



May 2016

TROUBLED ASSET RELIEF PROGRAM

Capital Purchase Program Largely Has Wound Down

GAO Highlights

Highlights of [GAO-16-524](#), a report to congressional committees

Why GAO Did This Study

CPP was established as the primary means of restoring stability to the financial system under the Troubled Asset Relief Program (TARP). Under CPP, Treasury invested almost \$205 billion in 707 eligible financial institutions between October 2008 and December 2009. CPP recipients have made dividend and interest payments to Treasury on the investments. The Emergency Economic Stabilization Act of 2008 includes a provision that GAO report at least every 60 days on TARP activities. This report examines (1) the status of CPP, (2) the financial condition of institutions remaining in the program, and (3) Treasury's strategy for winding down the program.

To assess the program's status, GAO reviewed Treasury reports on the status of CPP. In addition, GAO used financial and regulatory data to assess the financial condition of institutions remaining in CPP. Finally, GAO interviewed Treasury officials to examine the agency's exit strategy for the program.

GAO provided a draft of this report to Treasury for its review and comment. Treasury provided technical comments that GAO incorporated as appropriate.

View [GAO-16-524](#). For more information, contact Daniel Garcia-Diaz at (202) 512-8678 or garciadiazd@gao.gov.

May 2016

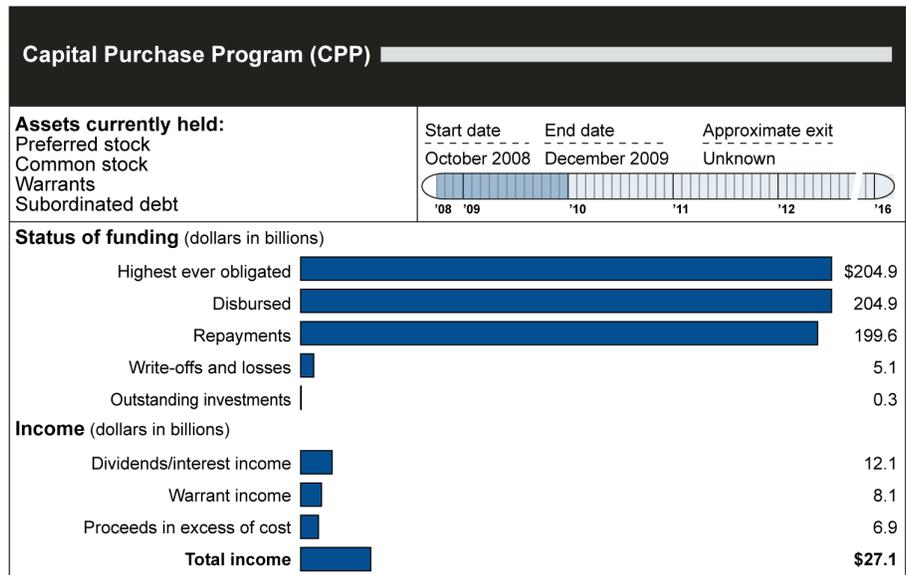
TROUBLED ASSET RELIEF PROGRAM

Capital Purchase Program Largely Has Wound Down

What GAO Found

The Capital Purchase Program (CPP) largely has wound down and the Department of the Treasury's (Treasury) returns on CPP investments surpassed the original amount disbursed. As of February 29, 2016, Treasury had received \$226.7 billion in repayments and income from its CPP investments, exceeding the amount originally disbursed by almost \$22 billion. As of the same date, 16 of the 707 institutions remained in the program. Treasury's most recent estimate of lifetime income for CPP (as of Nov. 30, 2015) was about \$16 billion.

Status of the Capital Purchase Program, as of February 29, 2016



Source: GAO analysis of Treasury data. | GAO-16-524

Most of the remaining CPP institutions have continued to exhibit signs of financial weakness. Specifically, 9 of the 16 institutions had negative returns on average assets (a common measure of profitability) in 2015. Also, 6 institutions had a lower return on assets in 2015 than they did at the end of 2011. Treasury officials stated that the remaining CPP firms generally had weaker capital levels and worse asset quality than firms that had exited the program. Also, nearly all the firms that are required to pay dividends have continued to miss payments.

