has awarded 31.17% of its total small business eligible dollars to small business contracts. A total of 10.80% and 11.16% have been awarded to small disadvantaged and women-owned small business concerns respectively. The Department of the Treasury has exceeded the statutory goals in these categories. This information is current through April 30, 2010, and was obtained from the Federal Procurement Data System-Next Generation.

5. What is the Treasury Department doing to ensure a diversity of companies can compete for any contracts that you offer?

Treasury has a robust small business program. Procurement authority is delegated to each Bureau. Each Bureau has an assigned Small Business Specialist who is responsible for ensuring that small business concerns have an opportunity to compete for contracts. These individuals are advocates within their Bureau for small business concerns.

Treasury hosts vendor outreach sessions, which provide an opportunity for small business concerns to market their firm's capabilities. Additionally, Bureau Small Business Specialists and the Office of Small and Disadvantaged Business Utilization (OSDBU) staff participate in numerous conferences and trade fairs to educate small business concerns about doing business with Treasury. Bureau Small Business Specialists also host vendor days, procurement specific events and marketing sessions at their respective Bureau. We have great success in our outreach efforts.

Congress requires a goal that, in the aggregate, agencies award 5 percent of Federal contracts to women-owned small businesses (WOSBs) and small disadvantaged businesses (SDBs), respectively. Over the previous three years, Treasury has awarded over 7 percent of its contracts to WOSBs and over 8 percent to SDBs.

Treasury's OSDBU hosts an annual vendor outreach session in recognition of Women's History Month in March to recognize WOSBs, and to encourage increased use of WOSBs in Treasury's contract awards.

Additionally, the OSDBU staff and Bureau small business specialists participate in numerous conferences and trade fairs in support of WOSBs. The Director of OSDBU has provided numerous presentations on "How to Do Business with the Department of the Treasury" to members of the U.S. Women's Chamber of Commerce, the National Association of Minority and Women-Owned Law Firms, and the "Women in Business" Conference.

Treasury works closely with the U.S. Small Business Administration and other Federal Agencies to either host or participate in more than 50 small business conferences. In FY 2009, this included:

(1) The Annual Alliance Mid-Atlantic Conference Small Business Procurement Fair
(2) The National Center for American Indian Enterprises Development Reservation (RES)
(3) The Annual Chicago Business Opportunity Fair
(4) The Arkansas Procurement Opportunities Conference
(5) 19th Annual OSDBU Procurement Conference
(6) The Latino Coalition Economic Summit
(7) The 17th Annual "Keeping the Promise" Conference, California Disabled Veterans Alliance Business Matchmaking
(8) The Annual National *Power*Networking Conference
(9) The U.S. Pan Asian CelebrAsian Business Opportunity Conference
(10) The Maryland/District of Columbia Minority Supplier Diversity Council Business Procurement Conference

The Department of the Treasury works closely with our Prime Contractor partners to increase small business participation, and holds multiple events, including:

(1) Virginia Minority Supplier Diversity Council
(2) Booz-Allen-Hamilton Treasury Industry Day

(3) CSC Small Business Workshop

The Department of the Treasury enthusiastically supports the Veteran community. We annually participate in the following events:

(1) Annual National Veteran Small Business Conference and Expo
(2) "Keeping the Promise" The California Disabled Veteran Enterprise Alliance Expo
(3) American Legion Annual Small Business Conference

The OSDBU also maintains a website at www.treasury.gov/osdbu to provide information on procurement opportunities for all small businesses. Small businesses are encouraged to register in the OSDBU small business database to participate in various outreach events.

In addition to these activities, each bureau Small Business Specialist hosts vendor days, procurement specific events, and marketing sessions at their respective bureaus aimed at increasing small business participation within Treasury.

Questions from Congressman Culberson

1. **Please review the efforts you have underway to encourage banks to move toxic commercial real estate assets off their books, while balancing the need to encourage banks to continue making sound loans and extending performing loans.**
   - **What results do you expect in what timeframe from these initiatives?**
   - **What efforts focused on this toxic asset problem do you have underway that are specifically targeted to the local community banks sector?**
   - **What new regulations are under consideration among bank regulators that will help banks to more expeditiously address their problem commercial real estate loans? Please give some specific examples based on the current regulation or guideline vs. the proposed one.**

   Treasury launched two initiatives to improve the flow of credit: the Public Private Investment Program (PPIP) and the Term Asset-Backed Securities Loan Facility (TALF), a joint program with the Federal Reserve. Programs such as TALF and PPIP have re-introduced liquidity and reduced the cost of financing for commercial mortgage backed securities (CMBS). For instance, spreads on senior quality CMBS increased to 1500 basis points over its benchmark during the height of the financial crisis. Today, the same securities trade at approximately 300 basis points over its benchmark. With confidence being restored and the cost of financing for CMBS falling, certain banks are beginning to extend commercial real estate loans again. Treasury has also taken additional steps to assist the commercial real estate market. Treasury issued real estate mortgage investment conduits (REMIC) guidance to provide additional flexibility to special servicers and borrowers in working out their distressed loans. Lastly, bank supervisors issued Commercial Real Estate (CRE) guidance in October 2009 providing additional clarity and flexibility among banks to work out their loans with their performing borrowers, and to those loans which are not performing will need to be written down. Government actions have brought down the base cost of credit, and by keeping it there, have prevented tough CRE conditions from becoming worse.

   In terms of addressing the troubled CRE assets held by banks, the regulators (OCC, FDIC, Fed, and OTS) issued CRE guidance in October 2009 providing flexibility in working with those borrowers who are current on their loans as well as guidance to write down those loans which are not current. Although too early to fully capture the impact of this guidance, the regulators have instructed their supervisors to provide preliminary feedback.

   Recovery of the commercial real estate market ultimately depends on restoring a robust, thriving economy with strong job creation that stimulates demand for existing and new projects. Winding down government programs is an essential part of that recovery. The commercial real estate market will not become fully stable until temporary government supports are reduced so buyers and sellers can price transactions with confidence that demand, supply and cap rates are driven by the private sector.

2. **What will prevent banks from passing on the costs of the proposed bank tax to consumers, as the Congressional Budget Office has warned?**

By levying a fee on only the largest firms – thereby excluding over 99 percent of financial institutions – the Financial Crisis Responsibility Fee will place its heaviest burden on the firms that pose the greatest risks to the financial system and those that received the biggest benefits of assistance, both directly and indirectly. This also significantly reduces the ability for firms to pass along the cost to businesses and consumers, as they would risk losing business to the 99 percent of financial institutions that are not covered by this fee. It is those smaller institutions that provide the majority of loans to businesses and farms across the country. On this front, the CBO noted that the fee "would improve the competitive position of small- and medium-size banks, probably leading to some increase in their share of the loan market."

3. **Please point me to what you are doing to ensure that the ongoing concentration of mortgage lending and financial services, in general, is not further concentrated into the big 4-6 financial services companies. (Specifically, the top 4 mortgage lenders have over 50% market share, and growing, of the US market.) Is it your view that more concentration is better or worse for the US economy and taxpayers?**

Large banks in other countries are larger as a share of GDP than in the U.S. For example, U.S. banks with more than $500 billion in assets have assets of approximately 40% of U.S. GDP. The assets of our largest bank, JP Morgan Chase, are only 15% of U.S. GDP. In contrast, the UK's top three financial institutions are each greater than 100% of GDP.

We are committed to promoting a strong financial services market with properly aligned incentives and capital standards that advances both financial stability and competition. There are a number of protections currently in place that limit concentration in the financial services sector, in particular the 10% limit on bank deposit concentration. But more fundamentally, we believe that a vibrant and competitive financial services market is one which has consistent and transparent standards for all market participants. Our financial reform bill is a significant step in this direction and it levels the playing field for everyone and limits the advantages conferred on larger institutions.

Our financial reform proposal also has strong measures so that no firm in the U.S. should ever be too big to fail, including:

- Imposing higher prudential requirements (capital rules, liquidity rules, concentration limits, prompt corrective action, death plans) and more intensive supervision on very large and complex firms;

- Explicitly empowering the Federal Reserve to require systemic firms to sell assets or terminate activities if they endanger the firm or financial stability; and requiring the Federal Reserve to review large acquisitions by systemic firms to ensure that the acquisition does not impair financial stability; and

- Giving the government the tools it needs to facilitate the orderly demise of a failing firm, while imposing the costs of that failure on the common stockholders and other providers of regulatory capital of the failing firm – not the taxpayers.

Going forward, as part of our housing finance reform process, we will be carefully evaluating the mortgage finance system and will seek to implement reforms which promote competition and open access for market participants.

4. **During your testimony before the subcommittee on March 10, you stated that you would be happy to measure your record on fiscal responsibility with the previous 8 years. Can you please document with precise spending data and graphs how the Obama Administration has spent less than the Bush Administration (in a similar scale of time)?**

   The most straightforward way to compare our record on fiscal responsibility with that of the Bush Administration is to consider the effect that major policies have had on debt held by the public (net of financial assets). This captures the cumulative effect of tax and spending changes, inclusive of the increase in interest payments that is required when policies raise the deficit and result in additional government borrowing.

   The table on the next page summarizes the actual and projected contribution of several major policies—the Bush tax cuts, the Medicare Part D program, the war in Iraq, and the American Recovery and Reinvestment Act—to publicly held debt. The table also gives the impact of the recent recession on the current and future levels of government debt.

   As can be seen from the table:

   The total increase in debt held by the public from FY 2000 to FY 2009 was $3.3 trillion, of which about two-thirds ($2.1 trillion) was attributable to the Bush Administration's tax cuts.

   The total projected increase in publicly held debt (net of financial assets held by the government) from FY 2009 through FY 2020 is more than $10 trillion, of which $5.3 trillion reflects the Bush tax cuts, $2.9 trillion is attributable to the effects of the economic slowdown, and less than $1 trillion is related to the Recovery Act.

   These statistics demonstrate that virtually all of the deterioration in the Federal government's fiscal position reflects the policies of the previous Administration—specifically, the decision not to pay for a major extension in entitlement spending, a large tax cut, and a war—together with the effects of one of the most severe economic downturns of the postwar period.

Contribution of the Policies Listed Below to Debt held by the Public, Net of Financial Assets

(trillions of dollars)

	2000-09	2009-20	2000-20
Total increase in debt	3.3	10.0	13.4
Estimate of specific policy impacts on debt			
Bush Tax Cuts	2.1	5.3	7.4
Prescription Drugs (Medicare Part D)	0.1	0.8	0.9
Current Recession (automatic stabilizers)	0.3	2.9	3.3
ARRA	0.2	1.0	1.2
Sum of policies above	2.7	10.0	12.8

Note: Each contribution includes associated debt service

THURSDAY, APRIL 22, 2010.

FINANCIAL CRISIS AND TARP

WITNESSES

HERBERT M. ALLISON, JR., ASSISTANT SECRETARY OF THE TREASURY FOR FINANCIAL STABILITY

NEIL BAROFSKY, SPECIAL INSPECTOR GENERAL FOR THE TROUBLED ASSET RELIEF PROGRAM

Mr. SERRANO. The subcommittee will come to order. Good morning.

Today this subcommittee will examine the Treasury's responses to the financial crisis and the implementation of TARP. We are pleased to have two key witnesses on this topic. Leading off will be Herbert Allison, Assistant Secretary of Treasury for financial stability, who oversees the TARP program. He will be followed by Neil Barofsky, the special inspector general for TARP.

The financial crisis caused the deepest economic decline since the Great Depression in the early 1930s. Although the economy has stabilized since the freefall of late 2008 and early 2009, credit continues to shrink and unemployment remains near 10 percent. We have a long way to go before most Americans will feel that the economy is back on its feet again. We need to understand the role TARP has played or could play in responding to our economic problems.

TARP funds have been used for a variety of purposes. Roughly 700 banks have received capital infusions, totaling more than $200 billion. With several major modifications along the way, TARP funds have been used to provide mortgage modifications to homeowners. Support for the auto industry has totaled more than $80 billion. Funds were set aside to back up efforts to revive flows for credit, for small businesses, students, and consumer credit cards. TARP funds have also provided a backstop for Federal Reserve actions with AIG.

There is also a budget angle to today's hearing. The TARP legislation allows Treasury to spend on administration whatever it decides without further congressional check. To decide how much to appropriate for Treasury, however, this subcommittee needs to understand how much Treasury is spending because of TARP and where it draws the line between appropriator funds and TARP-related money.

In addition, the TARP legislation created the SIGTARP and provided it with $50 million that authorizers tell us they expected to last the life of the TARP. They were granted another $50 million last spring. Last October, SIGTARP came to our subcommittee with an urgent request for $23 million to avoid having to shut down this spring. In other words, SIGTARP had made hiring and other commitments that far exceeded the funds that the authorizers thought sufficient to last through the life of TARP. We provided those funds for fiscal year 2010, and SIGTARP has requested another $49 million for fiscal year 2011, far more than the $30 million annual budget for the Treasury Department's IG.

We look forward to hearing from our witnesses how effective each of the various TARP initiatives have been in restoring a healthy flow of credit, a growing economy, and relief for worthy borrowers. And we welcome you to our hearing today.

With those opening remarks, I would like to recognize Ms. Emerson for any comments she may want to make.

Mrs. EMERSON. Thank you, Mr. Chairman.

Secretary Allison, thank you so much for being here today. We are grateful to you.

The Emergency Economic Stabilization Act was passed by Congress to buy troubled assets. I am very disappointed that both the current and the former administrations have instead used this authority to bail out banks and to become majority or nearly majority owners of AIG, Citigroup, and auto manufacturers.

Acquiring stock shares and lending hundreds of billions of borrowed dollars across the financial sector with little accountability or transparency in return is not what we in Congress intended. It is impossible to justify to taxpayers why banks received billions of dollars without being required to increase lending, account for the funds they received, or take meaningful steps to limit executive compensation.

Most of the experts I talk to in Missouri see little sign of how TARP improved the financial environment they work in every day. And I am concerned that many of the troubled assets TARP was meant to purchase still exist. They may still be out there, hindering our economic recovery. No way do the expenditures of TARP to rescue troubled assets even begin to approach the estimates still being made today of how many troubled assets continue to exist in our country's financial sector.

Despite the taxpayers' investment in banks in 2008 and 2009, the FDIC reported that bank lending declined in 2009. The Missouri small-business folks I talk to all tell me that credit is still very, very hard to get, even for businesses with perfect—and I mean perfect—credit histories. In addition, meaningful steps to reform executive compensation have not been taken, home foreclosures and unemployment are still unacceptably high, and some experts project a crisis in the commercial real estate market.

I understand that $186 billion of TARP funds have been returned, and I am very pleased that Secretary Geithner previously testified before our full committee saying that the funds repaid to TARP should be used for deficit reduction and not new government spending.

Regarding the costs of the Office of Financial Stability—regarding the costs that you all's office incurs to administer the TARP programs, I am concerned that you estimate spending at $298 million in mandatory funding for fiscal year 2011. And I hope that you will explain this to us because I need to understand why this level the administrative spending is necessary, given that most of the TARP funds banks received have been returned and all of the TARP programs should be winding down during fiscal 2011.

Despite my concerns, I know that you and all of the staff at the Office of Financial Stability are working hard to improve our Nation's economy, and I am grateful and appreciative of your efforts.

Thanks, Mr. Chairman.

Mr. SERRANO. Thank you.

Mr. Allison, you know the drill. Five-minute presentation, your full statement will go in the record, and then we can ask you some questions. Please proceed.

Mr. ALLISON. Thank you very much, Chairman Serrano and members of the subcommittee. Thank you for the opportunity to testify today regarding the Troubled Asset Relief Program, or TARP.

Many Americans believe that the Federal Government bailed out Wall Street and forgot about Main Street. But what many Americans at first viewed as a distant financial crisis on Wall Street posed the risk of devastating consequences for Main Street.

In the fall of 2008, we faced the possibility of a second Great Depression. Credit markets froze, and people lost confidence in the banking system. Without credit and confidence, our financial system was facing collapse. Had that happened, people would have not been able to use their credit cards to buy gas or groceries, families would not have been able to get a loan to buy a car or send their kids to college, businesses large and small would not have had the credit to buy inventory or pay their workers. People were seeing the values of their homes plummet and their retirement savings shrink. Without bold action, job losses that were already growing could have skyrocketed and our economy could have collapsed. So our government took unpopular but necessary steps, like creating the TARP program, to avert complete failure of the financial system.

Before we could start economic recovery, we first had to achieve financial stability. The American Recovery and Reinvestment Act and the Financial Stability Plan launched by the Obama administration provided economic stimulus and restored liquidity that have enabled businesses to resume hiring, provided much-needed financing to States, and improved consumer confidence.

With the new administration, the focus of TARP changed from primarily investing in larger financial institutions to helping homeowners avoid foreclosures and improving small-business lending.

For the past year, TARP has been assisting distressed homeowners through the Home Affordable Modification Program, or HAMP, and other innovative methods. HAMP is now providing substantial relief to more than 1 million homeowners. Their mortgage payments have been reduced by about a third, or about $500 per month on average, for an estimated total savings of more than $3 billion to date.

We have recently enhanced HAMP to help more homeowners whose mortgages are under water and those who are temporarily unemployed to assure homeowners that they won't face foreclosure while being considered for a mortgage modification.

We have also launched an innovative program to provide additional relief to the 10 States hardest hit by the mortgage crisis and high unemployment.

The administration is also focusing its financial recovery efforts on small business. We are now seeking legislation to create a new $30 billion small-business lending fund outside of TARP that would provide small and mid-sized banks with capital on terms with strong incentives to increase small-business lending.

Additionally, Treasury will provide TARP funds to community development financial institutions, or CDFIs, to lend to small business. CDFIs play a vital role in providing financial services to some of the hardest-hit and poorest communities.

Together, TARP and the Recovery Act are already producing positive results. Jobs are being created. Borrowing costs for State and local governments have been reduced. Securities markets essentially frozen 15 months ago have reopened. And housing markets are showing signs of stabilizing.

With improving economic conditions and careful stewardship of taxpayers' money, TARP investments are delivering better returns than originally expected. We estimate that TARP will ultimately cost about $120 billion—far less than the maximum $700 billion appropriated by Congress.

200 billion dollars in repayments and income from TARP investments have already been reused to reduce the national debt. If Congress joins the President in enacting a financial recovery fee, TARP will not cost the American taxpayers a dime.

Because of the bold actions taken by Congress and the administration, our financial markets are more stable and signs of recovery are increasingly visible on Main Street.

Thank you very much, and I am happy to answer your questions.

[The prepared statement of Mr. Allison follows:]

Written Testimony of Herbert M. Allison, Jr.,
Assistant Secretary for Financial Stability
United States House of Representatives
Committee on Appropriations
Subcommittee on Financial Services and General Government
April 22, 2010

Chairman Serrano, Ranking Member Emerson, and Members of the Subcommittee, thank you for the opportunity to testify today regarding the Emergency Economic Stabilization Act of 2008 (EESA) and the Troubled Asset Relief Program (TARP).

Country Faced Economic Crisis

In October of 2008, the country faced economic difficulties not encountered since the Great Depression: credit markets were frozen; the global economy and the nation's economy were declining at an accelerating rate; and Americans had already lost trillions of dollars of wealth, in the value of their homes and in their savings. Interest rate spreads on credit cards and auto loans peaked at roughly 600 basis points, or six times their normal rates. This stagnation in the credit markets had a direct impact on Americans' daily lives: credit card limits were drastically reduced, obtaining a home loan became very difficult, and cars became more expensive due to the increased cost of credit.

Purpose of TARP

TARP is part of a broad effort by the Administration to promote financial stability and to stimulate the economy. The purpose of TARP was to restore liquidity and stability to the financial system, and the beneficiaries of TARP are the American people. Financial stability is a necessary precondition for economic recovery and growth. Investment of taxpayer funds in financial institutions was necessary in order for this stabilization to occur. These investments directly and indirectly continue to benefit taxpayers by re-establishing the willingness of banks to lend to consumers, by keeping interest rates low, and by helping homeowners stay in their homes. The TARP programs were created in order to benefit the American taxpayer.

Financial System Showing Signs of Stability

Our financial system has experienced a partial but significant recovery over the past year. The condition of most securities markets and large financial institutions has improved substantially. Borrowing costs for large banks, nonfinancial businesses, and state and local governments have returned to near normal levels. Securities markets that were essentially frozen a year ago have reopened, allowing businesses to issue over $1 trillion in debt without government guarantees. Prices for many "legacy" securities most exposed to losses that were held by banks have improved, and trading in these assets has resumed. Large banks are better capitalized than they were before the crisis, and restructuring in the financial industry is well underway. Housing markets are also showing signs of stabilizing. All of these indicators ultimately benefit the taxpayer. Stabilization of the financial system was a necessary precondition to many of the specific efforts we have undertaken to assist our citizens.

Government policies are responsible for many of the improvements to date. A combination of federal loans, capital injections, and guarantees has helped restore investor confidence in U.S. financial markets and institutions, which has translated into lower borrowing costs. The "stress test" of our largest financial institutions provided the transparency necessary for them to raise substantial capital from private sources to absorb losses from the crisis and repay government investments. Securitization markets important for consumer and small business loans have also improved, in large part because of a joint Treasury-Federal Reserve program, the Term Asset-Backed Securities Loan Facility (TALF) supported by TARP. The recovery of the securitization markets has helped increase the availability of credit for consumers and small businesses and has helped lower the cost of that credit. Availability of credit is critical for small businesses to grow and for consumers to make home improvements, buy a new car, or send their children to college. Additionally, the health of the securitization markets, and the companies that issue asset-backed securities, has had a positive impact on employment throughout the country. It is not just financial firms that rely upon the securitization markets for funding. Car companies, student loan companies and many small businesses are examples of non-bank institutions that need functioning capital markets in order to succeed. TALF helped accomplish this.

Home sales are improving due to a combination of housing policies. Mortgage rates are near historical lows, thereby stimulating home sales and refinancing. The American Recovery and Reinvestment Act of 2009 (Recovery Act) continues to improve the employment outlook, provide important support for state and local governments, and lay a stronger foundation for long-term economic growth. The improved health of the banking system is enabling some institutions to repay TARP funds.

