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FINANCIAL NEWS FOR THE MORTGAGE MARKET

Fed let AIG subsidiary into emergency funding program sans documentation

by JON PRIOR
October 4th, 2011

The **Federal Reserve Bank of New York** allowed an unnamed entity sponsored by **American International Group** (AIG: 19.66 -3.91%) into an emergency funding program during the height of the crisis without documenting why, according to an audit released Tuesday.

In October 2008, the **Federal Reserve** launched the Commercial Paper Funding Facility to provide a backstop to issuers of commercial paper as money market mutual funds and other investors faced a liquidity crisis. The name of the subsidiary was not disclosed.

But in 2009, the New York Fed allowed an AIG-sponsored company to issue to the CPFF, "even though a change in program terms by the Federal Reserve Board likely would have made it ineligible," according to an audit from **Government Accountability Office**.

"FRBNY staff said they consulted the Federal Reserve Board regarding this situation, but did not document this consultation and did not have any formal guidance as to whether such continued use required approval by the Federal Reserve Board," said Orice Williams Brown, managing director and community investments at the GAO, in testimony before a House subcommittee Tuesday.

The Dodd-Frank Act requires any decisions on future emergency programs be documented fully. Brown said her office had to sit down with Fed officials in order to obtain information on the AIG situation through interviews.

When asked if any further work was being done to reveal why the AIG subsidiary was allowed to participate, Brown replied, "No further work is being done as to why that was allowed to occur."

AIG paid back $2.15 billion in Troubled Asset Relief Program bailouts in August, leaving $51 billion still outstanding, according to the **Treasury Department**.

The GAO made several recommendations to the Fed, including increasing transparency on these programs, provide contracts competitively — those doled out during the crisis were not – and strengthen risk management practices for future crisis lending.

At its peak, emergency loans outstanding to financial institutions from the Fed reached more than $1 trillion in late 2008.

Mark Calabria, a director of financial regulation studies at the **Cato Institute,** said the Fed has consistently resisted efforts to make its actions more transparent, specifically with AIG.

"I distinctly remember, as a staffer for the Senate Banking Committee, listening to then Fed Vice Chair Donald Kohn tell that committee that making the names of AIG's derivatives counterparties public would severely harm our financial markets," Calabria said before the committee Tuesday. "When those names were eventually released, our world did not come to an end."