Treasury expects most remaining CPP institutions to exit through restructurings but has not set time frames for winding down the program. Over the past 6 years, repayment of Treasury's investment and Treasury's auction of CPP securities to interested investors were the primary means by which institutions exited CPP. Restructurings—the expected exit method for the remaining firms—allow institutions to negotiate terms for their investments and require institutions to raise new capital or merge with another institution. With this option, Treasury agrees to receive cash or other securities, typically at a discount. Treasury officials expect to rely primarily on restructurings because the overall financial condition of the remaining institutions makes full repayment unlikely.

Contents

Letter		1
	Background	3
	CPP Largely Has Wound Down and Program Income Surpassed Original Investments	4
	Most of the Remaining CPP Institutions Continue to Exhibit Signs of Financial Weakness	8
	Treasury Expects Most Remaining Institutions to Exit through Restructurings	10
	Agency Comments	13
Appendix I	GAO Contact and Staff Acknowledgments	16
Figures		
	Figure 1: Status of the Capital Purchase Program, as of February 29, 2016	5
	Figure 2: Status of Institutions That Received Capital Purchase Program Investments, as of February 29, 2016	7
	Figure 3: Remaining Capital Purchase Program Investments, as of February 29, 2016	8
	Figure 4: Exits from the Capital Purchase Program, as of December 31, 2015	12

Abbreviations

CDCI	Community Development Capital Initiative
CPP	Capital Purchase Program
EESA	Emergency Economic Stabilization Act of 2008
FDIC	Federal Deposit Insurance Corporation
SBLF	Small Business Lending Fund
TARP	Troubled Asset Relief Program
Treasury	Department of the Treasury

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May 6, 2016

Congressional Committees

From October 2008 through December 2009, the Department of the Treasury (Treasury) invested almost \$205 billion in 707 financial institutions as part of federal efforts to help stabilize U.S. financial markets. The investments were made through the Capital Purchase Program (CPP), the first and largest initiative under the Troubled Asset Relief Program (TARP).¹ The Emergency Economic Stabilization Act of 2008 (EESA) gave Treasury the authority to buy or guarantee up to \$700 billion, later reduced to \$475 billion, of the “troubled assets” that were believed to be at the heart of the financial crisis, including mortgages, mortgage-backed securities, and certain other financial instruments.² Under this authority, in October 2008 Treasury created CPP to provide capital to viable financial institutions by purchasing preferred shares and subordinated debt. In return for its investments, Treasury received dividend or interest payments and warrants.³ The program was closed to new investments on December 31, 2009. Since then, Treasury has continued to oversee and divest its CPP investments, collect dividend and interest payments, and sell warrants.

EESA includes a provision that GAO report at least every 60 days on TARP activities and performance.⁴ We have been monitoring, analyzing, and providing updates on TARP programs, including CPP, in response to

¹The Emergency Economic Stabilization Act of 2008 (EESA), Pub. L. No. 110-343, 122 Stat. 3765 (codified as amended at 12 U.S.C. §§ 5201-5261), established the Office of Financial Stability within Treasury and provided Treasury with broad authority to purchase and guarantee certain types of troubled assets to stabilize the financial markets.

²§§ 3(9), 101, and 115(a), 122 Stat. at 3767 and 3780 (codified as amended at 12 U.S.C. §§ 5202(9), 5211, and 5225(a)). The Dodd-Frank Wall Street Reform and Consumer Protection Act reduced Treasury’s authority to purchase or insure troubled assets to a maximum of \$475 billion. Pub. L. No. 111-203, § 1302, 124 Stat. 1376, 2133 (2010) (codified as amended at 12 U.S.C. § 5225(a)).

³A warrant is an option to buy shares of common stock or preferred stock at a predetermined price on or before a specified date.

⁴§ 116(a), 122 Stat. at 3783-85 (codified at 12 U.S.C. § 5226(a)).

this provision.⁵ This report examines (1) the status of CPP, including repayments and other proceeds, as well as investments outstanding; (2) the financial condition of institutions remaining in CPP; and (3) Treasury's strategy for winding down the program.