TARP Funds Generated A Positive Return For Taxpayers

Treasury now expects to *make* – not lose – money on the $245 billion of investments in banks made through TARP programs. This is in sharp contrast to the original 2010 President's Budget estimate that Treasury's investments in the banks would cost taxpayers $79 billion. In fact, Treasury is being repaid at a very substantial rate. As of April 16th, banks have returned $176 billion in taxpayer investments – nearly 75% of all TARP funds invested in the banking system—and TARP has received $19 billion in dividend and warrant proceeds from banks.

In addition, Chrysler Financial has fully repaid (with interest) the $1.5 billion loan that it received. Just this month, General Motors made another repayment to the government in the amount of $1 billion. Repayments from all TARP recipients now total $181 billion, well ahead of last fall's projections for 2010 and represent repayment of nearly forty-six percent of all TARP disbursements to date. These early repayments are testaments to the success of the government's efforts to stabilize and rehabilitate our financial system.

TARP Costs Significantly Less Than Expected

Before President Obama took office, nearly $240 billion of taxpayer money had been invested into banks, accounting for about three quarters of the assets of the entire banking system. In addition, the Federal Reserve, Treasury and FDIC put in place guarantees and special liquidity facilities that amounted to trillions of dollars.

Since President Obama has taken office, Treasury has taken steps to dramatically bring down the cost of TARP and to shift its focus to small business and housing. As of the midsession review of the 2010 Budget, the projected cost of TARP was $341 billion. At that time, the Administration removed a $250 billion reserve included in the 2010 Budget, originally earmarked should additional stabilization efforts be necessary. After improved financial conditions and careful stewardship, the 2011 Budget projects the total costs of TARP to be less than $127 billion[1]. If Congress joins the President in enacting the financial recovery fee, American taxpayers will not have had to pay a penny for TARP.

TARP Exit Strategy

Because the various TARP investments have helped to stabilize the financial system and many have earned a positive return for taxpayers, the Administration is winding down many of its programs. As the President has previously said, Treasury will seek to exit its TARP investments as soon as practicable, in a manner protecting the taxpayers' interests. This will mean different timetables for different programs and institutions. For example, some institutions are thriving and have the ability to repay Treasury now or in the very near future. Other institutions will need more time to recover and repay Treasury, which is to be expected given the nature and impact of this financial crisis.

Treasury has already wound down many of its largest investment programs. The Capital Purchase and Capital Assistance Programs have closed. The Asset Guarantee Program, which generated positive returns for taxpayers, has been terminated. The previously discussed TALF has ceased making loans against collateral other than newly issued commercial mortgage-backed securities, and the final subscription for new issue commercial mortgage-backed securities is expected in June. We currently anticipate that TALF, as well, will generate positive returns for taxpayers.

Most of the TARP programs have ended or are ending, and our focus has shifted to continuing our careful management of those investments, protecting homeowners and stimulating small business lending.

Focus on Helping Homeowners

As the Obama Administration came into office last year, the country faced extraordinary economic and housing market conditions that required the rapid introduction of unprecedented policies designed to stabilize the housing and mortgage markets. On February 18, 2009, President Obama announced a comprehensive Homeowner Affordability and Stability Plan (HASP), which sought to address the issue of mortgage affordability for millions of struggling homeowners in America.

The Administration's goal is to promote stability for both the housing market and homeowners. To meet these objectives, the Administration has developed a comprehensive approach using mortgage modifications and refinancing, support for Fannie Mae and Freddie Mac, tax credits for homebuyers, state and local housing agency initiatives, and neighborhood stabilization and community development

[1] The 2011 Budget estimated the deficit impact of TARP to be $117 billion, including programmatic costs and downward interest on reestimates of approximately $10 billion.

programs. With the record-low mortgage rates seen this past year and, thanks in large part to these programs, more than four million homeowners have refinanced their mortgages to more affordable levels helping to save more than $7 billion in the past year; more than one million homeowners have had a reduction in mortgage payments averaging $500 per month through trial-period and permanent loan modifications under the Administration's mortgage modification program; home equity (wealth for homeowners) increased by more than $13,000 for the average homeowner in the last three quarters of 2009; and the economy is growing.

Our housing initiatives must balance the need to help responsible homeowners struggling to stay in their homes, with the recognition that we cannot and should not help everyone. The President has said: "We can't stop every foreclosure." And in fact, we can't maintain this balance if we try to assist every borrower. For example, investors and speculators should not be protected under our efforts, nor should Americans living in million-dollar homes or defaulters on vacation homes. Some people simply will not be able to afford to stay in their homes because they bought more than they could afford. Instead, the Administration must focus on providing responsible homeowners opportunities to obtain a modification or to refinance and prevent avoidable foreclosures and, when necessary, facilitate the transition to a more sustainable housing situation. The newly announced adjustments to the FHA and Home Affordable Modification Programs are tailored to accomplish these goals by helping a targeted group of borrowers.

Treasury has set aside $50 billion in TARP funds to address the housing problem. Programs targeting this problem include first-lien modifications, second-lien modifications, Home Affordable Foreclosure Alternatives Program (HAFA) and the newly announced adjustments to the FHA Refinance Program designed to address borrowers with significant negative equity situations.

On February 19, 2010, we announced the $1.5 billion HFA Hardest-Hit Fund for five state HFAs in the nation's hardest-hit housing markets to design innovative, locally targeted foreclosure prevention programs. On March 29, 2010, we announced a $600 million expansion of that program for an additional five states. Overall, we anticipate that all of the housing programs together will utilize the $50 billion allocation in full.

Focus on Small Businesses

The other area in which Treasury anticipates an ongoing commitment is helping small businesses. Recently, Treasury announced final terms for the Community Development Capital Initiative (CDCI) program that will provide TARP funds to Community Development Financial Institutions (CDFIs) to lend to small businesses. The CDFIs play a vital role in providing financial services to some of the hardest-hit and poorest communities. This program will help deploy funds to the communities that most need the funds by leveraging the valuable experience of CDFIs.

Additionally, we launched a program for Treasury to purchase, using TARP funds, securities that have been guaranteed by the Small Business Administration (SBA) under its section 7(a) program, and we conducted our first purchases on March 18th. This program is designed to provide additional liquidity through the secondary market so that banks using SBA programs will have increased capital to lend to small businesses. This program – combined with Recovery Act provisions that temporarily increased SBA loan guarantees and reduced fees –has helped significantly increase SBA loan volumes and secondary market activity.

Finally, the Administration has called for the creation, through legislation, of a new $30 billion Small Business Lending Fund outside of TARP to invest capital in community and smaller banks with incentives to support additional small business lending. The Administration is also working with Congress to consider additional ideas that might be included in the Small Business Lending Fund proposal.

Promoting Long Term Economic Stability- The Need for Regulatory Reform

The financial crisis was in large part the result of failures in government policy and oversight, failures in the design and enforcement of rules and regulation. But we are still living with the same financial system that brought us to the edge of collapse, and the success of the crisis response, without financial reform, will make future crises more likely. Even with improving credit markets and reduced borrowing costs, when we speak with businesses across the country, they tell us that banks are lending less, in part because they are not certain what new rules are coming. Delaying reform forces them to live with that continued uncertainty. Financial reform is necessary to help prevent future crises and bring certainty to the families and businesses that depend on the financial system to protect their savings and finance their home purchases, college educations, or business growth.

Today, the financial system is operating under the same rules that led to its near-collapse and to the recession. These rules must be changed to address the moral hazard posed by large, interconnected financial institutions considered "too big to fail." The Administration has proposed comprehensive financial reforms that seek to address this moral hazard by forcing these institutions to internalize the risks they impose on our financial system and to remove expectations of government support.

As we look ahead, we must not forget the lessons we have learned from this period. We need to reform our nation's laws to provide stronger, more effective regulation of our financial system and to protect consumers. Reforming our regulatory system in a way that is stronger and better suited to manage risk and ensure safety and soundness must be our highest priority.

Conclusion

The Congress has played a critical role in pulling our financial system back from the brink of collapse. We have made great progress to date, but it is important that we continue this progress by focusing on small businesses, the housing issue and comprehensive regulatory reform.

Mr. SERRANO. Thank you so much for your testimony.

Let me, just on your last comment, what you are saying, I think, is that we may allocate as much as the $700 billion, but at the end of the day it may cost $120 billion because the rest would have been paid back?

Mr. ALLISON. Yes, that is correct. In fact, we have not invested the entire $700 billion.

Mr. SERRANO. Okay.

Mr. ALLISON. We plan to invest about $535 billion. And already we have seen that the investments in the banks, which have amounted to about $245 billion, have produced returns of about $20 billion. And we have been paid back about 70 percent of that money.

Mr. SERRANO. So did we, the Congress or the administration, overestimate the need?

Mr. ALLISON. I think——

Mr. SERRANO. Because there was, what, 787, right? Oh, I am sorry.

Mr. ALLISON. Well, that was the stimulus act.

Mr. SERRANO. Numbers here, numbers there. Okay.

Mr. ALLISON. Actually, many people——

Mr. SERRANO. Well, that is an area code in Puerto Rico. Either way.

Mr. ALLISON. Right.

A lot of people conflate the Recovery Act with TARP. And TARP's purpose was to achieve financial stability, and, of course, ARRA was to recover the economy.

Mr. SERRANO. Right. But you are saying that, at the end of the day, it may cost $120 million?

Mr. ALLISON. It could. Now——

Mr. SERRANO. But then you also said it may not cost a dime.

Mr. ALLISON. Exactly. Let me explain that.

A year ago, the estimated cost was $341 billion. By last fall, the estimate was down to $117 billion. That is the number I am using here today.

We will be updating this number again. We expect that the cost could come down further. We have been encouraged by developments at AIG and General Motors, the car companies. We are starting the sale of Citigroup shares very soon. And we are doing our best to move out of these investments as rapidly as we can, consistent with protecting the interests of taxpayers.

Mr. SERRANO. Okay. I would just give you a little bit of advice, which usually we give at the end of the hearing, not at the beginning. But whatever office it is you have that puts out that information—I think Ms. Emerson would agree with us—should be putting it out a little better. Because the public's perception is that it may be going down a hole. And you are telling us that, at the end of the day, it may not cost a penny. So I think people need to know that.

Mr. ALLISON. Thank you.

Mr. SERRANO. Mr. Allison, as we consider the Treasury and SIGTARP budgets for next year, it is helpful to understand your plans for TARP activity and the relationship between your budget and the rest of the Treasury budget.

You run the Office of Financial Stability, where most of the TARP administrative expenses seem to be incurred. Our regular appropriations has always funded Treasury efforts on financial stability. How does the Department decide what TARP pays for and what the regular Treasury appropriation pays for?

Mr. ALLISON. We keep very careful track of our expenditures. We have our own finance department within TARP, which is unusual for a government program.

We have also established an internal review department within TARP that monitors all of our expenditures. They are currently auditing these expenditures to make sure that all of the money allocated to TARP is spent only on TARP activities and not on Treasury activities.

Mr. SERRANO. And that is pretty much established?

Mr. ALLISON. Yes, sir.

Mr. SERRANO. I mean, if people were to look at it or the press were to ask, you could see that clearly?

Mr. ALLISON. Yes, sir. And we also work closely—our own financial people work closely with the GAO and the special inspector general and other oversight bodies who are also concerned with making sure that we only spend TARP funds on TARP matters.

Mr. SERRANO. Also, last June, the report language for our bill asked the Treasury for detailed information on the staffing and budget for specific TARP-related activities. On March 10th, when I expressed my disappointment in the information that had been provided, Secretary Geithner replied, and I quote, “We will provide that information as quickly as we can. I assume we can do it quite quickly, but I just want to underscore we are now in the process of winding down TARP.” That is the end of his quote. Six weeks later, we have yet to receive any additional information as for winding down TARP.

The budget documents show the FTEs in your Office of Financial Stability are expected to increase from 260 this year to 271 next year. So the question is, when will the Department finally provide us with how the TARP-funded staff is being assigned by subject area, as specified in our report language, and the same for your contract employees?

And the February budget documents for your office show an estimate for contractor services this year at $314 million, up from an initial estimated $213 million. What are the services that you are buying, and why did the estimate go up almost 50 percent?

Mr. ALLISON. Yes, sir. First of all, we are still increasing our staff. We expect that our staff could be in the high 260s or in the 270s by the end of this fiscal year. After that, it will begin coming down somewhat. We project 271, as you mentioned, for the end of the next fiscal year.

The reason why the staff is still increasing is that we are still improving our control systems, and we are building systems that can last us the years that TARP continues to operate. Even though we will stop making new investments on October 3rd, we will still have to monitor these investments. We are very concerned about protecting the taxpayers’ interest. That means having very strong controls and oversight and reporting capabilities. So our increases are devoted to those functions. And we will be winding down other parts of our program over time as we are repaid.

Now, while we have received about 70 percent of the funds back from the banks, relatively few banks accounted for those funds. And so we still have well over 600 banks whose moneys we have to oversee. So the burden on the staff has not been reduced materially by being paid back all those funds.

Mr. SERRANO. You say there are 600 banks that have——

Mr. ALLISON. Over 600 banks, yes. And this is primarily today. It is no longer a large-bank program. The large banks have repaid. Today, we have over 600 banks that are mid-sized and small banks. So our program today is a small-, mid-sized-bank program, not a large-bank program. But it requires that we monitor the funds of 600 different institutions.

Mr. SERRANO. And what is it that these small and mid-sized banks are not doing? They are not reporting back on time?

Mr. ALLISON. Actually, sir, the banks are reporting.

Mr. SERRANO. Right.

Mr. ALLISON. We require reports from them monthly and quarterly.

Mr. SERRANO. Right.

Mr. ALLISON. By the way, those are all disclosed on our Web site. We also disclose all of our transactions, and have, within 48 hours after the transactions are consummated. We provide fulsome reporting, and we continue to improve our reporting for the public. And that is available on financialstability.gov.

Mr. SERRANO. All right. Thank you.

Mrs. Emerson.

Mrs. EMERSON. Thanks, Mr. Chairman.

Secretary Allison, one of the things that really is still troubling me, and maybe you can make me feel better about this, really is the question of the viability of our financial institutions.

I watch and hear from different economists, from one spectrum to the other philosophically, talking about the current tactics of financial institutions is to kind of extend and pretend with the mountain of debt caused by assets still on their books from the collapse of the mortgage-backed derivatives market in 2008. And so, I am really worried, still, that we haven't gotten to the crux of the problem yet.

And back in November of 2009, Dominique Strauss-Kahn of the IMF said that only 50 percent of all the bad assets held by banks had been declared to that date. And on October the 26th, IMF is actually scheduled to release the next Global Financial Stability Report, and we have been told that the percentage of unreported bad assets may go up as high as 66 percent in that document.

So I guess I have four short questions to ask you: one, if you agree with Mr. Strauss-Kahn's numbers. How would you define a bad asset? As banks leave the TARP, what provisions are being made for ensuring a more complete disclosure on remaining bad assets? And, four, have you all looked at why the audits for the banks have not been used to disclose these bad assets?

Mr. ALLISON. Well, first of all, we have been watching the situation of the mid-sized and smaller banks. You referred to the commercial real estate and bank portfolios. Those are concentrated primarily in mid-sized and smaller banks. These are banks to which we still have advanced funds, as I mentioned earlier.

By the way, we do not get repaid until the regulators of the banks approve repayments. And the regulators are the ones who are most responsible for overseeing the financial condition of the banks. That is not a function of the Treasury Department. So, again, we rely on the regulators.

However, as we have looked at the commercial real estate issue, while we do think it is a serious challenge for these institutions, we do see that actions are being taken to moderate that problem. There have been, first of all, write-downs of those assets, and, therefore, their values today have been written down, in many cases substantially, closer to the present value of those investments.

And so we are pleased to see that the accounting is coming to terms with the actual condition of those assets.

Mrs. EMERSON. Do you believe that all the bad assets—I mean, they have been written down, but, I mean, what do you all estimate still exists in the financial community? And I need you to define what you believe a bad asset is.

Mr. ALLISON. Well, I think what we have found—"bad asset" is a vague term, of course, and I don't think we have a precise definition for what a bad asset is. However, there were assets that were seriously troubled because they could not be traded. They couldn't easily be valued because there were no markets that were highly liquid at that time during the height of the crisis. So banks didn't know, in some cases, what the assets were worth or what the other bank's assets were worth. And so trading between banks, which is necessary for a fully functioning money market, for example, was breaking down. That is why TARP was so necessary: to provide additional confidence.

I think now some markets have reopened. Spreads on assets are down substantially, meaning that those assets are viewed as less troubled today than they were a year and a half ago. And there has been a tremendous improvement in credit spreads, which are indicative of the risk seen in those assets by the markets.

So I think what you see is the situation of the banks is much healthier than it was before. Many banks of all sizes have improved their capital ratios. They hold more equity in other capital as a percentage of their total assets today, so they are better able to support those assets. At the same time, the assets have been written down in value. So the overall condition of these banks, by and large, is far stronger than it was before.

Mrs. EMERSON. But, yet, they are doing nothing about lending to small businesses. You know, they are not taking—I mean, when they have customers who seriously—and I have had several meetings over the past few weeks with small-business people who have tremendously perfect credit scores, who actually have been growing their businesses in spite of the bad economy, and yet either they can get loans at 8 percent, which is ridiculous given the fact that the banks are borrowing at 0 or maybe 0.2 percent or something like that, and yet they are not lended out any money.

And then, you know, the examiners are saying, well—they are being very difficult on the one hand, but then you are saying that the regulators are really the people who are in charge. But, yet, the regulators are also the people who let us down in the first place.

So I am not as optimistic as perhaps you are, and I need you to just convince me that I should be.

Mr. ALLISON. All right. Well, Congresswoman Emerson, you point out an issue of real concern. And we agree that lending did decline. Small businesses especially have been hard-hit by this because they don't have the same access to the capital markets that larger corporations do. And small businesses are the creator of many jobs in this country, so it is vitally important that they have access to borrowings and capital.

So we have been meeting with small businesses and with banks of all sizes, including just last week, to ascertain from them what is the state of lending. Now, it is normal that in a deep recession, like we have just had, lending contracts for a number of reasons. First of all, the banks are suffering losses, they pull back, they are trying to conserve capital, they are very cautious, they raise their landing standards, typically. Small businesses and large businesses pull back initially, as well, because they were concerned about dropping revenues, and they weren't sure they wanted to take on the risk of additional borrowings.

Now the economy has improved significantly, and the financial markets have, as well. We have been told by banks as recently as last week that they anticipate increasing loans to small business, for example, this year. They were uniform in saying this to us. Now, we are going to be meeting with them every quarter because we want to make sure that they are following through with this.

We also have proposed to Congress the establishment of a $30 billion small-business loan fund. And it has terms in it, if it is passed, that would provide very strong encouragement to banks to lend. Because the more they lend, the lower the dividend rate that they will be paying on this capital. But they are going to have to perform before the rate comes down.

Mrs. EMERSON. I appreciate that. And we will follow up when it is my next turn to ask questions on the small-business lending. Thanks.

Mr. ALLISON. Sure. Thanks.

Mr. SERRANO. Commenting on when your next turn comes up, we will have better attendance than usual today, so we will—and we have some votes lurking in the near future, so we will adhere to the 5-minute rule.

With that in mind, Mr. Edwards.

Mr. EDWARDS. Thank you, Mr. Chairman.

Mr. Allison, as I recall, according to former President Bush, his Chairman of the Federal Reserve, Mr. Bernanke, and his Secretary of the Treasury, Mr. Paulson, all said in the fall of 2008 that we were potentially on the edge of facing a second Great Depression.

I realize there are some today in Washington that, for whatever reasons, would elevate the Herbert Hoover approach to preventing depressions to some exalted level. I am one who, along with President Bush, agreed we needed to take aggressive action.

There are some who would suggest that TARP was a terrible mistake. I would suggest to them that they should go back and see what happened to the stock market in the last 3 minutes of the first vote of TARP when literally hundreds of billions of dollars of families' life savings and businesses' savings were lost when the stock market went down 3 percent in the last 3 minutes of that vote when the market realized it was actually going down. I would have to believe if the market believed there wasn't a chance to come back and have a second vote, it might have even dropped more precipitously than that.

I think some who suggest the Herbert Hoover approach to getting us out of the terrible economic disaster we were facing forget that, in the year prior to the Great Depression, household wealth dropped by 3 percent, on average. I believe, in the year prior to this recession, or in the first year of the recession, household wealth dropped by 17 percent. You know, I think it was Sam Rayburn of Texas, maybe among others, who said, "It is awfully easy to kick down a barn. It is a lot harder to build one."

I want to talk about TARP. My first question would be to ask you, if you could send to this subcommittee a list of leading economic indicators going back to the fall of 2008 and then send us what those economic indicators are today. And I would like to just touch on those very briefly with a couple of very specific questions that might allow a short answer.

One, do you recall whether we had positive or negative economic growth in the last quarter of 2008?

Mr. ALLISON. I am not sure what the growth rate was. I will be happy to check for you.

Mr. EDWARDS. On an annualized basis, I think it went down about 6 percent. And then, after TARP and after the economic recovery efforts in the last quarter of 2009, if you had checked, I believe that economic growth, on an annualized basis, went up 5.7 percent. A lot better going up 5.7 percent than down 6 percent.

As I recall, and if I could check these numbers for our committee, the last quarter of 2008, the monthly job loss in America was about 700,000 jobs per month being lost. And I believe the last economic report said that America gained 162,000 jobs, last month I believe. So, instead of losing 700,000 jobs a month, we are gaining 162,000.

If you would check, I believe these numbers are close to correct, but in the year of 2008, the last year of the Bush administration, the S&P 500 that a lot of businesses and families have their investments in and children's college funds and their families' retirement funds, the S&P went down 38 percent. And I believe, since March of 2009, it has gone up over 70 percent. If you could verify those numbers, along with other economic indicators, and send that to the committee, I would appreciate it.

