

Introduction

As we write this report, the world is struggling with the major financial crisis of this generation. Its depth in the United States is reflected in the increased number of workers in search of employment, the steep decline in economic activity, and the sharp growth in home foreclosures and bankruptcies. *The New York Times's* grim account underscores the severity of the situation: “The fortunes of the American economy have grown so alarming and the pace of the decline so swift that economists are now straining to describe where events are headed, dusting off a word that has not been invoked since the 1940s: depression” (Goodman 2009).

The federal government has responded with a set of aggressive policies, including the Troubled Asset Relief Program (TARP). Congress approved the TARP during the waning days of President George W. Bush’s tenure. The \$700 billion in funding it authorized is being used in nine initiatives that aim to provide liquidity to financial institutions, as well as in the “stability” (loan modification) component of the Obama administration’s Homeowner Affordability and Stability Plan.

Implementing the TARP entails new responsibilities for the federal government. These new responsibilities include:

- taking major ownership positions in complex financial firms,
- auditing and restructuring troubled financial institutions,
- valuing poorly performing, complex financial assets,
- implementing large scale auctions and securitizations of poorly performing assets,

Key Acronyms

EESA	Emergency Economic Stabilization Act of 2008
FDIC	Federal Deposit Insurance Corporation
FHFA	Federal Housing Finance Agency
FIRREA	Financial Institutions Reform Recovery and Enforcement Act
FSLIC	Federal Savings and Loan Insurance Corporation
HOLC	Home Owners’ Loan Corporation
RTC	Resolution Trust Corporation
TARP	Troubled Asset Relief Program

- knowing when financial institutions are in such dire financial straits that they must be placed under conservatorship, and
- overseeing \$75 billion of the TARP funds to modify three to four million of the subprime mortgages at the foundation of the current crisis.

The public debate has primarily centered on the size and nature of the TARP—essentially the *policy* involved. Less attention has been paid to *administrative* issues:

- What organizational capabilities or capacities are necessary for any government entity that carries out the policy?
- What type of expertise, for example, does government need to implement these new responsibilities?

- What are the organizational challenges in carrying out the new tasks?
- What oversight mechanisms will ensure adequate accountability while at the same time allowing for organizational flexibility?
- How many employees are needed to implement the new responsibilities?

These are not incidental questions. Scholars note that government often lacks the capacity to implement policies (Pressman and Wildavsky 1984). Failure to achieve policy objectives contributes to public frustration and undermines confidence in government's ability to solve public problems. This report considers the simple but important question:

What administrative capacities are necessary for government to implement the new responsibilities?

Even under the best of circumstances, challenges confronted by government may be too big or complex to resolve, and present circumstances in U.S. finance are indeed challenging. However, there are examples in U.S. history of dire economic circumstances in which public agencies were created, took on new responsibilities, and defied expectations to satisfactorily resolve serious problems. Their stories offer insights into what administrative arrangements and capacities might best facilitate success in the present crisis.

Looking Back: Learning from Previous Government Experience

The experiences of two historic federal agencies suggest answers to the administrative challenges now facing the federal government in 2009:

- The Home Owners' Loan Corporation (HOLC), created by Congress in 1933 to resolve the foreclosure crisis of the Great Depression
- The Resolution Trust Corporation (RTC), created by Congress in 1989 to resolve the more recent savings and loan crisis

We examine the RTC and HOLC for two reasons. First, the agencies were charged with responsibilities that resemble those taken on by the government in

The Emergency Economic Stabilization Act

The **Emergency Economic Stabilization Act of 2008** (Public Law 110-343) was signed into law by President George W. Bush on October 3, 2008.