But I would like to, finally, ask you specifically—and you touched on this. But, had we not passed TARP, an effort to stabilize the financial system of the United States and even the world, do you think there could have been a high probability that we could have seen either a much deeper recession than we already have suffered through or even the odds were that we could have faced an actual depression?

And I remember what my father told me it was like to go through the first Great Depression. I certainly didn't want to go through a second one.

How serious of a problem were we facing in the fall of 2008 when President Bush asked Democrats and Republicans to support the financial stabilization bill?

Mr. ALLISON. Congressman Edwards, first of all, your comparisons are absolutely right. I think no one expected——

Mr. EDWARDS. Is your microphone on, Mr. Allison. I guess it was on. I am sorry. Please go ahead.

Mr. ALLISON. No one expected that we would see the recovery this quickly, a year ago. And I don't think it is possible to exaggerate how serious the financial and economic problem was in the fall of 2008. We were facing a potential catastrophe if action hadn't been taken quickly.

And I think that the people who were in the government at the time and especially the people in Congress who had to take a very difficult vote for TARP were courageous and bold to do so. And I think that those actions saved the financial system and saved the economy.

Mr. EDWARDS. Thank you.

Thank you, Mr. Chairman.

Mr. SERRANO. Thank you.

Mr. Crenshaw.

Mr. CRENSHAW. Thank you, Mr. Chairman.

Another way to answer that question that Congressman Edwards was talking about—and I think it is kind of clear and straightforward. Can you tell us, in your opinion, if we had done nothing, would that have been more expensive or less expensive than passing a TARP program?

Mr. ALLISON. Well, first of all, the TARP program is going to turn out to be far less expensive than anyone expected. It already has been.

And, secondly, the cost to the country of a financial collapse would have been immeasurable. We would have seen the financial system essentially destroyed in this country. It literally wouldn't have been possible for people to cash checks. There was almost a run—there started to be a run on money market funds, which many people depend upon for their cash. And so the government had to step in and guarantee $3 trillion of money market funds, overnight almost, to prevent a classic run of the bank, if you will, like we saw back in the 1930s.

This country depends on a strong financial system. Every day, people are using their credit cards. They are borrowing money for a car or for their house or for college education. Without this system, this economy can't function. It is part of the lifeblood of people's everyday lives. And so, it was essential at the time to take unprecedented action.

And because those actions were taken, we are recovering at a very rapid pace, far quicker than most people imagined a year ago. Now, we are not totally out of the woods. We——

Mr. CRENSHAW. No, but, just, I mean, I think whatever you are saying is that, you know, regardless of how much money TARP ends up costing—and it is going to cost less than we thought to start with—that is going to be less expensive than it would have been to do nothing. And that is your opinion. And I appreciate that, sir, because I happen to believe that.

Mr. ALLISON. Yeah.

Mr. CRENSHAW. Now, let me ask you—you know, everybody that comes before our subcommittee talks about, “We can’t sustain the kind of debt that we have, both on an annual basis or our total national debt. It is just unsustainable.” And so, people talk about how to get out of that mess. They talk about raising taxes. You hear about the value-added tax. You hear about the bank tax.

And let me ask you—it is interesting, because I would like to, kind of, go through those numbers again to see how much TARP is going to cost. But one of the things—when you say, maybe TARP doesn’t cost us anything, and that would be wonderful, but one of the proposals the President has made is a bank tax, I think he calls it a fee, that will raise $90 billion by taxing banks that have over $50 million, in terms of their deposits.

And one of the justifications for that tax or that fee is that that money would be used to pay back the TARP money. But you can see, if TARP didn’t cost us anything, then I guess you would agree that we wouldn’t need that $90 billion of new taxes to pay for the TARP that didn’t cost anything. Would that be correct?

Mr. ALLISON. What I said in my testimony, Congressman, was that we estimate—the latest estimate is that TARP would cost about $120 billion. And——

Mr. CRENSHAW. But if it didn’t cost anything—I mean, let’s assume—I hope you are right that it doesn’t cost anything. Then would you say, well, we don’t need to talk about this fee on banks to raise $90 billion. Because if you raised it, you might use it for something other than paying back TARP money, because it would have been paid back.

Mr. ALLISON. What I said, Congressman, was that if a financial recovery fee is enacted by Congress, TARP won’t cost the taxpayers a dime, because those moneys could offset——

Mr. CRENSHAW. So, best case maybe you would be $90 billion short, so you would assess a fee and have that $90 billion paid off. And I can appreciate that.

Let me go through those numbers because, as I understand it, there is $700 billion, but some of the money hasn’t really been spent. Isn’t there about $300 million just sitting in the bank?

Mr. ALLISON. Well, we were authorized to spend $700 billion. We estimate that we are going to utilize about $545 billion or $550 billion of that money.

Mr. CRENSHAW. So that is about $250 billion that you are not going to utilize?

Mr. ALLISON. It is about $150 billion, yes——

Mr. CRENSHAW. Okay.

Mr. ALLISON [continuing]. That we don’t expect to utilize.

Mr. CRENSHAW. Now, what are you going to do that? If you don’t utilize it, would you ever consider paying down the national debt or giving it back? Or would you, kind of, hang on to it just in case you need it somewhere along the way?

Mr. ALLISON. Well, our ability to invest these funds expires on October 3rd of this year. And any money——

Mr. CRENSHAW. Well, what are you going to do if you have $150 billion on October 3rd of this year?

Mr. ALLISON. All of that goes back——

Mr. CRENSHAW. Where does it go?

Mr. ALLISON [continuing]. To the Congress. Well, we have not spent it. That would be used to reduce, along with the moneys we receive back, the national debt—or the perceived planning of the national debt.

Mr. CRENSHAW. You wouldn't spend it on something else?

Mr. ALLISON. No, sir.

Mr. CRENSHAW. Okay.

Thank you, Mr. Chairman.

Mr. ALLISON. All the money we receive back goes into the Treasury to reduce the national debt.

Mr. CRENSHAW. Thank you.

Mr. SERRANO. You said exactly what he wanted to hear.

Mr. Boyd?

Mr. BOYD. Thank you, Mr. Chairman.

And thank you, Mr. Allison, for your years of service to the country.

I want to focus on CDCI.

Mr. ALLISON. Yes, sir.

Mr. BOYD. You alluded to it briefly in your opening remarks. And I think most of us understand what it is designed to be.

And one of the things that we find out in our communities is that our CDCI applications have—they are dragging out, and they have very long waiting periods before approval or denial.

Can you bring the committee up to speed on how CDCI is working in our communities to provide TARP funds in a timely manner? You know, obviously, the objective there is to infuse capital into our small businesses and those troubled, mostly rural areas.

Mr. ALLISON. Yes, sir. And, Congressman Boyd, thank you for asking about the CDFIs. We believe and we know that they provide an essential service, especially in disadvantaged areas of this country that are not banked. Many banks don't even have branches in some of these areas where the CDFIs operate. So they are providing a vital and a unique role in the communities where they operate.

So we believe it is very important to assure their continued operation during this very difficult time. And so we have already instituted a program for CDFIs. These are regulated CDFIs that provide the bulk of the lending and assets to those communities.

And we are seeing very strong interest in this program. The application period to participate in our capital program, where we can make capital available to the CDFIs, up to 5 percent of their risk-weighted assets, on very good terms, that program, the application period expires on April 30th. So we have been urging them and the Secretary has written a letter to the CDFIs urging them to participate in this program.

And we are very encouraged by the high percentage that are showing interest. And we expect a substantial number of the regulated CDFIs to participate, which means that more capital would be available to them so they can continue and grow their activities, where possible.

Mr. BOYD. So you have a cutoff date for applications of April 30?

Mr. ALLISON. Yes, sir.

Mr. BOYD. The approval or denial of those applications, has that already started?

Mr. ALLISON. Yes, sir. Yes.

Mr. BOYD. Is there anything that we can, as individual Members, be doing about the expedition of the decision of approval or denial?

Mr. ALLISON. Well, first of all, thank you for your interest in this program.

We are encouraged, as I mentioned, by the application rate, which is quite high. And the applications have to be processed through the regulators of these CDFIs. And I know the regulators are working hard to process those as rapidly as possible. So we do expect a large participation. And, of course, we will be reporting on all of this to the public.

Mr. BOYD. Okay. Have some of those applications already been approved or denied, or they will all be coming at once?

Mr. ALLISON. Some applications—a large number have already been forwarded to us by the regulators. So they have been approved by the regulators.

Mr. BOYD. Okay. Thank you very much.

Mr. ALLISON. Thank you.

Mr. BOYD. Thank you, Mr. Chairman.

Mr. SERRANO. Thank you, Mr. Boyd.

Ms. Lee?

Ms. LEE. Thank you very much.

Good to see you.

Mr. ALLISON. Thank you.

Ms. LEE. And I am one who was very skeptical about voting for TARP. You know, I am glad to see that the financial markets were stabilized and we saved the economy from going into a depression. And I am delighted that many of the goals of TARP have been or are being achieved.

But many of my constituents don't know that. And I will tell you why: Many don't have credit cards. Many don't have access to capital. Because they are minority-, women-owned small businesses, they can't get credit. Many have lost their homes due to the scams of the loan sharks. And I hope that there will be some criminal prosecutions of these individuals. And so it is very difficult to explain in terms of Main Street benefiting from this.

So I am curious in terms of how this administration, how you see us moving forward for those millions of people who really don't quite understand why we did this for the financial system and why in the world we can't require these banks and lending institutions to step up to the plate and lend to minority-owned businesses and small businesses. Because they are just not doing it. We had an opportune time to do that when we bailed them out. We didn't require them to do it. And now we are looking at many of our communities that are devastated as a result of the last 8 years, quite frankly.

And so, how do we begin to turn this around and make sure that these financial institutions that did receive TARP money know that they have a responsibility to be fair and to provide equal opportunities to small businesses and to minority-owned businesses? Because they just haven't done that.

Mr. ALLISON. Congresswoman Lee, we fully understand and appreciate your concerns. And you have been eloquent and very strong in speaking out about these things for a long time.

We have undertaken a number of programs addressed specifically at that point. The first is the CDFI program, because, as you know, in many of these communities the CDFIs are the only financial institutions that people can turn to.

Secondly, the Obama administration has set up a facility of about $23 billion for housing finance agencies to innovate approaches to deal with housing issues in these communities.

Thirdly, we have launched what we call the Help for the Hardest-Hit Housing Markets, which is a program designed to encourage HFAs in the 10 States whose people have been hardest hit by unemployment and house price declines to innovate solutions for those people; for instance, by helping to make more people eligible for HAMP modifications, for example, providing additional assistance to unemployed people.

We also, in Treasury, have been encouraging in our programs participation by minority groups. In fact, now we are launching, soon, our sale of Citigroup's stock, and Morgan Stanley has pledged to us that it will devote 25 percent of the economics they receive to minority- and women-owned firms. So we are committed to encouraging diversity in our own programs.

Much more still has to be done. And I think by shining a light on this issue and making it a high priority of the Obama administration, which, in addition to TARP and the other programs I mentioned, has comprehensive stimulus efforts, recovery efforts aimed at disadvantaged communities. We have to do more; I think this administration realizes that. And they have made all-out efforts to try to help in these areas.

Ms. LEE. Great. And I appreciate what you are doing futuristically and what we are beginning to do.

What I want to see, Mr. Secretary, is how—and I don't know if you have the numbers, the statistics, the reports on what lending these financial institutions—how they lend it, who they lended their money to. Did they lend to minority- and women-owned businesses? If so, what is the percentage? If not, we need to shine some light on it.

Mr. ALLISON. Yes.

Ms. LEE. I think we have anecdotal information, but I am not sure if we have the facts. And so I am wondering if we could ask you to report back to this committee the types of loans and to whom those loans went to these institutions that we bailed out.

Mr. ALLISON. Yes.

Ms. LEE. Because I think it is important that that never happen again. Because, you know, we raised a lot of expectations in many of these communities, and businesses have gone out of business because they could not get access to credit, regardless of whether TARP was there or not. They just froze it.

Mr. ALLISON. Yeah. We will be happy to follow up on that. Thank you for the question. We will come back to you.

Let me also mention, though, that in our housing program we have extensive reporting on the performance of the servicers in making modifications available. And we have been collecting data by race, for example, and gender since the beginning of this year. And as soon as we have statistically valid information on that, we are going to start reporting that, as well.

Ms. LEE. Thank you. It is very important, because these scam loan sharks—that is what I call them—they targeted minority communities. I mean, they didn't just do this de facto. They went in there and decided they were going after African Americans and Latinos. So it is very important that this report come out to show what has taken place.

And, also, I hope you will get back to us on the lending to minority- and women-owned businesses.

Mr. ALLISON. Thank you very much. We will do that.

Ms. LEE. Thank you very much.

Mr. SERRANO. Thank you.

Ms. Wasserman Schultz?

Ms. WASSERMAN SCHULTZ. Thank you, Mr. Chairman.

Thank you so much for your public service and for being with us this morning.

And I know that all of us feel that the whole notion of stabilizing our economy and creating jobs and getting the housing markets back on track—being a Floridian, that is particularly important, to make sure that we can continue to move forward.

And I read Mr. Barofsky's testimony, in which he discusses some of the missed TARP payments. And we have heard a lot of good news lately about Goldman Sachs and GM's payment of their debts in full. But I want to hear a little bit more about what you don't think is working very well and where there has been room for improvement. Which payments have you not yet received? And which have been late? And are there any that you anticipate not getting back at all?

Mr. ALLISON. We have had some banks not paying the quarterly dividends to us. If they don't pay us for six quarters, we have a right to appoint two directors to their boards.

Ms. WASSERMAN SCHULTZ. Okay.

Mr. ALLISON. We have had, though, I would say, given the magnitude of the crisis, a relatively low rate of outright losses. Today, the losses are a little over 1 percent of the total amount that was invested in the banks. But even with those losses, the total net return has been about 9 percent on the investments. And we have received over $20 billion of dividends and warrant proceeds and interest on those investments.

So, overall, this plan, this program, has benefited taxpayers. They have profited from this program, so far, substantially.

Ms. WASSERMAN SCHULTZ. In other words, we have actually made more back than we initially invested.

Mr. ALLISON. Yes. We have made about $20 billion on those investments.

Ms. WASSERMAN SCHULTZ. Wow. That is certainly something that I would love to see get out there more. Because the hatred of the TARP and the whole notion of TARP has been understandable because we certainly wish we were never in this situation in the first place. But the fact that we have made the investment back with interest, to the tune of $20 billion, that is an important point that Americans should know.

I want to ask you a little bit about the AIG subsidiaries, selling off AIG subsidiaries. There is a concern that AIG is selling off some of the better parts of its business just to repay the government. Is it AIG that is directing those sales, or is it the government looking to recover some of the money more quickly? And do you believe that AIG is cannibalizing its future earnings so that they can get short-term results?

Mr. ALLISON. First of all, let me emphasize that we are a reluctant shareholder in any of these companies.

Ms. WASSERMAN SCHULTZ. Yes.

Mr. ALLISON. And we would like to dispose of our investments in the stocks of AIG, General Motors, Citigroup as rapidly as possible, consistent with protecting the interests of taxpayers. We do not get involved in day-to-day decisions of these institutions, or strategic decisions.

We do expect that the asset sales that AIG is making today will enable the company to repay, first of all, the Federal Reserve for a large part or all of its investment. We do have continual communications with AIG about its condition and about its plans.

We are encouraged by the progress that the company has made, and especially the last 6 or 8 months. And we have seen the risk in the company come down dramatically. Financial Products, their financial products subsidiary, which was the cause of a lot of the problems in AIG, has dramatically reduced its exposures to the market. And so, we see a very positive trend so far in the improvement in AIG's condition.

Ms. WASSERMAN SCHULTZ. And, Mr. Chairman, forgive me, I was not here when you made your opening remarks. But, in my home State of Florida, restoring the housing market and helping ensure that we can keep people in their homes and prevent them from being foreclosed on is incredibly important. Our recovery is lagging behind the rest of the country.

Can you talk a little bit about the Hardest-Hit Fund, how that and other innovative ideas using TARP funds that are designed to help make sure that we can bring that part of the economy up?

Mr. ALLISON. Yes. Well, we think that the Hardest-Hit Fund is extremely important, especially in these 10 States. And Florida, of course, is one of those. And I believe Florida is receiving more than $400 million.

Ms. WASSERMAN SCHULTZ. Yes.

Mr. ALLISON. And this will enable the State, the housing finance agency and others, to look at the particular conditions within Florida and certain areas of Florida to see what methods might be used to assist in stabilizing the housing markets and relieving the pressure on homeowners in those areas.

And, as you well know, this housing crisis is highly concentrated in certain parts of the country. Southern Florida is one that has been particularly hard-hit, as you well know.

Ms. WASSERMAN SCHULTZ. Yes.

Mr. ALLISON. And, fortunately, what we do see are signs of stabilizing of prices. And that is going to be essential, so that we attract more demand for houses and we begin to stabilize and balance supply and demand in those areas.

So we are encouraged by some of these developments. Even though it has been extremely painful, maybe we are nearing the point where that market——

Ms. WASSERMAN SCHULTZ. Do you have that sense, that we are?

Mr. ALLISON. Our sense is that, increasingly we are seeing—some of the hardest-hit places are the ones where the prices rose the quickest.

Ms. WASSERMAN SCHULTZ. Right.

Mr. ALLISON. They came down the furthest. But they are actually maybe reaching a point quicker than some other parts of the country where they have an equilibrium of supply and demand. And so——

Ms. WASSERMAN SCHULTZ. From your mouth to God's ears.

Mr. ALLISON. Yes, well, we hope so.

Now, we are not complacent about this. That is why we just implemented this new program. We still think we have to do more. And, frankly, in the eyes——

Ms. WASSERMAN SCHULTZ. Pushing the banks to work mortgages out is incredibly important, as well.

Mr. ALLISON. Exactly. And we are also publicizing their performance. And, frankly, they still have more to do.

Ms. WASSERMAN SCHULTZ. A lot more.

Mr. ALLISON. All of them. And we meet with them continually. And we are seeing progress, but it is not fast enough. And I think, frankly, they need to invest more in their mortgage activities in order to reach the type of scale that we need.

However, let me mention that last month is the first month when we actually saw the servicers convert more mortgages to final modifications than they had new trial modifications. So it does show capacity is increasing, and we are starting to get on top of this problem. And we expect that we will have seen decisions made on trial modifications awaiting decisions. Most of those should be completed by the end of June.

But we are still working with the banks to increase their capacity. This is still a very serious problem. We still see the possibility of a million foreclosures in this country this year; maybe 3 million foreclosure starts, but usually about a quarter to a third of those turn into actual foreclosures. We are trying to prevent as many of those as we can.

And that is why we have the HAMP program. And we are encouraged that we have over a million people who have already benefited from that. But we want to make sure that people know the program is available. We want to make sure that the servicers—and we have already reached an understanding with the servicers. From now on, starting in June, they must look at every 60-day-plus delinquent mortgage to see whether the homeowner could be eligible for HAMP.

Ms. WASSERMAN SCHULTZ. That is good.

Mr. ALLISON. And so, that should also bring more people into this program. But we have to publicize it more.

Ms. WASSERMAN SCHULTZ. Yes.

Mr. ALLISON. We are holding events throughout the country, including in Florida, to——

Ms. WASSERMAN SCHULTZ. Let Members of Congress know how we can help you publicize it.

Mr. ALLISON. We will. Thank you very much.

Ms. WASSERMAN SCHULTZ. Thank you very much.

Mr. ALLISON. Thanks for your questions.

Ms. WASSERMAN SCHULTZ. Thank you for your indulgence, Mr. Chairman.

Mr. SERRANO. Thank you.

Mr. Culberson.

Mr. CULBERSON. Thank you, Mr. Chairman.

Secretary Allison, as a general rule, when a company accepts Federal dollars, they are subject to all the Federal rules and regulations. And, in this case, a company that has paid back the TARP money is still subject to all the Federal guidelines that they accepted the money under? Or are they completely free of Federal strings once they repay the money?

Mr. ALLISON. Once they have repaid the money entirely, they are free from the TARP restrictions. Of course, they are subject to all other laws——

Mr. CULBERSON. Certainly. But, I mean, in terms of the TARP restriction.

Mr. ALLISON. Yes, sir.

Mr. CULBERSON. And it is my recollection, didn't the original language of the October 2008 TARP legislation leave it—I don't know that it was mandatory, but is it the Secretary's discretion to use the money that is repaid to pay down the deficit?

Mr. ALLISON. The money that comes back to the Treasury that is repaid under the TARP program is put back into the general account of the U.S. Treasury for debt reduction.

Mr. CULBERSON. For debt reduction.

Mr. ALLISON. Yes, sir.

Mr. CULBERSON. But the Congress and this new Congress and the President have just routinely rechurned that money, so it is not—well, let me ask you this: Has any of that money been applied to debt or deficit reduction? Because if it has, I am not aware of it. I am not aware of any of that money being used to pay down the debt or the deficit.

Mr. ALLISON. Well, actually, I would be glad to send you information on this. But, so far, we received about $170 billion, roughly, in repayments—no, I am sorry, $186 billion. And we have received another $20 billion in proceeds from dividends and interest and sales of warrants.

Mr. CULBERSON. About $180 billion, and has that $180 billion all been used to pay off, pay down the debt or deficit?

Mr. ALLISON. Absolutely. It has been used to pay down the debt and the deficit.

Mr. CULBERSON. Then that is terrific. Is it going to continue to be any money that is paid back used to pay down either the debt or the deficit?

Mr. ALLISON. Absolutely and that is under EESA law.

Mr. CULBERSON. So that is required. It is mandatory. And it is not just, of course, the Treasury Department, but the Federal Reserve, FDIC have all been in the business of guaranteeing loans and ensuring, helping to provide some underpinning to a whole variety of industries. How much money and to whom has the Federal Reserve been loaning money?

Mr. ALLISON. I don't have the answer off the top of my head. We will be glad to contact the Federal Reserve and provide that information to you.

Mr. CULBERSON. You could provide that to the committee?

Mr. ALLISON. I will. We will request the Federal Reserve to provide it to you.

Mr. CULBERSON. Have they provided it to you? Has the Department of Treasury seen in detail how much money the Federal Reserve has loaned and to whom and under what terms?

Mr. ALLISON. I will find the answer to that for you, but my own department doesn't look at that, but I will see whether others in Treasury have done so.

Mr. CULBERSON. To your knowledge, has Treasury received that information from Federal Reserve?

Mr. ALLISON. I don't know.

Mr. CULBERSON. How much money, do you know a ballpark figure, as to how much money the Federal Reserve has either loaned out or guaranteed?

Mr. ALLISON. I don't have that information right in front of me, but if you would like, I will certainly try to get the information for you.

Mr. CULBERSON. Thank you. What about the FDIC, I understand they are also a part of this as well?

Mr. ALLISON. Well, the FDIC oversees——

Mr. CULBERSON. Sure.

Mr. ALLISON. It has had its own facilities where it has guaranteed borrowing for a period of time. That program has been terminated however.

Mr. CULBERSON. Has the United States Government, or excuse me, U.S. taxpayers, more accurately, ever guaranteed this much money in the private sector, this many loans, this much money on this broad of a scale ever in U.S. history?

Mr. ALLISON. I don't know. I would doubt it, but there hasn't been a crisis—this is, I think, a unique financial crisis that this country faced. And as I mentioned before in my testimony, it would have been catastrophic if actions hadn't been taken.

The cost to this economy would have been incalculable if these actions hadn't been taken. And what we have seen is, thanks to these actions, the economy has recovered far faster than most people would have dared to predict.

Mr. CULBERSON. What is the amount of money that the Secretary of Treasury has available to him to use under the TARP fund to continue to make loans or guarantees? You have got money coming back in that is repaid, but isn't there a continuing amount of money that the Secretary of Treasury has available to continue to use at his discretion?

Mr. ALLISON. The amount of TARP funding available that allocated at TARP was $700 billion.

Mr. CULBERSON. Right. You say $180 billion of that has been repaid, applied to deficit reduction. And that is gone; that has gone to pay off debt, right?

Mr. ALLISON. Yes. But the entire $700 billion has not been used. And as the Secretary announced when he extended TARP to October 3 of this year, we don't expect to use more than about $550 billion. We actually have made investments of about $390 billion, as I recall, but we plan to make, we have made commitments of about $491 billion, and we plan to utilize about $545 billion to $550 billion.

Mr. CULBERSON. And as that money comes back in and is repaid, you will apply that specifically to debt?

Mr. ALLISON. That is correct.

Mr. CULBERSON. Buying back U.S. Treasury debt?

Mr. ALLISON. It is done. It reduces the national deficit, yes, sir.

Mr. CULBERSON. And then the money is not reused? We will make sure——

Mr. ALLISON. The money is not reused.

Mr. CULBERSON. Thank you, Mr. Chairman.

Mr. ALLISON. However, let me be totally clear with you, as the money is repaid, that increases the head room, because the actual authorization remains constant at $700 billion. However, we are totally transparent that the money that has been repaid goes back to reduce the National Debt. We disclose all of the utilization of the money on our Web site, and the amounts that I have given you will indicate that we have not used the entire $700 billion.

Mr. CULBERSON. Maybe someone could follow up on that, Mr. Chairman, because it is still a little bit of source of confusion. The authorization level stays the same. You say you are paying down debt with it.

Mr. ALLISON. That is right.

Mr. CULBERSON. But you continue to churn within that $700 billion.

Mr. ALLISON. No, sir, because any new investment— under the law, we strict reply follow the EESA law. Any money returned to us is used to pay down the National Debt. Within the $700 billion, we may make additional investments, but we have not come close to utilizing the entire $700 billion, so it is really a moot point. So any money we return back goes to reduce the National Debt. We will be glad to give you a table showing you exactly what has been utilized so far and how much has been paid back.

Mr. CULBERSON. You are always gracious with the time. I have some follow up. Thank you, sir.

Mr. SERRANO. That is all right. The gentleman answered about nine times it was going back to pay the National Debt. Just for the record.

But I understand your concern. It is the concern of many folks.

Last year the TARP was used to create new public-private investments to increase credit for small businesses, students, car buyers and other consumers. How would you evaluate the effectiveness of these programs in making more credit available for creditworthy small business, students and consumers?

Mr. ALLISON. The impact has been both direct and indirect. When the Public-Private Investment Program was announced about a year ago, it had an almost immediate effect on the credit spreads for Commercial Mortgage-Backed Securities and Residential Mortgage-Backed Securities. Those rates, you can trace it to the day of the announcement. The rates came in dramatically, which helped to improve the cost of credit throughout that sector of the financial markets.

And, since then, we have been working with nine investment managers to invest in this these types of instruments, which help to provide additional liquidity to the market and also price discovery, which stabilizes and creates more confidence in those markets.

And, again, that program will be also fully invested soon, and we plan no others because the markets have improved so much in terms of spreads returning to near normal, in many cases, that there is not a need for adding to that program.

Mr. SERRANO. My only concern would be that that is the program that speaks, those programs speak to areas where the people with the least power, if you will, in the society were benefited. So when you say we don't intend to add more to it or whatever, that is fine if everything is okay. But I would hope we know everything is okay before we decide to cut back on that.

Mr. ALLISON. Well, what we are seeing is that, even as that program nears being fully invested, we are seeing that the spreads in those markets remain quite low, especially compared to where they were at the height of the crisis. And they have returned to near normal in many cases. We would like to see more activity in those markets. That is going to take some time, but they have been improving and healing, thanks to these programs.

Mr. SERRANO. Right.

In the last year, banks have reduced their credit outstanding to commercial and industrial businesses by almost 20 percent or $300 billion. When businesses lose credit like that, they cut back jobs. Recently the financial press has reported that the financial services sector has paid out more than $100 billion in bonuses this year. Do you agree that the money, if retained instead of paid out in bonuses, could have been conservatively leveraged to increase credit in our struggling economy by hundreds of billions of dollars?

And what do you think will be required to get a satisfactory resumption of credit growth in the country? Treasury is required to review the executive compensation at hundreds of banks. How is that process going, and do you see any significant change in that compensation?

Mr. ALLISON. Well, first of all, I think many Americans have been outraged by the level of bonuses in the financial industry, especially among the largest financial institutions that received the largest amount of TARP funds. These institutions have repaid TARP. I think what is important, our administration believes what is important is to enact financial reform legislation that would, for example, provide for shareholders to have a say in pay for the top executives of these financial companies. I think we are going to see over time, if this is enacted, much more discussion and much more information about how pay is determined in these companies, and that in, in turn, should help to lead to better control over that type of activity.

We are, like you, we have been troubled by the shrinkage in lending. We do see signs, as I mentioned before, that lending is increasing. A number of the largest banks have pledged that they will increase lending here in 2010. We hope that happens as soon as possible.

Mr. SERRANO. You know, as you speak, I think of something, and my last statement here, for anyone who will care to listen, if they could help us with this, but the statement I just made, the question I just asked you raises some eyebrows at City Hall back in my hometown in New York, because, as you know, Mayor Bloomberg and others have said, sure, go after Wall Street, and in the process, you will destroy New York's economy.

You know, New York gets caught up in a little situation there where we know that these bonuses are totally improper and outrageous, but then taxes are collected on people who work in New York and collect those bonuses. I wish there was a way that we could come up with some sort of a presentation that would say these restrictions do put this kind of slight pain on New York, but look at what the rest, in dealing with this issue in general, will do for the State and for the city, and no one has been able to do that.

And I wish someone could direct me in the direction as to where we could get those numbers to indicate that, while we may put restrictions on folks who work on Wall Street in New York, in the long run, it is better for New York City and New York State to have this in place rather than what we had before, because it is not enough to say we are trying to put restrictions on the folks who caused the problem to begin with.

People tend to forget, you know, they tend to forget that we shouldn't have invaded Iraq or we should have been out of Afghanistan. They forget, so they somehow forget who caused the problem. Now it is, who is going to cause the current problem or the next problem, or why hasn't this been taken care of?

So if you know anyone that you could direct us to, to begin to put together a presentation that would say, yes, we will restrict, but here is the final outcome for places like New York or Chicago or financial centers throughout the Nation.

Mr. ALLISON. I think you ask a very interesting question and make a terrific observation. Let me also mention that for the seven companies that receive special assistance, what we call exceptional assistance, from TARP, the special master that was appointed by the Secretary of the Treasury directly oversaw the compensation of the top 25 executives in each of these companies. We saw that their compensation declined dramatically under the special master's oversight. Those companies are all doing better than they were before, and they are still very competitive.

And so certainly the administration is well aware of the need for responsibility and farsightedness in compensation awards by these companies. And the President, of course, is speaking today up in New York about the financial industry and the need for financial reform, which includes greater disclosure and a say on pay.

And it is vital that shareholders have the ability to voice their views about the compensation in financial companies.

Mr. SERRANO. Because, as you know, the argument we get, if you keep doing this, they will leave. Where are they going to go? I mean, are they going to quit their job on Wall Street and go elsewhere? When you have people in my congressional district in the South Bronx who might have gotten, and I am not being funny here, might have gotten a $100 Christmas bonus at their job and somebody is fighting over whether they are getting $5 million or $10 million in a bonus, I don't think it is much of an argument.

Thank you.

Mrs. Emerson.

Mrs. EMERSON. Thank you, Mr. Chairman.

All right. Let's go back to small business lending, if we could. You know, I am a little bit confused here. I have got a letter from the Special Inspector General, dated February 19th, that says, in essence, that Treasury perhaps was going to include the SIGTARP in overseeing the new Small Business Lending Program and then—or at least that is what your legislation would reflect—and then you all decided not to.

But yet the way that I understand that the program has actually been designed really sounds pretty much like an extension of the Capital Purchase Program, so I am just a little bit confused. And perhaps you can explain to me or perhaps assure me that there is no reason at all why you all would want to involve SIGTARP's oversight in this newly proposed program. And just because it was kind of back and forth, back and forth, so I am not quite sure where we are in the process right now.

So please explain.

Mr. ALLISON. Yes. Well, first of all, it is important to point out that the new program would be subject to special legislation. The program would be outside of the TARP Program. It is not identical to the Capital Purchase Program. It is qualitatively different because it will be providing direct incentives for lending. It will be geared to stimulating lending. It is not primarily, as the Capital Purchase Program was, to bolster the capital of banks. This was to give them capital that they may need in order to expand lending, and they will only get a reduced dividend if their lending grows.

We didn't think it was appropriate in legislation for us to tell Congress how we ought to be overseen.

Mrs. EMERSON. But you are using TARP money to do it, right?

Mr. ALLISON. No, we would not be using TARP money. This would be done entirely outside of TARP, under separate legislation, without using TARP funds.

Mrs. EMERSON. Okay, but, if, in fact, Congress determined that it was, you know, because of the whole SIGTARP office has really ramped up and actually has the ability to oversee this, it would not be something that you all would push back on, would it? In other words, if, in fact, we decided in our legislation to have SIGTARP oversee, that is not a problem, is it?

Mr. ALLISON. We welcome strong oversight over all of our programs. We have oversight not only by the Special Inspector General but by the Congressional Oversight Panel, the Financial Stability Oversight Board and the GAO.

We think that they all add value to what we do. And the only advice we would give is that there should be continued strong oversight of all of these programs.

Mrs. EMERSON. Well, certainly we need to protect the taxpayer, but it seems to me if we have got an entity that is really doing its job well, we might as well just keep using them.

The small, as I said earlier, my small businesses are just troubled by the lack of their ability to access credit. And so I am hopeful that whatever program comes about actually is going to work.

Can you tell me what specific actions your office took to encourage lending, particularly from the banks receiving TARP funds, and then anything in excess of that?

Mr. ALLISON. We think one of the best ways, Congresswoman Emerson, to encourage lending by the banks is to shine a light on their lending practices, and so we disclose their lending and have since the beginning on our Web site.

We have also asked them to report to us periodically on how they are using TARP capital. And, by the way, some of those are recommendations of SIGTARP, which we thought were very constructive.

We are working with banks. We have been talking to many banks about their lending practices to encourage them to try to lend responsibly. In fairness, we have seen collateral values, especially this affects small business, the value of their collateral, such as their commercial real estate that they may pledge or their personal real estate that they may pledge in order to get a loan, has dropped substantially. And that is one reason why some banks have cut back on their credit.

Nonetheless, with the stimulus activities by the government, by the funding of many programs, by the improvement in the economy, we think and we are hearing from banks that they are reaching an inflection point where you are likely to see a pick up in lending in 2010, and that is very encouraging for small business and for the economy.

Mrs. EMERSON. Well, it certainly, in almost every single newspaper article that I can read, including another article in USA Today, "Banks Who Took Aid Decreased Lending," every single headline. And that is very troubling, given the fact that part of the whole reason that we—those of us who supported TARP—it was to get Main Street back in business.

Mr. ALLISON. Let me just also mention on that point, one can't just look at the loan balances on the bank's books to see what their current activity is, because banks have had to write down a lot of bad loans. And so even their lending activity may be stronger today, but the overall balance comes down because other loans have either matured or been written down.

So one has to look at the actual lending activity of the bank, not at the balances on the bank's balance sheet, to get the real picture as to what is going on.

Mrs. EMERSON. All I have to do is talk to small businesses in my district, and I can get the real answer to this question. And we are not talking about Bank of America banks; we are talking Missouri, big Missouri banks, just for example.

But, I know that for much of the last year, the secondary market for many types of loans was frozen, and so whether it is mortgages, SBA loans, other asset-backed securities currently functioning, I mean, tell me what steps you all are taking to ensure those markets do continue to function effectively so we can move this along faster.

Mr. ALLISON. You have just given the rationale, Congresswoman Emerson, for this Small Business Lending Fund that we would like Congress to enact. This program is designed specifically to encourage lending. We totally agree with your points. We hear the same anecdotes from many businesses across the country. I get letters from many of these businesses.

You are pointing to a real problem, and we understand that. That is why we have designed this program. That is why we are hopeful that the Congress will enact it as soon as possible so we could be providing capital to these banks and enabling, giving them the confidence and the capital so they can increase their lending.

Mrs. EMERSON. So what is going to happen if we don't pass legislation?

Mr. ALLISON. I think it will simply take longer for the lending to recover. Eventually it will increase again, but we would like to see it happening sooner rather than later. We want to help create jobs, and jobs depend upon small business being able to get funding to purchase inventories, to make new investments in plant and equipment to hire more people. And so to get the economy moving more rapidly, we think providing capital to the smaller banks who do an outsized portion of small business lending across the country is extremely important.

I and my colleagues have been talking with many of these banks across the country in all districts. And what they tell us is that they see good quality companies that they want to be lending to. I think that we are seeing some parts of the country where lending is going to pick up a little more rapidly than other parts. But by providing the capital, we enable banks to take another look at their lending practices to review loans that they may have turned down but they might want to review again with the prospect of perhaps increasing lending to those companies.

Mrs. EMERSON. Well, it is a problem, and hopefully we will get to this issue. I would certainly encourage you all just to make it a lot easier on yourselves by saying SIGTARP can handle the oversight here.

But I also want to just, before I close, I also want to mention, there is another issue—and this isn't specific to our subcommittee at all—but the fact is that the credit unions are actually trying to increase the cap on their member business lending so they, in fact, could make some of these small business loans the banks are so reluctant to do because they have the capital to do it.

And it seems to me ridiculous that the Treasury Department would be pushing back on this and saying—and this isn't in your field—but it is just a frustrating thing. You have got these very stable financial institutions wanting to do something to help keep the economy going, and, you know, Treasury is pushing back on them. And it seems to me that it would be a win/win if we were able to do something in that regard simply to increase the inventory of financial institutions that have money to offer. Thanks.

Mr. ALLISON. Thank you.

Mr. SERRANO. Thank you. Thank you, Mrs. Emerson.

We are going to recognize remaining members, and then we are going to try to wind down this first panel so that we can get going with the second panel. We hope to unwind this before we face the impending votes on the House floor.

Mr. Edwards.

Mr. EDWARDS. Mr. Chairman, in the remaining time, I have no additional questions other than I did want to ditto the line of questioning of Mrs. Emerson; while I believe we needed financial stabilization measures in 2008 and 2009 to keep us from going into the second Great Depression, clearly small businesses all across the country, and it certainly reflects that and I see that in Texas, they are having challenges. Anything we can do together to free up that liquidity in a responsible way would be very, very important.

Mr. SERRANO. Thank you.

Mr. Culberson.

Mr. CULBERSON. Thank you. A follow-up on that same line of questioning, I can back up what Mr. Edwards and Mrs. Emerson are saying, but pointing directly to information that I have gotten and I know they probably have heard, too, from the Associated General Contractors in Texas, the Greater Houston Builders Association, the Associated Builders and Contractors in Houston, the Houston Association of Realtors, the Texas Association of Realtors, I am sure this is true across the country, that the banks are flush with money. And the regulators have instructed the banks to unload real estate loans, stop loaning money for real estate loans or commercial real estate, even if it is a blue chip borrower who has always paid back their loans. So it is a regulatory problem as well, but these banks who have received this money are absolutely flush with money.

This is within Treasury's jurisdiction. I know FDIC is a key part of this, but I know all of us, and I suspect Mr. Edwards would join me in this, he is nodding back there, we would all encourage it. We want the banks to loan money to people who can pay it back, but they are not loaning money to people who can pay it back.

To what extent can you help, can Treasury help put pressure on regulators to quit forcing banks to unload or stop making real estate loans to good borrowers? I mean, these are good credit risks. In fact, most of the home building, Chet, in Houston, I just had home builders come see me yesterday, and several of them have gone out of business because the banks will not lend them money. And these are solid credit risks. They have always—you could have a nuclear attack from the Russians, and these guys would pay their loan back.

What can you do to help get the regulators to quit pressuring the banks to stop making these loans to good credit risks?

Mr. ALLISON. Well, first of all, we fully understand the importance of increasing lending to small business.

Mr. CULBERSON. But good credit risk.

Mr. ALLISON. Yes, sir, I understand. We do not control the regulators. The regulators are totally independent from the Treasury Department. We know that they have provided additional guidance to their examiners throughout the country about lending to small business.

Mr. CULBERSON. They have, indeed. They are putting this——

Mr. ALLISON. Well, I would think that perhaps the regulators should speak for themselves on that issue.

Mr. CULBERSON. You have got a role in that, though; it is atmospherics. And to the extent you can, I hope you will, as the Department of Treasury, do whatever you can. What can you do? They are not complete. I mean, obviously, they are independent. You want them to be.

Mr. ALLISON. Well, the regulators are well aware of that issue, and that is one reason why they have communicated additional guidance to their supervisors and their examiners. But I would invite you to speak with the regulators directly because they are independent of the U.S. Treasury Department. We obviously have dialogue with them, but they make their own decisions.

Mr. CULBERSON. Mr. Chairman, I know it would be very helpful for this committee to do whatever we can, obviously, making sure that we want loans to be made to people who can pay them back. I am sure it has happened in New York, too, and in Pennsylvania. They are absolutely not making loans to creditworthy borrowers who will pay them back. And we need to do whatever we can, Mr. Chairman, to help get the regulators to quit putting the screws to the banks.

Mr. SERRANO. The point is well taken. It is a problem in every community in this country.

Mr. Fattah.

Mr. FATTAH. Thank you, Mr. Chairman.

Well, we don't live in a socialist country. We can't dictate to the banks what they do in a free market economy, but I do empathize with much of what has been said that there is a concern about getting credit flowing.

Let me start here, first, to really congratulate the Department in its work on the TARP Program. I mean, it is an amazing feat, an extraordinary one, and unexpected by many of the critics of the TARP Program that the Department would have made money and expect to make money in totality when the funds were made available to banks to stem the financial crisis. The economy has bounced back significantly, and the stability in the financial markets, I think, is obvious to everyone.

So you have done a very good job, and you have maintained stewardship over the taxpayers' money in a way that I think deserves to be noted for you and the work of Secretary Geithner.

I do think that where we see a need that is not being filled in the market, it isn't inappropriate at all for the government to step in. That is what SBA exists for, and I think the administration's program of moving some $30 billion through CDFIs, through community banks, so that it can be available to small businesses who are good credit risks, I think, is an appropriate role.

And this is what we have done where the market has not worked in the past, and the government has stepped in. And I think that that is something we should move expeditiously on. I know that the Department is working on it. The administration is working on it. And I just want to voice my support for it, because I know many small businesses in the Philadelphia community who have still had some challenges, notwithstanding being very good credit risks and having, you know, in essence, the narrow deals have had difficulty getting loans.

But I think that we don't on the one hand want to criticize banks for the risks that they took that took the country to the edge of a financial disaster, as regulators are saying that they need to be more conscious of the risk they are assuming, and at the same time say, well, we want Treasury to put pressure on regulators to back off. I mean, you know, we can't have our cake and eat it, too, in that sense. But I do think that we can step in through the Treasury, through SBA, and provide assistance.

I am more interested in what we are doing about mortgage foreclosures, and I know a billion and a half was made available to the housing and finance agencies to develop programs related to the unemployed, in terms of foreclosure prevention, different from the foreclosures we saw in the front end of this problem, which were largely driven by the subprime and other issues.

The foreclosures that are moving through the market now are driven in large part because people have lost their job and then followed their home. And it makes no sense for us to create deadbeats out of persons who are taxpaying, law-abiding citizens, paying their bills. It created a situation where we now have a vacant home in the neighborhood and driving prices down, but also have them out on the street and their credit rating ruined for a decade or so.

And the cost for the taxpayer for a foreclosure, which doesn't get discussed a lot, is, you know, quite substantial, somewhere above $80,000 per foreclosure.

We have a program in Pennsylvania through our housing and finance agency that I helped create a few decades ago that has worked very well to step in and help unemployed homeowners who have lost their job through no fault of their own and through no risk to the taxpayers. We have gotten every dollar paid back, and the average amount of help was 4 or 5 months of assistance to that homeowner with those dollars being paid to the long-term payment of the mortgage.

So I was very happy to see the Treasury's initiative focused on the hardest-hit States. We have, in the Wall Street reform bill, the House version, a $3 billion allotment to mirror those efforts throughout the country to step in to help homeowners.