The Act, also known as EESA, created the **Troubled Asset Relief Program (TARP)** and a series of subsequent housing and capital investment programs for financial institutions. The TARP program authorized the Department of the Treasury to establish programs to stabilize the U.S. financial system and prevent a systematic collapse. The TARP program has nine components:

- A capital assistance program
- A consumer and business lending initiative
- A making home affordable program
- A public-private investment program
- Regulatory reform
- A capital purchase program
- An asset guarantee program
- A targeted investment program
- An automotive industry financing program

The **"Making Home Affordable Program"** includes three components:

- The Home Affordable Refinance Program for responsible homeowners suffering from falling home prices
- The Home Affordable Modification Program
- Support of low mortgage rates by strengthening confidence in Fannie Mae and Freddie Mac

The **"Home Affordable Modification Program"** has three components:

- \$75 billion from TARP for a loan modification program to reach three to four million homeowners by shared effort with lenders to reduce mortgage payments and providing incentives to servicers and borrowers
- \$2 billion from the Department of Housing and Urban Development for neighborhood stabilization program grants for innovative programs that reduce foreclosure
- \$1.5 billion to provide renter assistance, reducing homelessness and avoiding entry into shelters

the current crisis. The RTC was created during the midst of what was then described as the worst financial crisis since the Great Depression. As with certain financial institutions in the current crisis, savings and loans in the 1980s were severely undercapitalized. Congress created the RTC to stem the rising tide of failures by seizing control of failing thrifts, shutting them down, and selling institutions and assets back into the private sector. The HOLC was also charged with addressing a problem familiar to policymakers today: a crisis in home mortgage foreclosures. Today one in ten homeowners is in arrears or foreclosure, and new policies are charging the federal government to help defaulting homeowners. The HOLC was asked to do just that in 1933.

A second reason to look carefully at the RTC and HOLC is that both succeeded in their core tasks. The RTC took over and resolved 747 thrift institutions (nearly 40 percent of the savings and loan industry), with assets in excess of \$465 billion in 1989 dollars (Cassell 2002). The HOLC originated new mortgages for three years, which resulted in the HOLC ultimately owning 20 percent of the residential mortgages in the United States. HOLC was deemed successful in refinancing distressed homeowners while breaking even financially for taxpayers. And both agencies managed what few thought possible of public organizations: They shut their doors after completing their tasks.

Given their accomplishments, it is not surprising that in 2008 policymakers called for the creation of an RTC- or HOLC-like entity. In an editorial in the *Wall Street Journal*, then presidential candidate Hillary Clinton proposed “[a] new Home Owners’ Loan Corporation (HOLC), to launch a national effort to help homeowners refinance their mortgages. The original HOLC, launched in 1933, bought mortgages from failed banks and modified the terms so families could make affordable payments while keeping their homes. The original HOLC returned a profit to the Treasury and saved one million homes. We can save roughly three times that many today (p. A19).”

Clinton’s view was shared by policy experts from academia (Koppel and Goetzmann 2008), Blinder (2008) and Stelzer (2008), think tanks (Pollack 2008), and private consultants (Salsman 2008). The chair of the President’s Economic Recovery Advisory Board, Paul

Oversight of the “Making Home Affordable Program”

Many federal agencies are charged with implementing and overseeing the program:

- The Department of the Treasury oversees the entire program
- The Federal Housing Finance Agency is the conservator of the program
- Fannie Mae and Freddie Mac are responsible for monitoring compliance by servicers
- Federal Deposit Insurance Corporation and the Department of Housing and Urban Development both play roles in overseeing the program
- The Federal Housing Administration and the Department of Veterans Affairs have authority to provide claims in the event of bankruptcy or voluntary modification

Volcker, former Treasury Secretary Nicholas Brady, and former Comptroller of the Currency Eugene A. Ludwig argued, in a column in the *Wall Street Journal* (2008, p. A27), for a new RTC that would buy bad debt, restore liquidity to the financial system, and gain the flexibility to work with financially stressed homeowners to avert foreclosures.

A number of previous studies have examined the histories of the HOLC and RTC. The goal in this paper is not to retell these histories comprehensively, but to focus on aspects of the stories—framed here as questions—that highlight features which, in retrospect, turn out to have shaped performance. These organizational strengths and shortfalls can inform the debate policymakers should currently be having over what administrative capacities government needs to succeed with its current crisis resolution responsibilities.