So I would just like to get from you what has happened with the initial $1.5 billion and what these hardest-hit States are doing, if you can comment.

Mr. ALLISON. Congressman Fattah, thank you very much for your comments and your question for help for the hardest-hit States. As you know, the first billion and a half, as you said, was devoted to five States. We then allocated another $600 million to five other States. And we have received the proposals from the first five States as of last Friday. We are looking at those right now.

I think you would be pleased that the HEMAP Program in Pennsylvania has been looked at very closely by a number of those States as maybe they could model something after HEMAP to tide people over, as you said, who are unemployed. This programs is aimed at areas most affected by high unemployment and by falling housing prices. And this is a localized problem in that it is acute in some particular parts of the country, and that is why we allocated the money to those particular 10 States.

So we are looking forward to seeing what their proposals are, to working with them on implementing those proposals.

We will have final decisions next month on those proposals, and then they can get moving.

But we totally agree with your analysis of this problem. That is why we innovated this program. And we have high hopes that it will be truly creative and develop solutions that best suit these particular areas of the country, because they are developed by people who know those communities.

And we found that, because this is a highly concentrated problem, we need local expertise to work alongside the Treasury Department and the Department of Housing and Urban Development to provide and develop the most effective solutions possible.

Mr. FATTAH. Let me thank you for your testimony. Thank you for your testimony.

I am going to thank the chairman.

Mr. SERRANO. Thank you.

Mr. Allison, we thank you. I have one more question to submit to the record.

Mrs. EMERSON. Mr. Chairman, I have several to submit to the record. If you would like to wind this down, I can wait.

Mr. SERRANO. We will wind it down. The one I do have for the record is one that probably should have been the first one, and that is, tell us how you are going to wind down TARP and, as that winds down, all of the information.

So we thank you for your testimony. We thank you for your service, and we thank you for what I know is your desire to keep us informed on all the different issues that we presented.

As you well understand, both programs that were put forth, in our opinion, were very necessary, but they have created a lot of controversy and created a lot of questions, and that is why we ask so many questions and ask you to keep us informed.

Mr. CULBERSON. Mr. Chairman, could I ask, if I could, for the witness to provide the chairman as well the information about how much money the Federal Reserve has loaned out and to whom and under what conditions? I know the chairman would be very interested in that as well.

Mr. SERRANO. The chairman would be very interested in that.

Mr. CULBERSON. Thank you.

Mr. SERRANO. Thank you.

Thank you, Mr. Allison.

Mr. ALLISON. Thank you, sir.

Mr. SERRANO. In my opening statement an hour and a half ago, I told you that our next witness would be Mr. Barofsky, and we ask you now to come forward and give us your testimony. We will try to do this as painless as possible because we are running against a time constraint.

I am always amazed at how Members of Congress get in so many hearings, considering what we are always up against. And you know the drill; 5-minute presentation, and we will put anything else in the record.

Mr. BAROFSKY. Thank you, Mr. Chairman.

Thank you, Mr. Chairman, Ranking Member Emerson, members of the committee.

It is a privilege to appear before you today to testify about SIGTARP's proposed budget for 2011. As you know, in the President's budget request for 2011, he includes a request for approximately $49.6 million for the operations of SIGTARP. That proposed budget will allow us to continue to operate as the agency that stands between hundreds of billions of taxpayer dollars and those who would seek to steal, waste or abuse them. We carry out this role in three different areas: Transparency, oversight and enforcement.

Let me start with enforcement. As the only oversight body in the TARP legislation with law enforcement authority, we literally have the role as the TARP cop on the beat. And to meet those challenges, we built a sophisticated law enforcement agency. We have 84 ongoing investigations. We have recently opened up offices in New York and are about to do the same in L.A. and San Francisco, and we are trying to establish a nationwide presence to deter and detect TARP fraud.

Our cases are as diverse as the 13 sub-TARP programs that have developed. For example, we recently arrested and got criminal charges against the president and CEO of Park Avenue Bank for his attempt to try to steal $11 million from the TARP Program. We have brought criminal charges against two individuals out in California who are running a mortgage modification fraud scheme that brought in a million dollars from struggling homeowners.

In Tennessee, Gordon Grigg, a hedge fund executive, is serving 10 years in prison for a fraud that he was doing by trying to sell fictional investments that he called TARP-backed securities. In Atlanta, we have a number of convictions and charges related to our investigation of Omni Bank, another TARP applicant. We have executed search warrants in California against a law group that is alleged to have participated in other mortgage modification scams. And in Florida, two banks, one of which had received conditional approval, was about to receive $553 million in TARP funds that never went out the door.

On the civil side, we work with the SEC and the New York State Attorney General in their investigations into Bank of America. And all told, our investigations division has helped in the recoupment or the prevention of loss through fraud of more than $700 million.

We also leverage our resources with other law enforcement agencies. We formed the TALF PPIP Task Force in New York consisting of eight different law enforcement agencies. We have the TARP Inspector General counsel that we founded here in Washington, and we have a leading role in the President's Fraud Enforcement Task Force.

With respect to transparency and oversight, we do that through our auditing and reporting function. This week we issued our sixth comprehensive quarterly report reviewing operations of TARP and of SIGTARP for the preceding quarter, and these reports are intended to be desk books, reference guides that try to translate all the Wall Street terminology into Main Street language.

The American people have a thirst for information about this program in which they are investors. In SIGTARP, we have tried to meet that thirst with more than 42 million hits to our Web site since our inception.

As far as audits, we have issued eight audits to date. Just as a way of example, they have covered issues such as TARP recipient use of funds, the impact of outside influences on the TARP application process, the decision by government officials to pay the equivalent of 100 cents on the dollar to AIG's counterparties for securities that were worth less than half of that amount, and most recently, on the HAMP, the mortgage modification program, the administration's response to the foreclosure crisis.

We have made about 50 recommendations to date. And while many have been adopted, some have not. But those that have, I believe, have significantly contributed to the TARP being better run, better executed and, most importantly, better protected against the risk of loss through fraud as a result.

Finally, one of our roles is, of course, to keep the Congress informed of what is going on in TARP and what is going on at SIGTARP. And we have conducted dozens and dozens of individual Member briefings, staff briefings. And today marks my 14th time testifying before Congress as the Special Inspector General to discuss what is going on in the TARP and the TARP programs.

Mr. Chairman, Ranking Member Emerson, again, thank you for this opportunity today. I look forward to answering any questions you may have.

[The prepared statement of Mr. Barofsky follows:]

OFFICE OF THE SPECIAL INSPECTOR GENERAL FOR THE TROUBLED ASSET RELIEF PROGRAM

ADVANCING ECONOMIC STABILITY THROUGH TRANSPARENCY, COORDINATED OVERSIGHT AND ROBUST ENFORCEMENT

FOR OFFICIAL USE ONLY UNTIL RELEASED BY THE
HOUSE COMMITTEE ON APPROPRIATIONS
SUBCOMMITTEE ON FINANCIAL SERVICES AND GENERAL GOVERNMENT

STATEMENT OF NEIL BAROFSKY

SPECIAL INSPECTOR GENERAL
FOR THE TROUBLED ASSET RELIEF PROGRAM

BEFORE THE
HOUSE COMMITTEE ON APPROPRIATIONS
SUBCOMMITTEE ON FINANCIAL SERVICES AND GENERAL GOVERNMENT

April 22, 2010

Chairman Serrano, Ranking Member Emerson, and Members of the Committee:

Overview
Thank you for the opportunity to testify today about the critically important oversight mission of the Office of the Special Inspector General for the Troubled Asset Relief Program ("SIGTARP").

As you know, SIGTARP was created by the Emergency Economic Stabilization Act of 2008 ("EESA") to conduct and coordinate audits and investigations concerning the Troubled Asset Relief Program ("TARP"). As such, SIGTARP is primarily responsible for reporting upon, auditing and conducting criminal and civil investigations concerning TARP. Initially envisioned as a large but relatively straightforward toxic asset purchase program, TARP has morphed into multiple complex programs — the current count is 13 — that touch on nearly every major aspect of our economy, from too-big-to-fail Wall Street giants, to regional and community banks, to the asset-backed securities markets, to small-business lending initiatives, to the automobile industry, and, perhaps most broadly to the mortgages of millions of struggling homeowners around the country. I would like to take this opportunity to explain how SIGTARP has used the funding it has already received to meet this extraordinary oversight task thus far and how we anticipate using the $49.6 million requested for SIGTARP in the President's fiscal year 2011 budget.

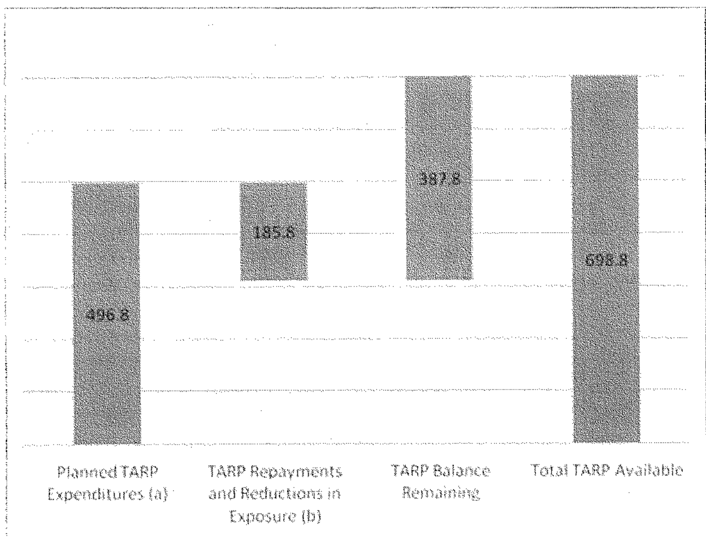
In just 16 months of existence, SIGTARP has had a tremendous impact on the TARP program. As discussed in more detail below, it has made significant and demonstrable contributions to the transparency of the program; it has worked closely with the Department of the Treasury ("Treasury") and the other agencies administering TARP-related programs to make those programs more effective and less susceptible to waste, fraud and abuse; and it has successfully brought to justice those who have sought to benefit criminally from this national crisis.

- SIGTARP Quarterly Reports: SIGTARP has fulfilled its EESA-mandated reporting function by producing comprehensive quarterly reports explaining the TARP programs in a detailed but comprehensible manner. SIGTARP's reports are designed to be the desk reference for what is happening in TARP for policy makers in Congress and the Administration and for the general public. Each quarter, SIGTARP describes what is happening in the various TARP programs, what SIGTARP has done over that past quarter, and its recommendations for TARP program implementation.

- SIGTARP's audits: since its inception, SIGTARP has initiated eight audit projects and has issued 20 audit reports. SIGTARP's audits are designed to address the most important issues facing TARP implementation, and its audit reports have had a substantial impact on the debate about these issues, including TARP recipients' use of funds, the circumstances around the first TARP investments, including the extraordinary support received by Bank of America, the American International Group, Inc. ("AIG") bonuses, the AIG counterparty payments, and the early disappointing results in the mortgage modification program.

- SIGTARP's investigations: SIGTARP has rapidly developed into a sophisticated white-collar law enforcement agency. SIGTARP has over 84 ongoing investigations, and important criminal and civil cases have resulted from SIGTARP's investigations involving banks that have attempted to steal TARP funds and fraudsters who have victimized dozens of individuals making false promises about TARP assistance.

Background: TARP, the Creation of SIGTARP, and SIGTARP's Budget Authority
TARP consists of 13 announced programs, six of which are closing or are closed to further purchases. As of March 31, 2010, Treasury had announced programs involving potential spending of $537.1 billion of the $698.8 billion maximum available for the purchase of troubled assets under TARP as authorized by Congress. Of this amount, Treasury had expended or committed to expend approximately $496.8 billion through the 13 implemented programs to provide support for U.S. financial institutions, the automobile industry, the markets in certain types of asset-backed securities ("ABS"), and homeowners. As of March 31, 2010, 77 TARP recipients had paid back all or a portion of their principal or repurchased shares for an aggregate total of $180.8 billion of repayments and a $5 billion reduction in exposure to possible further liabilities, leaving $387.8 billion, or 55.5%, of TARP's allocated $698.8 billion available.



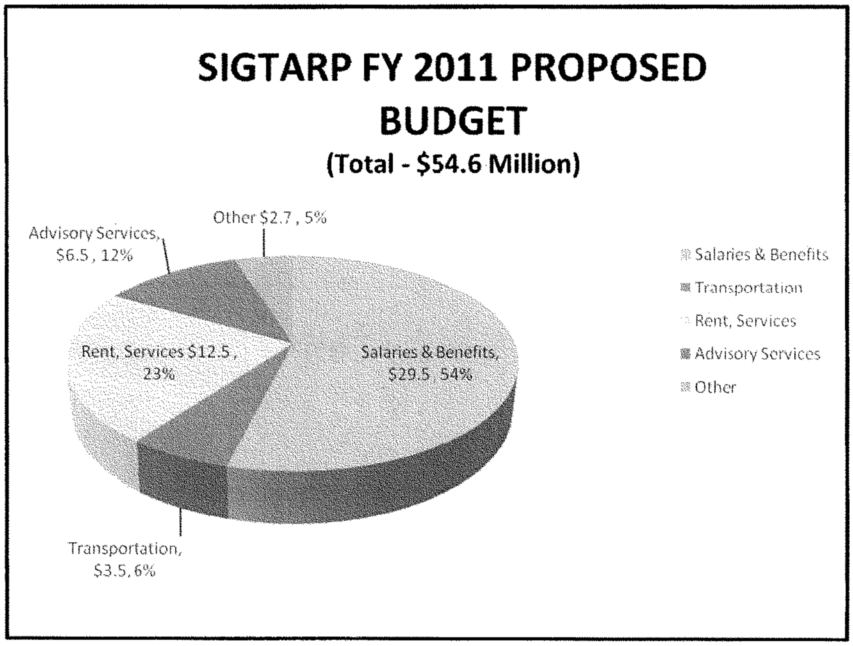
Notes: Numbers affected by rounding. The "planned expenditures" referenced throughout this report represent the funds Treasury currently plans to expend for each program, and a majority of those are committed funds (e.g., signed agreements with TARP fund recipients).
a Repayments include $135.8 billion for CPP, $40 billion for TIP, $4.6 billion for Auto Programs, and a $5 billion reduction in exposure under AGP.
b Treasury experienced a $2.3 billion loss on some investments under the CPP program
Sources: Treasury, "Transactions Report," 4/2/2010; Treasury, response to SIGTARP data call, 4/12/2010.

In addition to the principal repayments, Treasury has received interest and dividend payments on its investments, as well as revenue from the sale of its warrants. As of March 31, 2010, $14.5

billion in interest, dividends, and other income had been received by the Government, and $5.6 billion in sales proceeds had been received from the sale of warrants and preferred stock received as a result of exercised warrants. At the same time, some TARP participants have missed dividend payments: among participants in the Capital Purchase Program ("CPP"), 104 have missed dividend payments to the Government, although some of them made the payments on a later date. As of March 31, 2010, there was $188.9 million in outstanding unpaid CPP dividends. In addition, three TARP recipients have failed and several others have restructured their agreements with Treasury, increasing the potential for further losses.

Section 121 of EESA created SIGTARP as an independent agency within Treasury responsible for conducting, supervising, and coordinating audits and investigations of any actions taken under EESA. SIGTARP commenced operations on December 15, 2008, with the swearing in of the Special Inspector General. It is important to note that although Secretary of Treasury has extended TARP until October of this year, SIGTARP's oversight and investigative responsibilities do not end at that time. SIGTARP exists as long as Treasury holds purchased assets or insures them. Under the TARP program known as the Public Private Investment Program ("PPIP"), Treasury will hold assets for an anticipated 8-10 years. In addition, although 6 of the 13 TARP programs have closed to new purchases, Treasury is continuing to roll out new programs and initiatives, including several over the past quarter.

Section 121(j) of EESA, as amended, provided SIGTARP with $50 million in no-year money to fund operations. Additionally, section 402(c)(1) of the Helping Families Save Their Homes Act of 2009, Pub. Law No. 111-22, provided SIGTARP with $15 million to "prioritize the performance of audits or investigations of recipients of non-recourse Federal loans made under any" EESA program. These supplemental no-year funds are thus not available for SIGTARP's general operational uses, and SIGTARP expects that it will take approximately three fiscal years, *i.e.,* $5 million per year for FY 2010, FY 2011, and FY 2012, to expend them as directed. In the late spring of 2009, SIGTARP determined that its initial operating funds would be expended during the second quarter of fiscal year 2010 and requested an additional $28.3 million that would be needed to fund operations throughout fiscal year 2010. In light of $15 million made available to SIGTARP by Pub. Law No. 111-22, SIGTARP requested additional fiscal year 2010 funding of $23.3 million. On December 16, 2009, the President signed Public Law No. 111-117, the Consolidated Appropriations Act of 2010. The Appropriations Act at Division C, Title 1, provided SIGTARP with the $23.3 million requested. SIGTARP's budget as submitted in the fiscal year 2011 President's budget request is $54.6 million, of which $5 million will be provided under Pub. Law No. 111-22.



Between its commencement in December of 2008 and March 31, 2010, SIGTARP has been extraordinarily productive: publishing six comprehensive quarterly reports to Congress concerning TARP, opening more than 84 investigations, initiating 20 audits, issuing eight audit reports, leveraging oversight resources, testifying at 14 Congressional hearings, building infrastructure, and hiring staff. SIGTARP has secured temporary office space and equipment for staff; has contracted for permanent space and the rehabilitation of the same; has contracted with public and private vendors for personnel services, procurement assistance, publication consulting, data processing and analysis, and office equipment and services. In March of 2010, SIGTARP moved into half of its permanent space at 1801 L. Street, NW, Washington, DC. Further, as of March 31st, SIGTARP has hired 116 managers, lawyers, auditors, investigators, and other professionals with a wealth of experience in program auditing, criminal law enforcement, securities enforcement, and other relevant curricula. To successfully accomplish this hiring challenge, SIGTARP relied on direct hire authority and dual compensation authority waiver delegated by the Office of Personnel Management, as well as authority provided by the Special Inspector General for the Troubled Asset Relief Program Reform Act of 2009, Public Law No. 111-15.

Quarterly Reports to Congress
SIGTARP has issued six wide-ranging quarterly reports to Congress, describing the activities and plans of SIGTARP; explaining and evaluating the various TARP programs (both implemented and announced); reviewing the operations of the Office of Financial Stability ("OFS"), the Treasury entity that administers TARP; and recommending changes to TARP programs and procedures to increase transparency and effective oversight and decrease the potential for fraud, waste and abuse. SIGTARP expends substantial time and resources on its reports to Congress, which are designed to be the comprehensive reference concerning TARP activities for policy makers, Congress and the American people. SIGTARP's reports also satisfied the requisite reporting requirements of SIGTARP's authorizing statute by detailing its operations; describing the categories of troubled assets purchased or otherwise procured by Treasury; explaining the reasons Treasury deemed it necessary to purchase each such troubled asset; listing each financial institution from which such troubled assets were purchased; listing and detailing biographical information on each person or entity hired to manage such troubled assets; estimating the total amount of troubled assets purchased, the amount of troubled assets held, the amount of troubled assets sold, and the profit or loss incurred on each sale or disposition of each such troubled asset; and listing the insurance contracts issued. To date, SIGTARP's quarterly reports include 58 detailed recommendations to improve TARP programs and procedures. Many of these recommendations have been adopted. These quarterly reports are publicly available at http://www.sigtarp.gov/reports.shtml.

Investigative Activities
SIGTARP's Investigations Division ("ID") has developed into a sophisticated white-collar law enforcement agency. Currently, ID has 84 open criminal and civil investigations that concern suspected TARP fraud, accounting fraud, securities fraud, insider trading, bank fraud, mortgage fraud, mortgage servicer misconduct, fraudulent advance-fee schemes, public corruption, false statements, obstruction of justice, theft of trade secrets, money laundering, and tax-related investigations. Although the majority of SIGTARP's investigative activities remain confidential, I would like to highlight several cases that have been brought as the result of SIGTARP's investigations.

- **The Park Avenue Bank**: On March 15, 2010, Charles Antonucci, the former President and Chief Executive Officer of The Park Avenue Bank, was charged by the United States Attorney's Office for the Southern District of New York with offenses including self-dealing, bank bribery, embezzlement of bank funds, and bank, mail and wire fraud, among others. In particular, Antonucci allegedly attempted to steal $11 million of TARP funds by, among other things, making fraudulent claims about the bank's capital position. These charges marked the first time an individual was criminally charged with attempting to steal TARP funds.

  According to the allegations, Antonucci falsely represented that he had personally invested $6.5 million in The Park Avenue Bank to improve its capital position. As set forth in the charges, however, the funds were actually borrowed from The Park Avenue Bank itself and reinvested as part of an undisclosed "round-trip" transaction. The complaint further alleges that this fraudulent transaction was touted by The Park Avenue

Bank in support of its application for TARP funds as evidence of its supposedly improving capital position. The case and investigation are ongoing.

- **Bank of America**: On February 4, 2010, the New York Attorney General charged Bank of America, its former Chief Executive Officer Kenneth D. Lewis, and its former Chief Financial Officer Joseph L. Price with civil securities fraud. According to the allegations, in order to complete a merger between Bank of America and Merrill Lynch & Co., Inc. ("Merrill Lynch"), the defendants failed to disclose to shareholders spiraling losses at Merrill Lynch. Additionally, after the merger was approved, it is alleged that Bank of America made misrepresentations to the Federal Government in order to obtain tens of billions of dollars in TARP funds. The investigation was conducted jointly by the New York Attorney General's Office and SIGTARP, and the case remains pending in New York state court.

  SIGTARP also assisted the SEC with its Bank of America investigation. On February 22, 2010, the Honorable Jed S. Rakoff, United States District Judge for the Southern District of New York, approved a $150 million civil settlement between the Securities and Exchange Commission ("SEC") and Bank of America to settle all outstanding SEC actions against the firm, and ordered significant corporate governance changes at the bank.

- **Nations Housing Modification Center**: On March 19, 2010, Glenn Steven Rosofsky was arrested by agents from SIGTARP and the Internal Revenue Service, Criminal Investigation Division and charged by the U.S. Attorney's Office for the Southern District of California with one count of conspiracy to commit wire fraud and money laundering and one count of money laundering. A separate information the same day charged Michael Trap with conspiracy to commit fraud and money laundering. As set forth in the charges, Rosofsky, Trap, and others operated a telemarketing firm, ostensibly to assist delinquent homeowners with loan modification services. Operating under the names "Nations Housing Modification Center" and "Federal Housing Modification Department," Rosofsky and Trap took advantage of the publicity surrounding the Administration's mortgage modification efforts under the TARP-supported Making Home Affordable ("MHA") program and are alleged to have used fraudulent statements to induce customers to pay $2,500 – $3,000 each to purchase loan modification services that were not actually provided. It is alleged in court documents that the fraud grossed more than $1 million. Trap pled guilty to the charges listed in his March 19 information the following day. The case against Rosofsky remains pending.

- **Federal Felony Charges Against Gordon Grigg:** On April 23, 2009, Federal felony charges were filed against Gordon B. Grigg in the U.S. District Court for the Middle District of Tennessee, charging him with four counts of mail fraud and four counts of wire fraud. The charges are based on Grigg's role in embezzling approximately $11 million in client investment funds that he garnered through false claims, including that he had invested $5 million in pooled client funds toward the purchase of fictional investments he described as the TARP-guaranteed debt. Grigg pleaded guilty to all charges and was sentenced to 10 years imprisonment.

- **Omni National Bank Cases**: Omni National Bank ("Omni") was a national bank headquartered in Atlanta with branch offices in Birmingham, Tampa, Chicago, Fayetteville, N.C., Houston, Dallas, and Philadelphia. Omni failed and was taken over by the Federal Deposit Insurance Corporation ("FDIC") on March 27, 2009. Prior to its failure, Omni had applied for but had not been approved for TARP funds under CPP. SIGTARP has participated in several investigations concerning Omni that have led to criminal charges as part of a mortgage fraud task force that includes SIGTARP, the U.S. Attorney's Office for the Northern District of Georgia, the Federal Deposit Insurance Corporation Office of Inspector General ("FDIC OIG"), the Office of Housing and Urban Development Office of Inspector General ("HUD OIG"), the Federal Bureau of Investigation ("FBI"), and the United States Postal Inspection Service ("USPIS"). The criminal cases in which SIGTARP has participated include charges against Brent Merriell for lying to Omni's regulator and identity theft in connection with a scheme to prompt Omni to forgive $2.2 million in loans; against Dalroy Davy for bank fraud and conspiracy to commit bank fraud in connection with a fraudulent scheme to obtain millions in mortgage loans from Omni; and charges against Jeffrey Levine, Omni's former executive vice president, for making, and causing others to make, materially false entries that overvalued bank assets in the books, reports, and statements of Omni. SIGTARP's involvement in the investigations, including whether the various frauds had an impact on Omni's CPP application, is ongoing.

- **Mount Vernon Money Center**: On March 11, 2010, the U.S. Attorney's Office for the Southern District of New York indicted Robert Egan, president, and Bernard McGarry, chief operating officer, of the Mount Vernon Money Center ("MVMC") with bank fraud for allegedly stealing $50 million entrusted to their company. MVMC engaged in various cash management businesses, including replenishing cash in more than 5,300 automated teller machines owned by banks and other financial institutions. According to the charges, from 2005 through February 2010, Egan and McGarry solicited and collected hundreds of millions of dollars from MVMC's clients on the false representations that they would not commingle clients' funds or use the money for purposes other than those specified in the various contracts with their clients. Egan and McGarry misappropriated their clients' money — including the funds of several institutions in which the American taxpayer was an investor through TARP — to fund tens of millions of dollars in operating losses in MVMC's businesses, to repay outstanding client obligations, and to enrich themselves at their clients' expense. SIGTARP agents assisted with the investigation. A trial date remains to be set.

- **United Law Group**: On March 11, 2010, SIGTARP, along with the USPIS, FBI, U.S. Immigration and Customs Enforcement ("ICE"), and the Orange County District Attorney's Office, executed a publicly filed search warrant obtained by the U.S. Attorney for the Central District of California at the offices of United Law Group, LLC ("ULG") in Irvine, California. This investigation focuses on allegations that ULG engaged in a mortgage modification advance fee scheme. The company allegedly charged struggling homeowners fees ranging from $1,500 to $12,000 without performing services while advising victims to stop paying their mortgages and terminate contact with their lenders. Many ULG customers subsequently lost their homes to foreclosure.

- **Colonial Bank**: On August 3, 2009, SIGTARP, with the FBI, HUD OIG, and the FDIC OIG, executed search warrants at the offices of Taylor, Bean and Whitaker ("TBW"), formerly the nation's 12th-largest loan originator and servicer, and Colonial BancGroup ("Colonial"), which applied for assistance under the CPP. Prior to the execution of these warrants, SIGTARP had served subpoenas on Colonial after it had announced that it had met conditions imposed by Treasury to receive $553 million in TARP funding. Based upon, among other things, the actions of SIGTARP, the funding was never made. Both Colonial and TBW have been shut down, and this investigation, which is being conducted with the Department of Justice and the SEC as well as the FBI and HUD OIG, is ongoing.

- **FTC Action Against Misleading Use of "MakingHomeAffordable.gov"**: On May 15, 2009, based upon an action brought by the Federal Trade Commission ("FTC"), a Federal district court issued an order to stop an Internet-based operation that pretended to operate "MakingHomeAffordable.gov," the official website of the Federal Making Home Affordable program. The FTC's action, which was developed with the investigative assistance of SIGTARP, alleges that the defendants purchased sponsored links as advertising on the results pages of Internet search engines, and, when consumers searched for "making home affordable" or similar search terms, the defendants' ads prominently and conspicuously displayed "MakingHomeAffordable.gov." Consumers who clicked on this link were not directed to the official website, but were diverted to sites that solicit applicants for paid loan modification services. The operators of these websites either purport to offer loan modification services themselves or sold the victims' personally identifying information to others.

Audit Activities
SIGTARP's Audit Division ("AD") conducts, supervises, and coordinates programmatic audits with respect to OFS's operation of TARP and recipients' compliance with their obligations under relevant law and contracts; evaluates TARP policies and procedures; and provides technical assistance to Treasury. With respect to auditing, AD is designed to provide SIGTARP with maximum flexibility in the size, timing, and scope of audits so that, without sacrificing the rigor of the methodology, audit results, whenever possible, can be generated rapidly both for general transparency's sake and so that the resulting data can be used to improve the operations of the fast-evolving TARP. Our recommendations in our audits and quarterly reports have had an immeasurable impact by preventing and deterring fraud, waste and abuse of TARP funds. To date, AD has issued eight audit reports as follows.

- **Use of Funds**: In July 2009, SIGTARP issued its first formal audit report concerning how recipients of CPP funds reported their use of TARP funds based upon a February 2009 survey that SIGTARP sent to 364 financial and other institutions that had completed TARP funding agreements through January 2009. For some respondents, the infusion of TARP funds helped to increase lending; others were able to avoid a "managed" reduction of their activities; others reported that their lending activities would have come to a standstill without

TARP funds; and others explained that they used TARP funds to acquire other institutions, invest in securities, pay off debts, or that they retained the funds to serve as a cushion against future losses.

- **External Influences**: In August 2009, SIGTARP issued an audit that examined whether undue external influences had an impact upon the CPP decision-making process. SIGTARP found no information indicating that external inquiries on CPP applications had affected the decision-making process, but gaps in the internal controls by the Government agencies conducting the CPP application process made it impossible to determine if all attempts to influence TARP decisions were captured by the audit. In connection with the audit, SIGTARP made recommendations regarding the improvement of internal controls and record keeping, which Treasury has adopted.

- **Executive Compensation**: SIGTARP also issued in August 2009 an audit examining executive compensation restriction compliance. This audit examined the efforts of TARP recipients to comply with executive compensation restrictions in place at the time of SIGTARP's survey of banks' use of funds.

- **Original CPP and Bank of America Investments**: In October 2009, SIGTARP released an audit examining the review and approval process associated with TARP assistance to the first nine CPP recipients, with emphasis on additional assistance to Bank of America. The audit concludes that Treasury, the Federal Reserve, and the FDIC implemented programs designed to help prevent a further deterioration of the economy and a significant risk of financial market collapse. The audit also finds that Treasury and other regulators' descriptions of the financial conditions of the first nine institutions as "healthy" were inconsistent with the private beliefs of decision makers at Treasury and the Federal Reserve, and later proved to be inaccurate. In addition to the basic transparency concern that this inconsistency raises, by stating expressly that the "healthy" institutions would be able to increase overall lending, Treasury created unrealistic expectations about the institutions' conditions and their ability to increase lending. Treasury lost credibility when lending at those institutions did not in fact increase and when subsequent events — the further assistance needed by Citigroup and Bank of America being the most significant examples — demonstrated that at least some of those institutions were not in fact healthy.

- **Federal Agencies' Oversight of AIG Executive Compensation**: SIGTARP released in October 2009, an audit report that examined the extent of the knowledge of and oversight by officials from the Federal Reserve, the Federal Reserve Bank of New York ("FRBNY"), and Treasury over compensation programs at AIG, and, specifically, $168 million in retention award payments made to employees of AIG Financial Products Corp. ("AIGFP") in March 2009. The audit concluded, among other things, that Treasury officials effectively outsourced oversight of AIG's compensation systems to the Federal Reserve, failing to take any independent steps to assess broadly the amount or scope of AIG's compensation obligations despite the $40 billion TARP investment in November 2008. As a result, senior Treasury officials were apparently not aware of the details of the March 2009 AIGFP payments until February 28, 2009. This meant that Treasury invested tens of billions of taxpayer dollars in AIG, designed AIG's contractual executive compensation restrictions, and helped manage the Government's majority stake in AIG for several months, all without having any detailed information about the scope of AIG's very substantial, and very controversial, executive compensation obligations. Treasury's failure in oversight potentially resulted in a missed opportunity to avoid the explosively controversial events surrounding the AIGFP retention payments that followed and created such considerable public and Congressional concern.

- **AIG Counterparty Payments**: On November 10, 2008, the Federal Reserve and Treasury announced the restructuring of the Government's financial support to AIG. As part of this restructuring, a special purpose vehicle, Maiden Lane III, purchased certain assets underlying AIGFP's credit default swap ("CDS") contracts from AIG's counterparties using $24.3 billion of FRBNY financing in combination with a $5.0 billion equity investment from AIG. In exchange for this payment and being permitted to retain $35 billion in collateral payments already made (thus effectively being paid par or face value for the underlying assets), the counterparties agreed to terminate their CDS contracts with AIGFP. SIGTARP's audit, which was issued in November 2009, found, among other things, that the terms of the original FRBNY financing did not result from independent analysis, but were simply an adoption of the term sheet from an aborted private financing discussion, and those terms, which included an onerous effective interest rate of 11%, made modification of the terms and further Government action inevitable. The audit also found that, in structuring Maiden Lane III, FRBNY attempted to obtain concessions, or "haircuts" from the CDS counterparties — and one counterparty was prepared to take a modest haircut — but FRBNY's negotiating strategy was hampered by a series of policy decisions that severely limited its ability to obtain concessions, including its decision not to accept concessions unless concessions could be obtained from all of the counterparties, its refusal to use its leverage as regulator to some of the institutions involved, and its basic discomfort with interfering with the sanctity of the counterparties' contractual rights. These policy choices led directly to a negotiating strategy with the counterparties that even then-FRBNY President Timothy Geithner acknowledged had little likelihood of success. The audit further noted that, although Mr. Geithner has denied that his intent was to benefit the counterparties, the overall structure of the AIG bailout resulted in AIG's counterparties receiving tens of billions of dollars they likely would not have otherwise received had AIG gone into bankruptcy.

- **Additional Insights on Use of TARP Funds**: In December 2009, SIGTARP issued an audit conducted as a follow-up to SIGTARP's earlier audit on TARP recipients' use of TARP funds. The follow-up audit examined the use of TARP funds by six institutions — two automobile manufacturers (General Motors Company ("GM") and Chrysler Holding LLC ("Chrysler")), two automobile financing firms (GMAC Inc. and Chrysler Financial Services Americas LLC), and two life insurance companies (The Hartford Financial Services Group, Inc. and Lincoln National Corporation). The six companies were able to provide useful insight on their actual or planned use of TARP funds.

- **HAMP**: A SIGTARP audit report published in March of 2010, examined the design and operation of the Housing Affordable Modification Program ("HAMP") in detail. The audit first found that Treasury's publicly touted measure of success, the number of short-term trial modification *offers* that have been made to struggling homeowners, was largely meaningless, and that Treasury needs to clearly identify the total number of homeowners it actually intends to help stay in their homes through sustainable permanent mortgage modifications. The audit also found that the limited results to date stemmed from, among other things, flaws in HAMP's design, rollout, and marketing that diminished the program's effectiveness in providing sustainable relief to at-risk homeowners. In its original version, HAMP involved frequent and time-consuming revisions of guidelines that created confusion and delay; permitted reliance on unverified verbal borrower data that slowed down conversions to permanent modifications; suffered from insufficient outreach to the American public about eligibility and benefits; and did not fully address risk factors for re-defaults among participating borrowers, including negative equity and high total debt levels even after modification.

These audits may be reviewed in their entirety at http://www.sigtarp.gov/audits.shtml. Additionally, AD is working on the following audits.

- **CPP Warrant Valuation and Disposition Process**: This audit, which is being conducted in response to requests by Senator Jack Reed and Representative Maurice Hinchey, seeks to determine what processes and procedures Treasury has established to ensure that the Federal Government receives fair market value for the warrants it received in connection with TARP investments and the extent to which Treasury has controls in place to facilitate a transparent and well-documented decision-making process.

- **Automobile Dealership Closures**: This audit, undertaken at the requests of Senator Jay Rockefeller and Representative David Obey, examines the process used by GM and Chrysler to identify the more than 2,000 automobile dealerships that were slated for closure in connection with the recent GM and Chrysler bankruptcies. Its objectives are to determine whether GM and Chrysler developed and followed a fair, consistent, reasonable, and documented approach; to understand the role of the Federal Government in these decisions; and to review the cost savings or other benefits to GM and Chrysler.

- **Governance Issues Where U.S. Holds Large Ownership Interests**: SIGTARP received a request from Senator Max Baucus to undertake a body of audit work examining Federal Government oversight of, and interaction with, the management of institutions such as AIG, GM, Chrysler, and Citigroup, in which the Government has or is approaching majority owner status. The audit, which is being conducted jointly with the Government Accountability Office ("GAO"), will also examine the Federal National Mortgage Association ("Fannie Mae") and the Federal Home Loan Mortgage Corporation ("Freddie Mac"), which are under Government conservatorship.

- **Status of the Federal Government's Asset Guarantee Program with Citigroup**: This review, requested by Representative Alan Grayson, addresses a series of questions about the Government's guarantee of certain Citigroup assets through the Asset Guarantee Program such as: the basis on which the decision was made to provide asset guarantees to Citigroup and the process for selecting the loans and securities to be guaranteed; the characteristics of the assets deemed acceptable for inclusion in the program and how those assets differed from other Citigroup assets; whether adequate risk-management controls were in place to mitigate the risks to the taxpayer; and what safeguards existed to protect taxpayer interests and what the losses were on the portfolio.

- **CPP Applications Receiving Conditional Approval**: This audit examines those CPP applications that received preliminary approval from the Treasury Investment Committee conditioned upon the institutions meeting certain requirements before funds were disbursed. The audit will assess the basis for the decision to grant such conditional approvals and the bank regulators' role in such decisions; whether and how timeframes are established for meeting such conditions; and whether internal controls are in place to ensure that the conditions are met before funds are disbursed.

- **Selection of Asset Managers for the Legacy Securities Program**: This audit will examine the process Treasury followed to select fund managers to raise private capital for joint investment programs with Treasury through the PPIP. It will examine the criteria used by Treasury to select Public-Private Investment Fund ("PPIF") managers and minority partners, and the extent to which Treasury consistently applied established criteria when selecting fund managers and small, veteran- , minority- , and women-owned businesses.

- **Internal Controls for the Legacy Securities Program**: This audit will examine the internal controls in place for both Treasury and each of the PPIF managers for the Legacy Securities Program under PPIP. It will also assess the extent to which Treasury's internal controls mitigate PPIF manager conflicts of interest and ensure overall program compliance.

- **Term Asset-Backed Securities Loan Facility ("TALF") Collateral Monitors' Valuation**: This audit will examine the Federal Reserve's valuation determinations used to issue loans under TALF. It will assess how the Federal Reserve made valuation determinations, including the role of the collateral monitors, when making decisions regarding the eligibility of the collateral and the appropriateness of the requested loan amounts.

- **Office of the Special Master Decisions on Executive Compensation**: This audit will examine the Special Master's decisions on executive compensation at firms receiving exceptional assistance from the Federal Government. This audit will assess the criteria used by the Special Master to evaluate executive compensation and whether the criteria were consistently applied.

- **CPP Exit Strategy**: This audit will examine the process that OFS and Federal banking regulators have established for banks to repay Treasury and exit CPP.

- **Application of the HAMP Net Present Value ("NPV") Test**: This audit, which will be conducted in response to a request from Senator Jeff Merkley and eight other Senators, will assess whether the participating loan servicers are correctly applying the NPV test under the program; the extent to which Treasury ensures that servicers are appropriately applying the NPV test per HAMP guidelines when assessing borrowers for program eligibility; and the procedures servicers follow to communicate to borrowers the reasons for NPV test failure, as well as to identify the full range of loss mitigation options available to such borrowers.

- **Material Loss Review of United Commercial Bank**: SIGTARP is participating in a Material Loss Review of United Commercial Bank, based in San Francisco, with FDIC OIG. In November 2008, United Commercial Bank received $298.7 million of TARP funds through CPP. On November 6, 2009, the California Department of Financial Institutions closed the bank and appointed FDIC as receiver. The objectives of the audit are: determining the causes of the financial institution's failure and resulting material loss to the Deposit Insurance Fund; evaluating FDIC's supervision of the institution; and determining whether the FDIC and Treasury followed applicable procedures in recommending the bank for CPP funding and in monitoring its compliance with the securities purchase agreement.

Leveraging Oversight Resources

SIGTARP actively coordinates its activities with other oversight and law enforcement bodies in an effort to share expertise and leverage the resources of other agencies. In addition to meeting extensively with Treasury and the Federal Reserve concerning program proposals, SIGTARP regularly and continually coordinates with the Financial Stability Oversight Board, the Congressional Oversight Panel ("COP"), and GAO concerning our overlapping oversight responsibilities under EESA. Additionally, SIGTARP has initiated several efforts designed to augment audit and investigative resources. For example, SIGTARP founded the TARP Inspector General Council ("TARP-IG Council"), which includes the Comptroller General and the Inspectors General for Treasury, the Federal Reserve Board, the FDIC, SEC, the Federal Housing Finance Agency, HUD, the Small Business Administration, and the Treasury Inspector General for Tax Administration. The TARP-IG Council meets regularly to discuss developments in TARP and coordinate interconnected audit and investigative issues. Similarly, SIGTARP organized and chairs the Term Asset-Based Securities Loan Facility/Public-Private Investment Program ("TALF/PPIP") Task Force, which includes the Inspector General for the Federal Reserve Board, the FBI, the Financial Crimes Enforcement Network ("FinCEN"), ICE, the Internal Revenue Service Criminal Investigation Division ("IRS-CID"), the SEC, and the USPIS. The task force members participate in regular briefings about the TALF/PPIP, collectively identify areas of fraud vulnerability, engage in training exercises, and coordinate audit and investigative efforts. SIGTARP has also forged partnerships and launched joint investigations with the FBI, the SEC, IRS-CID, and the FTC, among others.

Recently, on February 24, 2010, SIGTARP hosted the inaugural meeting of the Rescue Fraud Working Group. President Obama established the Financial Fraud Enforcement Task Force ("FFETF") "to investigate and prosecute significant financial crimes and other violations relating to the current financial crisis and economic recovery efforts, recover the proceeds of such crimes and violations, and ensure just and effective punishment of those who perpetrate financial crimes and violations." A component of FFETF is the Rescue Fraud Working Group, co-chaired by Special Inspector General Neil M. Barofsky, Assistant Attorney General Lanny A. Breuer of the Criminal Division of the DOJ, and Timothy G. Massad, chief counsel of OFS. Attendees at the inaugural meeting included officials from agencies across the Federal Government, including

OFS; DOJ (Civil, Criminal, and Tax Divisions); the U.S. Attorneys' Offices for the Northern and Central Districts of California, the Eastern District of Virginia, the Eastern and Southern Districts of New York, and the District of New Jersey; the Office of the Comptroller of the Currency; the Office of Thrift Supervision; FinCEN; USPIS; the Board of Governors of the Federal Reserve; the SEC; and the FBI.

Congressional Testimony

One of the primary functions of SIGTARP is to ensure that members of Congress are kept adequately and promptly informed of developments in TARP initiatives and of SIGTARP's oversight activities. To fulfill that role, the Special Inspector General and his staff meet regularly with and brief members and Congressional staff. Since the commencement of SIGTARP, the Special Inspector General has testified before Congress 14 times, as follows.

- On February 5, 2009, Special Inspector General Barofsky testified before the Senate Committee on Banking, Housing and Urban Affairs, during a hearing entitled, "Pulling Back the TARP: Oversight of the Financial Rescue Program." The purpose of this oversight hearing was to explore how TARP can be made more effective in the areas of: protecting home values, college funds, retirement accounts, and life savings; preserving homeownership and promoting jobs and economic growth; maximizing the returns to the taxpayers for their investment; and enhancing some measure of public accountability.

- On February 11, 2009, Special Inspector General Barofsky testified before the Senate Judiciary Committee, during a hearing entitled, "The Need for Increased Fraud Enforcement in the Wake of the Economic Downturn." The purpose of the hearing was, among other things, to examine the issue of fraud in TARP.

- On February 24, 2009, Special Inspector General Barofsky testified before the House Committee on Financial Services, Subcommittee on Oversight and Investigations, during a hearing entitled, "A Review of TARP Oversight, Accountability and Transparency for U.S. Taxpayers." The purpose of this hearing was to ensure that the TARP oversight organizations created/assigned by EESA (*i.e.*, GAO, SIGTARP, and COP) understand their respective roles, cooperate with each other, and avoid repetitive efforts and inefficiencies. The hearing also examined how S.383 (the SIGTARP Act of 2009), which primarily deals with SIGTARP and had already been approved by the Senate, will improve TARP oversight.

- On March 11, 2009, Special Inspector General Barofsky testified before the House Committee on Oversight and Government Reform, Subcommittee on Domestic Policy, during a hearing entitled, "TARP Oversight: Assessing Treasury's Efforts to Prevent Waste and Abuse of Taxpayer Funds." The purpose of this hearing was to assess Treasury's oversight of the use of funds by financial institutions that received funds under TARP. Specifically, the hearing evaluated Treasury's data collection procedures for monitoring the use of TARP funds and examined Treasury's ability to detect and prevent waste and misuse of TARP monies.

- On March 19, 2009, Special Inspector General Barofsky testified before the House Committee on Ways and Means, Subcommittee on Oversight, during a hearing entitled, "Hearing on the Troubled Asset Relief Program: Oversight of Federal Borrowing and the Use of Federal Monies." The purpose of the hearing was to review the role of Federal borrowing in TARP, its impact on the national debt, and Treasury's efforts to protect public funds. In the latter regard, the hearing explored Federal tax compliance issues.

- On March 31, 2009, Special Inspector General Barofsky testified before the Senate Committee on Finance during a hearing entitled, "TARP Oversight: A Six Month Update." The purpose of the hearing was to survey the various TARP and TARP-related programs, and to examine SIGTARP's oversight of these programs.

- On April 23, 2009, Special Inspector General Barofsky testified before the Joint Economic Committee ("JEC") at a hearing entitled "Following the Money: A Quarterly Report by the Special Inspector General for the TARP." The testimony focused on the findings and recommendations of SIGTARP's April Quarterly Report.

- On July 21, 2009, Special Inspector General Barofsky testified before the House Committee on Oversight and Government Reform, during a hearing entitled "Following the Money: Report of the Special Inspector General for the Troubled Asset Relief Program." The hearing focused on SIGTARP's July Quarterly Report, and Special Inspector General Barofsky discussed his recommendations to enhance the success of TARP and highlighted the major themes of his report.

- On July 22, 2009, Special Inspector General Barofsky testified before the Oversight Subcommittee of the House Committee on Financial Services, during a hearing entitled "TARP Oversight: Warrant Repurchases and Protecting Taxpayers." The hearing examined warrants issued in connection with TARP. These warrants give Treasury the right to buy shares of TARP recipient stock at a set price at some point in the future and thus provide an opportunity for taxpayers to share in the upside for their TARP investments.

- On September 24, 2009, Special Inspector General Barofsky testified before the Senate Committee on Banking, Housing and Urban Affairs, during a hearing entitled "Emergency Economic Stabilization Act: One Year Later." In light of the first anniversary of EESA, the hearing examined how TARP was working.

- On October 14, 2009, Special Inspector General Barofsky testified before the House Committee on Oversight and Government Reform, during a hearing entitled "AIG Bonuses: Report of the Special Inspector General." The hearing focused on SIGTARP's audit examining Federal agencies' oversight of AIG executive compensation.

- On January 22, 2010, Special Inspector General Barofsky testified before the House Committee on Oversight and Government Reform, during a hearing entitled, "The Federal Bailout of AIG." The hearing focused on the Federal Government's response to AIG's collapse and on SIGTARP's audit report on the decision to pay AIG's credit default swap counterparties effectively at face value following AIG's near-bankruptcy.

- On March 25, 2010, Special Inspector General Barofsky testified before the House Committee on Oversight and Government Reform, during a hearing entitled, "Foreclosure Prevention: Is the Home Affordable Modification Program Preserving Homeownership?" The hearing focused on the execution and impact of Treasury's foreclosure prevention efforts, with particular attention to HAMP, and featured the release of SIGTARP's HAMP audit.

- On April 20, 2010, Special Inspector General Barofsky testified before the Senate Committee on Finance, during a hearing entitled, "The President's Proposed Fee on Financial Institutions Regarding TARP: Part 1" The hearing focused on a proposed bank fee to recoup losses experienced under the TARP, and findings and recommendations of SIGTARP's April 2010 Quarterly Report.

Chairman Serrano, Ranking Member Emerson and Members of the Committee, I want to thank you for this opportunity to appear before you in support of the President's fiscal year 2011 budget request for SIGTARP, and I would be pleased to respond to any questions that you may have.

Mr. SERRANO. Did you say 14, 14 times?

Mr. BAROFSKY. This is number 14. We counted up for the testimony today. I was surprised at the number.

Mr. SERRANO. I think you were here for most of the prior, previous testimony, so I am going to give you an opportunity to comment on the answers Mr. Allison gave, particularly on mortgage relief and the general effects of TARP on credit conditions, if you have anything you would like to add to that.

Mr. BAROFSKY. I think that, with respect to the mortgage program, the TARP mortgage program, HAMP, as I said, we recently released an audit, and we had new recommendations in our most recent quarterly report. It is a program that has a lot of promise. But it has had a lot of problems in execution. With only 230,000 permanent modifications more than a year into the program, it is making a very small dent into a much larger problem.

We addressed that in our audit through our recommendations. There has been problems with execution; a lot of the decisions and the practices in some ways have been rushed, which has resulted in some inefficiencies; a lot of borrower confusion, which has led to avenues for fraud. And there has been problems in some of the program design, which leaves it vulnerable to redefault. That is when someone gets a mortgage modification but is still unable or unwilling to continue to make the payments, either because the payments are still too unaffordable or because they are too hopelessly underwater.

To Mr. Allison and to Treasury's credit, after receiving that audit report, they announced some significant revisions to the program that do address things like underwater mortgages, carving out $14 billion of the program just for one program alone with FHA.

Those announcements also raised some significant concerns, which are addressed in our quarterly report. But we are hopeful and confident, and we will continue to work with Treasury to assist them in making this a program that will have the impact that the dollar amount that is committed to it should deserve.

Mr. SERRANO. When you speak about you hope to continue to work, has the past or recent past been rocky in that relationship? Are things getting better if they have been rocky? How do you see it? Because we in this panel want you all to get along.

Mr. BAROFSKY. I think we do get along. I think the nature——

Mr. SERRANO. Just in case, just for the record.

Mr. BAROFSKY. I think we get along. I think the nature of our oversight, we are very vigorous in our oversight.

Mr. SERRANO. Well, that is the key. We want you to work together. We don't want you to get along too much.

Mr. BAROFSKY. No. I think that, while there have been areas where certainly we have had some disagreement, certainly sometimes very passionate disagreement, I credit Treasury; I credit Mr. Allison. We are all working towards the same goal, which is helping to make sure this program protects the American people, it maximizes its efficiency, and it best protects against risk of loss from fraud. I think we have a great working relationship.

Mr. Allison and I spend, at least once a week where we sit down and discuss the TARP issues. And as I said before, I think that sometimes we have to work a bit longer and a little bit harder to get them to see our way. But overall, this program is in much, much better shape because of the willingness of Treasury to work with us and to try to meet us at least halfway, sometimes all the way on our side, with some of our most important recommendations.

Mr. SERRANO. SIGTARP's budget request of $49.6 million is higher than the budget request in the Treasury's Office of Inspector General, which is $30.3 million. So why is your organization so much more costly to operate? How much do you pay for contracted services, and what types of the services do you contract out?

Mr. BAROFSKY. Sure. The scope of our operations has changed dramatically since EESA was first passed, and originally it was contemplated to be one program basically to buy $700 billion of assets, direct purchases, a relatively straightforward program. It has changed a lot since then. As I said before, 13 subprograms that put a lot of demands on our agency, which I think are a lot different not just from the Treasury Inspector General but for most non-Special Inspector Generals.

We don't just address what is going on in Treasury. In other words, our oversight just isn't over Mr. Allison's office, the Office of Financial Stability. Because of the way that these programs have evolved, for example, the Capital Purchase Program, we also are providing oversight to more of the Treasury entities but also the FDIC and also the Federal Reserve. We also take a very aggressive role because we really are the sole law enforcement authority over all TARP-related programs. That really makes an expansive jurisdiction.

The Treasury Inspector General doesn't necessarily get out to those who come into the government for a program, so let me just give you an example. AIG, Bank of America, and Citi have devoted a lot of our audit and investigative resources, more than 700 banks, probably closer to 800 banks just through one program, the Capital Purchase Program, and we are responsible for safeguarding those investments.

The HAMP program is 110 different servicers, a lot of the large banks, and potentially millions of applicants coming in through the door.

The TALF program is a very complex program run by the Federal Reserve and Treasury. It involves 15 or 16 primary dealers and their customers.

The PPIP program is nine, now eight, sophisticated hedge fund asset management, which has a tremendous amount of challenges.

So I think one of the reasons why—our budget is larger is that our scope is very broad and our responsibility is very broad. And I would compare us to other Special Inspector Generals. For example, we based a lot of our growth on the Special Inspector General for Iraq reconstruction, which oversees about $50 billion, compared to our much larger scope of—and our budget, when they were reaching their peak, is right around the same area.

The other Inspectors General—just by way of example, when ours was passed, one Inspector General commented for us that it would only leave him resources with one auditor per billion dollars, which that Inspector General thought was an unmeetable goal. If we had one auditor for every billion dollars, our audit division alone would be 700, not even counting our investigations.

We have taken costs very seriously from day one. We try to be frugal, we try to be prudent, and, above all, we try to get the most bang for our buck to get the most coverage possible for this breathtakingly complex program.

Mr. SERRANO. Thank you.

Mrs. Emerson.

Mrs. EMERSON. Thank you.

Thank you so much for being here and thanks for the great job that your office is doing under your leadership. It really makes those of us who have to live and breathe this every day feel a lot better because you all are watching over our very precious tax dollars.

Let me ask you, you mentioned some of the audits and that sort of thing that you had done, and I read it in the part of the quarterly report I got through last night—I must say I didn't finish the whole thing—but, last year, you stated in written testimony—and I am going to quote: We stand on the precipice of the largest infusion of government funds over the shortest period of time in our Nation's history. History teaches us that an outlay of so much money in such a short period of time will inevitably attract those seeking to profit criminally. If by percentage terms some of the estimates of fraud in recent government programs apply to the TARP programs, we are looking at the potential exposure of hundreds of billions of dollars in taxpayer money lost to fraud, end quote.

So, number one, have your fears materialized and have you been able to find any large-scale fraud in the TARP programs? If so, what types of fraud have you uncovered? And then, third, how closely are other agencies such as HUD, the FBI, SEC, FTC, and U.S. Attorneys working with you all to investigate and prosecute cases of fraud?

Mr. BAROFSKY. I believe that ultimately the success of my organization of SIGTARP historically will be judged by how we do against those typical numbers of the 10 percent burn rate for the FBI. Sometimes it is 7 percent, sometimes it is 12 percent. I think we are really well on our way because, even more important from our investigative functions, I believe, in detecting and bringing people to justice, is how much we do as a job of deterrence through building and making our recommendations to make these programs as safe as possible and then for getting the word out and making sure that those who are contemplating committing fraud know we are out there.

We certainly are seeing fraud, probably inevitable of a program of this size. We are not so far seeing anything close to what the typical government burn rate is for fraud. Now we still have a ways to go to be sure, but I am very—we really try to get out in front.

I mentioned in my opening testimony the TALF PPIP Task Force. That is not just a law enforcement group where we sit around and figure out ways to arrest people. A lot of our recommendations came from those discussions. We try to get experts from the SEC, from the FBI together so we can make these programs well designed.

I think the TALF program, when we originally started, it was originally pitched to us by the Federal Reserve. It had virtually no fraud protection whatsoever. It was going to rely on rating agencies and investor due diligence, the two things that led to this financial crisis in many ways. I think now this program is remarkably well designed.

They took our recommendations to heart. I remember they came down the day after our first initial report, came down to Washington and sat with us and worked with us and put in some really, really good protections. Sometimes they went beyond what we said, which we thought was terrific.

They kept residential-mortgage-backed securities out of that program, which was a pretty courageous move. I mean, this is something that was announced by the Secretary and the Chairman of the Board of the Federal Reserve that they were going to put those securities through that program. We had real problems with it, because we didn't think the program was well designed, and they listened to it.

So, real quick—I hear the buzzing—we have had wonderful cooperation with the Department of Justice, the U.S. Attorney's office, our law enforcement partners. We work with HUD OIG, we work with FDIC CIG, really, every law enforcement agency that has a hand in white-collar law enforcement works with us on our cases, Postal, ICE, and we also work with State and local authorities as well, like the New York State Attorney General. The New York State Banking Superintendent is very supportive in our recent case in New York.

Mrs. EMERSON. I appreciate that. Thanks.

I think, just to let the other colleagues get a question in, I will wait and do another round if we do.

Mr. SERRANO. I agree. I thank you.

Mr. Fattah.

Mr. FATTAH. Let me go back to the chairman's question about contracted services, services you contract out for. You didn't describe any or make any response to that question.

Mr. BAROFSKY. Oh, I will be happy to.

Basically, for contracting, obviously, EESA gives us the authority to do so. And when we do our contracting, we always try to do it when it is most cost-effective. As a temporary agency, we have to be sort of selective in what we bring in-house and what we contract out, because we are not a permanent organization, to build and hire up.

Mr. FATTAH. Tell us what you do. What kinds of services have you the contracted out for?

Mr. BAROFSKY. Perhaps our most significant contract is a program manager to help us with the production and design of our quarterly reports. The quarterly report has a tremendous amount of data that we collect in it, that we crunch and turn into charts and numbers. We do extensive vetting; and we have a contractor, Deloitte, actually, financial advising services, which assists us in that.

We then have a bunch of smaller contracting services, everything from cars for our investigators, our special agents, to buy supplies for them, rent, obviously, as well as parking spots. We have other advisory services that help us with, you know, some of our human resource functions. We don't do all of our human resource functions in-house because, as I said, as a temporary agency it would just be too expensive.

Mr. FATTAH. Your total personnel complement is?

Mr. BAROFSKY. Right now, we are at 116 FTE.

Mr. FATTAH. Can you guesstimate for the committee the number, the percentage, of women, African Americans, Hispanics, what level of diversity? Since you are the cop for TARP, I was interested in the question of how diverse the picture might be. So can you give us a general notion?

Mr. BAROFSKY. I don't want to hazard numbers, because I don't have them, but I am happy to get those numbers to you, assuming our H.R. Department keeps track of them.

I know that I have emphasized from day one from to all of my senior managers who do the hiring on down the importance of diversity, and we certainly do strive for it.

Mr. FATTAH. Your senior managers, is it a diverse group of people?

Mr. BAROFSKY. I believe our senior staff is remarkably diverse.

Mr. FATTAH. In your contracting out, have you utilized women and minority-owned, veteran-owned firms?

Mr. BAROFSKY. Yes. We actually required for our largest subcontract with Deloitte that they subcontract to minority, small business, minority-owned, women-owned small business.

Also, with our other, smaller contracts, advisory contracts, I know that has been an emphasis.

As I said, I don't have the numbers and statistics at my fingertips, but I will get them for you.

Mr. FATTAH. Mr. Chairman, if we could have that request made for the record. Thank you very much.

Mr. BAROFSKY. My deputy reminded me that when we went out and contracted for our use of funds survey we did hire a minority, woman-owned small business as well. So it is something that is always on the forefront of what we are thinking, but I just don't have the data.

Mr. FATTAH. Thank you very much.

Mr. SERRANO. We will make that request on the record, Mr. Fattah.

Mr. Culberson.

Mr. CULBERSON. Thank you, Mr. Chairman. I will be as brief as I can.

Do you know how much money the Federal Reserve has loaned out and to who and under what terms and conditions and can you provide that to the committee, please?

Mr. BAROFSKY. We did a comprehensive review last July, not just the Federal Reserve but all the different Federal government support of the financial industry during the crisis. So we will get you a copy of our July 2009, report. I fully plan to update that in our next quarterly report this July; and, obviously, we will get that back to you as well.

Mr. CULBERSON. Thank you. I am sorry I didn't see it.

Does it give detail as to who, what entities the Federal Reserve loaned money to? Because that has always been a concern to Members of Congress. Who are they loaning my daughter and our kids' money to and under what terms and conditions?

Mr. BAROFSKY. Hopefully, that decision will be made by the Supreme Court.

Mr. CULBERSON. They are not releasing the information.

Mr. BAROFSKY. The Federal Reserve doesn't disclose it. There was recently a decision in the Second Circuit Court of Appeals that is going to order them to make available that type of information. My understanding is they are appealing that decision.

Mr. CULBERSON. I bet. Could you send that to me? I would love to see the court case, too.

We are running short of time.

The HOPE for Homeowners Program that the chairman asked you about, that is in section 110 of the TARP bill, I recall. It is now title 12 of the United States Code, section 5220. Was that the same program you were talking with the chairman about?

Mr. BAROFSKY. No, actually, HOPE for Homeowners is something a little bit different. That is a HUD program.

Mr. CULBERSON. It is a separate program, but, I mean, the statute, TARP, references that. The purpose of the subsection of TARP is to implement the provisions of HOPE for Homeowners is my point, right?

Mr. BAROFSKY. In certain aspects.

Mr. CULBERSON. Do I remember it correctly? That is the section we are talking about of TARP?

Mr. BAROFSKY. I don't remember the exact section either.

Mr. CULBERSON. That language of that section says that the Federal property managers can, as I recall—in order to encourage people to stay in their homes, to encourage homeownership consistent with HOPE for Homeowners Program, the Federal property manager can, to the extent that the Federal property manager or the Treasury owns a mortgage-backed security or mortgages, reduce the amount of principal, reduce the amount of the interest, will make any other modification they wish. Is that accurate? Essentially that is what it is, isn't it?

Mr. BAROFSKY. I mean, essentially, I think that was sort of a carryover of what TARP was originally intended to be, which was that the Federal Government was going to go out and buy toxic assets, including home mortgage loans, mortgage-backed securities. Because that really has never come to pass, I don't think those provisions have really——

Mr. CULBERSON. But is that the section you are talking about? You said to the chairman, there is 230,000 permanent modifications that have been made to mortgages. I think that is the same program, isn't it, Mr. Chairman?

Mr. BAROFSKY. No, Congressman, it is a separate program that has been initiated under TARP called the Home Affordable Modification Program.

Mr. CULBERSON. Okay, completely separate.

Mr. BAROFSKY. Completely separate. There the government doesn't actually own the mortgages. They are actually owned by private investors through private label mortgage-backed securities, or Fannie and Freddie, which technically is not the government owning those mortgages. But that program addresses privately-held mortgages.

We don't really have through TARP an inventory of mortgages. Although that was what perhaps was originally intended with legislation, it is not what came to pass.

Mr. CULBERSON. Well, I wish you would run this down for me, because it is in statute. And I spotted it, and I voted against the TARP, but this is one of the many reasons I voted against it. But it was a real source of concern to me.

This other program you were mentioning to me, does the Federal Government then have the ability to insist that the bank modify the principal, reduce the interest, or make any modifications they can to keep the person in the home or keep somebody in the home?

Mr. BAROFSKY. Once a mortgage servicer signs into the agreement—and so far more than 110 have, which covers about 90 percent of the market—they are required to run a net present value test, a computer model that determines whether or not the mortgage modification, which there will be certain incentives provided by the government, if that will make more money for the investor than rather just doing nothing. And when that NVP test is positive under the program, the servicer is required to—it is mandatory—to do certain modifications of the mortgage. Under the current program, it starts with the reduction of the interest rate, and then it is followed by other factors like extending the term of the loan or forebearing.

Mr. CULBERSON. Can we get the name of the program?

Mr. BAROFSKY. That is the HAMP Program, the Home Affordable Modification Program.

Mr. CULBERSON. Thank you, Mr. Chairman. I know we need to go vote, but it was a concern just because of obvious potential for fraud and abuse.

Mr. BAROFSKY. We are literally all over this program. We have more than two dozen criminal investigations pending relating to the HAMP Program.

Mr. CULBERSON. Two other quick questions.

If you could ballpark the total amount of the exposure of taxpayers, in your opinion, the potential liability of taxpayers. How much have taxpayers been exposed to both through the Federal Reserve and through the Treasury through this TARP Program and other guaranteed programs like it?

Mr. BAROFSKY. In July of 2009, when we did this analysis, it was about $3 trillion. What we are going to see, as I said, we are going to update it this July, and we will give you an updated number at this point.

Mr. SERRANO. There is no way we can leave to vote and come back. That will take quite a while. I don't want to have you wait here, but you have answered most of the questions.

I was going to ask one more. So I am going to ask one more, and Mrs. Emerson, and then we will let you go. And this is one of those great, loaded questions.

So if your staffing number is lower than expected in 2010, we assume that you will have money left over to carry into 2011, which means you won't need the over $49.6 million that you are asking for in 2011. Is that a fair assumption or are you going to tell me now how you need every bit of the $49.6 million?

Mr. BAROFSKY. I am told by my budget folks that we do. And the reason is that we have a lot of expenses that I think we anticipated that are going to be incurred in this year in 2010 that are not going to be—specifically with respect to our information technology, you know, we still—right now, we are sort of doing it with band-aids and duct tape.

We have to build our own IT structure, not completely from scratch, but decide on what off-the-shelf products we are going to use. We have been relying on Treasury to sort of get us through. And what I have been told is that those funds are not going to be spent in 2010 and are not reflected in the 2011 budget.

So to the extent that this carryover of that money is going to be still spent in 2011 and that carryover will apply to that, we do anticipate spending all of our—I get the terminology wrong, and I apologize—our annual money, the money that we are being provided for 2010, that will be spent. There will probably be something left over of our no-year money, which is part of the initial allocation, and I apologize if I am getting the terminology wrong.

But, again, as my staff tells me, because we haven't realized some of the expenses that we thought we would in 2010, that they are going to be realized in 2011.

Mr. SERRANO. Okay. We would like you to keep us informed of that. In other words, speak to staff as we go along to make sure that we feel comfortable that even if you don't meet the goals you expected that we are still not giving you more money than you should be getting only because, across the board, everybody is very tight, and we don't want to run into any problems.

Mrs. Emerson.

Mrs. EMERSON. Okay, 222 people haven't voted; and we have zero minutes remaining.

Very, very quickly, because I am still bothered by this, with regard to the Treasury Department, back in December, approving a tax rule that allowed Citigroup to avoid paying billions of dollars in taxes. And I understand that this ruling will help make Citigroup shares more valuable, allowing the Treasury to make more money when you sell the shares that the government owns. But I guess it is just difficult for me to understand why a company that receives tens of billions of dollars in government bailouts should receive special treatment in the Tax Code. So I want to know if you have looked into this matter and whether or not you believe that the government will receive more revenue once Citigroup shares are auctioned than it would have if the tax rule hadn't been changed.

Mr. BAROFSKY. This is the initiative that we have spent a lot of time thinking about. And, actually, Representative Kucinich has sent a letter to myself as well as to Senator Baucus, the chairman of the tax committee in the Senate, asking us to do two parts of a project that will review that: our side to review the decision-making process that led up to that decision, and on the Senate side to do a review of what the actual costs were, what is the dollars and cents.

It is a very complicated and complex formula. Originally, I was hopeful that we would be able—you know, we were thinking about doing it ourselves. We can't. We don't have the expertise. We would have to contract it out. It would cost a fortune.

So we are intending, we are going to work with the Senate and work with the tax committee and get to the point where we can, you know, make sure that that part of the project is being addressed. And, if so, we are certainly committed to addressing our part of getting and auditing what the decision-making process is.

Mrs. EMERSON. Thank you. I appreciate it.

Mr. BAROFSKY. Because we agree that it is a very significant concern. It is a concern where, basically, the stock prices of Citi is being potentially buoyed, which benefits the government, as a 28 percent shareholder of the common stock of Citi, but it also benefits those other 82 percent, or 72 percent. So it is something that is on our radar screen.

Mrs. EMERSON. I appreciate it. There is something that just smells funny about it to me. So I appreciate the fact that you all are going to look into it and will appreciate hearing back from you about what you may have found.

Mr. BAROFSKY. Absolutely.

Mr. SERRANO. We will all be interested in that.

Mr. Barofsky, we thank you, first of all, for your service. We thank you for the work you do. We thank you for testifying before us.

We are sorry that we are kind of rushing here, but we are at zero. And there are at least four votes, which means this will go on for a while down there, and we don't want to keep you waiting here for us.

So we thank you. We will continue to be in touch, and our staffs will continue to be in touch. And what you do is very important, very important to our mission here, to keep us informed and to do the right thing. And we thank you so much.

Mrs. EMERSON. Thank you.

Mr. BAROFSKY. Thank you very much.

SUBCOMMITTEE ON FINANCIAL SERVICES AND GENERAL GOVERNMENT

HEARING
ON
TARP and the Financial Crisis

QUESTIONS FOR THE RECORD:

U.S. DEPARTMENT OF TREASURY

ASSISTANT SECRETARY FOR FINANCIAL STABILITY

HERBERT M. ALLISON

APRIL 22, 2010

Questions from Chairman José E. Serrano

1. **A wave of home foreclosures is forcing families from their homes, driving down home prices, and depriving local governments of needed revenue. To its credit, the Treasury Department has attempted to address this problem by offering incentives to borrowers, servicers, and investors to modify loans through the Home Affordable Modification Program (HAMP). As of April 2010, however, only 230,000 homeowners had received more than temporary loan modifications. That number pales in comparison to the almost three million homeowners who have received a foreclosure notice since Treasury announced its program last year. Another six million borrowers are currently more than 60 days delinquent on their mortgages. Millions more are current on their mortgages but owe more than their homes are worth. Furthermore, a number of banks continue to resist meaningful mortgage modification.**

   Recently, the Treasury Department has proposed new measures to address the foreclosure crisis by assisting with mortgage reduction. Are the mortgage companies cooperating in this new plan? How many struggling homeowners will it likely help with permanent mortgage relief?

   The Administration's March 26 announcement noted that we would be enhancing options for homeowners facing hardships due to negative equity. These enhanced options included:

   - Revisions to the Second Lien Modification Program;
   - Adjustments to the Federal Housing Administration's refinance program; and
   - Consideration of an alternative modification approach that emphasizes principal relief in the HAMP waterfall.

   The Second Lien Modification Program (2MP) creates a comprehensive solution to help borrowers achieve greater affordability by lowering payments on second lien mortgage loans when the first is modified under HAMP. In addition to providing the basis for lien holders to share the cost of modifications, this program supports efforts to reduce total borrower indebtedness by providing the option for second lien holders to receive lump sum payments to extinguish their liens entirely. Revisions to program guidance increased the extinguishment schedule to better incentivize principal reduction in this area. To date, Bank of America, Citi, JPMorgan Chase, Wells Fargo Bank, Bayview Loan Servicing, Servis One, and iServe Servicing are participating in the program. Together, these seven servicers account for just over half of second lien loans and we expect more servicer participation in the future.

   Adjustments to FHA refinance programs will permit lenders to provide additional refinancing options to homeowners who owe more than their home is worth because of large declines in home prices in their local markets. These adjustments will provide more opportunities for qualifying mortgage loans to be responsibly restructured and refinanced into FHA loans as long as the borrower is current on the mortgage and the lender reduces the amount owed on the original loan by at least 10%. Treasury and HUD are working to finalize guidance for this program, and we expect this option to be available by the fall.

On June 3, 2010, Treasury published Supplemental Directive 10-05: *Modification of Loans with Principal Reduction Alternative (PRA)*. With these new rules, HAMP will offer mortgage relief to eligible homeowners whose homes are worth significantly less than the remaining amounts owed under their first lien mortgage loans.

Servicers will be required to evaluate all non-GSE HAMP-eligible loans with a mark-to-market loan-to-value ratio greater than 115% to determine if a principal reduction is beneficial. If the evaluation shows the net present value (NPV) for a HAMP modification using PRA is positive, servicers are encouraged to offer the principal reduction to the borrower. An updated NPV model reflecting principal reduction will be available to use for this evaluation.

PRA is earned over a three-year period and is initially treated as a PRA Forbearance. Each year (for three years) that the borrower is in good standing on the anniversary of their trial period effective date, the servicer must reduce the unpaid principle balance of the loan installments equal to one-third of the original PRA forbearance amount.

Additionally, servicers participating in the Second Lien Program (2MP) will be required to provide a principal reduction on the borrower's second mortgage in proportion to any principal reduction offered on the borrower's first mortgage.

The PRA Effective Date (i.e., the date the principal reduction evaluation is required) is October 1, 2010, though servicers may immediately offer PRA for HAMP-eligible modifications as long as the reduction follows all PRA requirements. Additionally, PRA will be retroactive and guidance regarding PRA for borrowers already in a HAMP modification is forthcoming.

Servicers have been receptive to these changes and are working to recalibrate their systems appropriately. They have committed to PRA as a standardized mechanism by which they can demonstrate that, when they forgive principal for modified mortgages, they are fulfilling their fiduciary duty. Along with its financial agents, Fannie Mae and Freddie Mac, Treasury will provide support to servicers over the coming months to assist them in making their systems fully functional by PRA's effective date.

As we had mentioned in an earlier Question for the Record from you, there continues to be little precedent for estimating the number of homeowners who ultimately receive a permanent modification under HAMP. We acknowledge that there will be fewer permanent modifications than trial modifications, as modifications are only offered permanent status once the homeowner has accepted a trial modification, has performed for at least three months in a trial modification, and has met the full documentation requirements for the permanent modification. The extent to which homeowners receive and maintain a permanent modification is therefore subject to a number of conditions that, even one year into the program, have been difficult to assess.

As these changes are implemented over the coming months, they will improve the program's ability to assist three to four million homeowners in avoiding foreclosure. However, the precise impact of these changes on program participation is still uncertain as they arrive with little precedent and will largely vary based on economic or housing market conditions going forward.

HAMP has been designed for homeowners who are at risk of foreclosure and can benefit from a reduced monthly mortgage payment. HAMP was not designed to help every borrower. Borrowers who purchase investment properties, second homes or vacation homes, for example, are not included in this program.

2. Why has the original HAMP program not been as successful as the Administration had hoped?

HAMP is the first national, standardized modification program—one that has led the way in setting an industry standard for affordable and sustainable mortgage modification. HAMP has been a catalyst for change by incentivizing servicers to develop the capacity and resources necessary to execute modifications on a large scale. HAMP defines a standard for an affordable and sustainable modification across the industry, set at 31% of gross monthly income. Until HAMP, the industry did not have a standard process for mortgage modifications, an affordability standard, or standard timelines by which modifications would be processed. HAMP has begun to systematize across servicers the method and process for modifying loans by setting affordability standards, requiring sound underwriting guidelines, and establishing a specific modification protocol and a defined timeframe for responding to modification requests. This has brought more efficiency and transparency to modifications.

HAMP has demonstrated real progress, as evidenced in our most recent public report. Homeowners in active modifications have had their monthly payments reduced substantially – around $500 for the typical homeowner – with aggregate savings totaling $3.2 billion.

In June, more than 50,000 borrowers in modifications received permanent status. There are now nearly 400,000 homeowners with permanent modifications, with servicers maintaining an average conversion rate of approximately 50,000 modifications per month for the past six months. The conversion rate from trial to permanent modifications is much improved, but is still not satisfactory.

Even those borrowers who do not obtain a permanent modification still benefit from reduced payments during the trial phase and the time the trial affords them to find an appropriate solution. In the May Servicer Performance report, Treasury published new survey data on the disposition of trial cancelations, which showed that nearly half of homeowners unable to enter a HAMP permanent modification entered an alternative modification with their servicer. Fewer than 10 percent of canceled trials move to foreclosure sale. In this way, HAMP is successfully helping homeowners avoid foreclosure and achieve more favorable outcomes.

Even with this success, we have encountered a number of challenges. The process of converting trial modifications to permanent has been hindered by several factors, including slow ramp up and insufficient capacity and execution at most servicing shops, a lack of willingness or ability to provide necessary documentation on the part of some borrowers, and a conversion and implementation process more complex administratively than originally conceived. We found that the parallel nature of the foreclosure process during a HAMP trial period has been confusing to borrowers and many have complained about conflicting signals regarding the status of their mortgage. Also, unemployment and negative equity have posed significant challenges and, until recently, have not been satisfactorily addressed by HAMP.

The enhancements announced on March 26, 2010 are responsive to these challenges and to the changing needs of homeowners across the country. Going forward, the newly enhanced program will provide temporary mortgage assistance to some unemployed homeowners; encourage servicers to write-down mortgage debt as part of a HAMP modification, allow more borrowers to qualify for modification through HAMP, and help borrowers move to more affordable housing when modification is not possible.

Lastly, the Administration has also recognized that key factors causing severe distress in certain markets could be addressed in a more targeted fashion by agencies most familiar with the dynamics of those markets. In response, the Administration announced the Housing Finance Agency Innovation Fund for the Hardest-Hit Housing Markets (the "HFA Hardest-Hit Fund") for ten state HFAs to design innovative, locally targeted foreclosure prevention programs. Focusing on these areas will allow limited funding to be deployed with enough scale to have a more significant impact. We expect state HFAs to begin implementing their programs starting this summer.

3. **In making his initial case for TARP, Secretary Paulson said that the $700 billion would be used to take "Troubled Assets" off the books of banks so that the banks would have the confidence to do more lending. Soon after the legislation passed, however, Treasury used the funds in much different ways. Almost $500 billion in TARP funds have been committed for a number of complex arrangements. I assume that, as long as those commitments remain, The Appropriations Committee will be asked to fund SIGTARP.**

   What are your plans for winding down your TARP commitments to the banks? To the auto companies? To AIG? To other arrangements?

4. **How long will that take?**

Response to questions 3 & 4:

As of October 3rd, 2010, there will be no subsequent TARP commitments as dictated by the legislation. As of the signing of the Dodd-Frank legislation, there will be no new TARP commitments for programs that have not already been announced. As TARP continues to wind-down, we have received repayments of $194 billion which has reduced total disbursements outstanding to $190 billion. We are also in the process of closing out AGP, TIP, and other programs as a result of the repayments of specific securities.

Seventy-six of the banks that received investments under Capital Purchase Program have repaid Treasury in full, and of the $205 billion invested, more than $146 billion has already been repaid. Treasury continues to work with federal banking regulators who must evaluate requests from CPP participants interested in repaying Treasury's investment.

Because of the size of certain positions as well as the overall portfolio, successful disposition will take time, as well as expertise. In addition, information about Treasury's intentions with respect to its investments could be material information and premature release of such information could adversely affect the ability of Treasury to achieve its objectives. Therefore, Treasury will make public announcements of its disposition plans when it is appropriate to do so.

Treasury has already begun to exit some of its investments under the AIFP. In July 2009, we terminated the Warranty Commitment Program, and Chrysler Financial fully repaid its loan. The Supplier Support Program was terminated in April of this year, and GM repaid the balance of its loan from Treasury. Treasury also received a $1.9 billion repayment as settlement of a loan made in early 2009 to finance Old Chrysler.

With respect to Treasury's continued investments in GM, Chrysler and Ally Financial (previously known as GMAC), we will periodically evaluate both public and private options to exit these investments. For example, for GM the most likely exit strategy is a gradual sell off of shares beginning with an initial public offering. Our goal is to exit the government's interests as soon as practicable. The government will commit itself to sell down, and ultimately sell off completely its interests in a timely and orderly manner that minimizes financial market and economic impact. At the same time, we cannot control market conditions and have an obligation to protect taxpayer investments and maximize overall investment returns within competing constraints.

Treasury's AIG preferred stock investment has no mandatory repayment date. AIG has replaced most of its board of directors, as well as its chief executive officer since September 2008, and is presently engaged in a variety of restructuring initiatives, including the divestment of assets to enable repayment of loans made by the FRBNY, as well as Treasury's TARP investment and the wind-down of exposure to certain financial product and derivative trading activities to reduce excessive risk taking.

5. **When the books are closed on TARP, what do you predict will be the total budgetary cost of TARP?**

6. **In August 2009, the Administration projected that TARP—which permitted up to $700 billion in Government financial assistance to be outstanding at any given time—would ultimately cost a total of $341 billion; today, that cost is over $225 billion lower. Please provide data on TARP recipients relating to their lending to minority and women-owned businesses.**

Response to questions 5 & 6

Last year as part of our commitment to Congress and to the public to enhance communication and provide information about our programs to stabilize the financial system, we began monthly bank lending surveys. Although information regarding minority- or women-owned businesses is not collected separately, our two surveys provide frequent and accessible information on the lending and other activities of banks receiving government investments.

The Monthly Lending and Intermediation Snapshot reports quantitative information that is voluntarily submitted by CPP participants about three major categories of lending – consumer, commercial, and other – and includes commentary explaining changes in each category as well as a discussion of lending demand and credit standards, which is designed to help Treasury and the public meaningfully and accurately interpret the quantitative data. The CPP Monthly Lending Report includes the average outstanding balances of consumer loans, commercial loans, and total loans of all CPP participants. Additional information on our surveys can be found at http://www.financialstability.gov/impact/surveys.htm.

SUBCOMMITTEE ON FINANCIAL SERVICES AND GENERAL GOVERNMENT

HEARING
ON
TARP and the Financial Crisis

QUESTIONS FOR THE RECORD:

NEIL BAROFSKY,

SPECIAL INSPECTOR GENERAL,

FOR THE TROUBLED ASSET RELIEF PROGRAM

APRIL 22, 2010

Questions from Chairman José E. Serrano

Questions for Neil Barofsky, Special Inspector General for the Troubled Asset Relief Program:

1. What does the SIGTARP see as the biggest challenges to ensuring transparency and effectiveness of the various TARP programs?

Answer: One of the biggest challenges to ensuring transparency and effectiveness relates to the Home Affordable Modification Program ("HAMP"). Many of Treasury's recent efforts have focused on HAMP and related foreclosure prevention initiatives. Unfortunately, HAMP continues to struggle to achieve its original stated objective, to help millions of homeowners avoid foreclosure "by reducing monthly payments to sustainable levels." Despite a seemingly ever increasing array of HAMP-related initiatives designed to encourage participation in the program, the number of homeowners being helped through permanent modifications remains anemic, with fewer than 400,000 ongoing permanent modifications (only approximately 164,000 of which are in connection with the TARP-funded portion of HAMP), and HAMP has not put an appreciable dent in foreclosure filings. Indeed, the number of trial and permanent modifications that have been cancelled substantially exceeds the number of homeowners helped through permanent modifications. One continuing source of frustration is that Treasury has rejected calls to announce publicly any goals or performance benchmarks for HAMP or its related initiatives concerning how many homeowners it actually expects to help stay in their homes, despite repeated recommendations that it do so from SIGTARP, the Congressional Oversight Panel and the Government Accountability Office. Instead, Treasury clings to its prior statements that it plans to offer trial modifications to three to four million homeowners, a measure that SIGTARP has previously shown to be essentially meaningless. Treasury's refusal to provide meaningful goals for this important program is a fundamental failure of transparency and accountability that makes it far more difficult for the American people and their representatives in Congress to assess whether the program's benefits are worth its very substantial cost. The American people are essentially being asked to shoulder an additional $50 billion of national debt without being told, over 16 months after the program's announcement, how many people Treasury hopes to actually help stay in their homes as a result of these expenditures, how many people are intended to be helped through other subprograms, and how the program is performing against those expectations and goals. Without such clearly defined standards, positive comments regarding the progress or success of HAMP are simply not credible, and the growing public suspicion that the program is an outright failure will continue to spread.

An additional challenge with respect to transparency, as found in several SIGTARP audit reports, is that Treasury is not adequately documenting its oversight and decision-making processes within individual TARP programs. Such documentation is necessary to ensure that similarly situated participants are treated the same, and that any disparities are thoroughly explained and reasonable. Absent this sort of documentation, TARP cannot achieve the transparency it needs to convince the public that Treasury is a competent steward of its tax dollars.

2. The SIGTARP budget submission notes that the SIGTARP expects to fund 133 Full-time Equivalent staff for fiscal year 2010. We are now more than halfway through the fiscal year. Does the SIGTARP still expect that number, or will it ultimately come in lower than that for the year? How many staff are currently onboard?

Answer: SIGTARP has made great progress in hiring staff this fiscal year. As of June 30, 2010, SIGTARP has 126 staff on board with an additional eight hires scheduled to begin service within the next few weeks. This represents a 41% increase since the beginning of the fiscal year for an anticipated total of 134 staff on board by the end of the fiscal year. As reflected in the FY 2011 President's Budget Submission, SIGTARP estimated funding 133 Full-time Equivalents ("FTE") (out of the 160 FTE ceiling) in FY 2010. With three quarters of the year under our belt, SIGTARP now anticipates that the annualized FTE for FY 2010 will be 116.

3. What percentage of the SIGTARP workforce is comprised of women? Of minorities?

Answer: Of SIGTARP's staff of 126 employees, 54% (68) are included among designated EEO groups (which are comprised of women, minorities, and individuals with disabilities). Further, 38.1% (48) of SIGTARP employees are women and 34.9 % (44) are minorities (which includes Hispanic, Black, American Indian, Alaskan Native, Asian, Native Hawaiian or Pacific Islanders, and those in 2 or more race categories). SIGTARP is committed to building and sustaining a diverse workforce while continuing to recruit the "best and brightest" to accomplish our mission. It is also important to note that minority status reporting is based on self-identification information collected at the time of employment.

4. Please provide any data you have on SIGTARP contracts and subcontracts going to small businesses, women-owned firms, minority-owned firms, and veteran-owned firms.

Answer: The following is a list of SIGTARP service contracts and goods purchases solicited from small businesses, woman-owned firms, minority-owned firms, and veteran-owned firms:

Vendor	Type	Product/Service Description	Amount
Information Innovators, Inc.	Woman-Owned Firm & Service-Disabled Veteran Owned	Automated IT Services	$577,584.38
Metro Office Solutions	Woman-Owned Firm; SBA Certified Disadvantaged Business; SBA Certified 8(a) Program	Office Furniture	$22,359.32

	Participant		
Edwards Systems Technology	Small Business	Badges/Insignia	$7,584.88
Buncher Carole	Woman-Owned Firm	Other Educational/Training Services	$6,500.00
Ball and Ball Communications Inc.	Small Business	Misc Alarm, Signal and Security Systems	$9,978.00
Unified Teldata Inc.	Woman-Owned Firm & SBA Certified 8(a) Program Participant	Installation of Automated Data Processing ("ADP") Equipment and Supplies	$24,914.14
National Journal Group Inc.	Small Business	Subscription	$3,499.00
Adaptive Digital Systems Inc.	Small Business	Video Recording and Reproduction Equipment	$18,650.00
Immixtechnology Inc.	Small Business	ADP Software	$23,631.44
Executive Protection Systems Inc.	Service Disabled Veteran-Owned Firm	Safety and Rescue Equipment	$32,822.56
Apptis Technology Solutions LLC	Small Business	ADP Software	$22,150.59
Sword & Shield Enterprise Security	Small Business	ADP Components	$53,057.33
Lyme Computer Systems Inc.	Woman-Owned Firm	ADP Support Equipment	$3,336.00
Red River Computer Company Inc.	Small Business	ADP Software	$10,177.42

Overall, as of June 25, 2010, SIGTARP has initiated direct procurement actions with 29 different vendors, 48.3% (14) of which are small businesses. Within the small business category, 28.6 % (4) are small disadvantaged, minority- or veteran-owned firms, and 35.7% (5) are women-owned enterprises. SIGTARP also has 21 interagency agreements with other federal government agencies that total $8,866,098.10.

WITNESSES