To assess the status of CPP, we analyzed data from Treasury. In particular, we used Treasury's February 2016 Monthly Report to Congress to determine the dollar amounts of outstanding CPP investments, and the number and geographical distribution of remaining participants as of February 29, 2016. We used data from Treasury's February 2016 Cumulative Dividends, Interest and Distributions report to determine the amount of dividends paid and the number of institutions that had made full repayments. We determined that the financial information used in this report is sufficiently reliable to assess the status of CPP based on the results of our audits of the financial statements for TARP (from fiscal years 2009 through 2015). As part of the financial statement audits, we tested Treasury's internal controls over financial reporting. To assess the financial condition of the 16 institutions that remained in CPP as of February 29, 2016, we analyzed financial and regulatory data from SNL Financial, which provides comprehensive regulatory financial data on financial institutions. For example, we compared various indicators of financial health—such as return on average assets and reserves to nonperforming loans. We assessed the reliability of SNL Financial data for previous studies by testing required data elements, reviewing existing information about the data and the system that produced them, and interviewing SNL officials. We determined that the financial information we used is sufficiently reliable for this report. We also leveraged our past reporting on TARP to inform our assessments of the financial institutions. To determine Treasury's strategy to exit CPP, we interviewed Treasury officials knowledgeable about the agency's strategy.

⁵See GAO, *Troubled Asset Relief Program: Opportunities Exist to Apply Lessons Learned from the Capital Purchase Program to Similarly Designed Programs and to Improve the Repayment Process*, [GAO-11-47](#) (Washington, D.C.: Oct. 4, 2010); *Capital Purchase Program: Revenues Have Exceeded Investments, but Concerns about Outstanding Investments Remain*, [GAO-12-301](#) (Washington, D.C.: Mar. 8, 2012); *Troubled Asset Relief Program: Treasury's Use of Auctions to Exit the Capital Purchase Program*, [GAO-13-630](#) (Washington, D.C.: July 8, 2013); *Troubled Asset Relief Program: Status of the Wind Down of the Capital Purchase Program*, [GAO-14-388](#) (Washington, D.C.: Apr. 7, 2014); *Troubled Asset Relief Program: Winding Down the Capital Purchase Program*, [GAO-15-367R](#) (Washington, D.C.: Mar. 6, 2015); and *Troubled Asset Relief Program: Status of Remaining Investment Programs*, [GAO-16-91R](#) (Washington, D.C.: Nov. 3, 2015).

We conducted this performance audit from January 2016 to May 2016 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

CPP was created to help stabilize the financial markets and banking system by providing capital to qualifying regulated financial institutions through the purchase of preferred shares and subordinated debt.⁶ Rather than purchasing troubled mortgage-backed securities and whole loans, as initially envisioned under TARP, Treasury used CPP investments to strengthen the capital levels of financial institutions. Treasury determined that strengthening capital levels was the more effective mechanism to help stabilize financial markets, encourage interbank lending, and increase confidence in the financial system. On October 14, 2008, Treasury allocated \$250 billion of the original \$700 billion, later reduced to \$475 billion, in overall TARP funds for CPP. In March 2009, the allocation was reduced to reflect lower estimated funding needs, as evidenced by actual participation rates. On December 31, 2009, the program was closed to new investments.

Under CPP, qualified financial institutions were eligible to receive an investment of 1–3 percent of their risk-weighted assets, up to \$25 billion.⁷ In exchange for the investment, Treasury generally received preferred shares that would pay dividends.⁸ As of the end of 2014, all the

⁶For CPP, qualifying financial institutions generally include stand-alone U.S.-controlled banks and savings associations, as well as bank holding companies and savings and loan holding companies.

⁷Risk-weighted assets are all assets and off-balance-sheet items held by an institution, weighted for risk according to the capital standards of the federal banking regulators. In May 2009, Treasury increased the maximum amount of CPP funding that small financial institutions (qualifying financial institutions with total assets of less than \$500 million) could receive from 3 to 5 percent of risk-weighted assets.

⁸For S corporations, a federal business type that provides certain tax and other benefits, Treasury received subordinated debt rather than preferred shares in order to preserve the special tax status of these institutions. The Internal Revenue Code prohibits S corporations from having more than one class of stock outstanding. Interest rates for this debt are 7.7 percent for the first 5 years and 13.8 percent for the remaining years.

institutions with outstanding preferred share investments were required to pay dividends at a rate of 9 percent, rather than the 5 percent rate in place for the previous 5 years. EESA requires that Treasury also receive warrants to purchase shares of common or preferred stock or a senior debt instrument to further protect taxpayers and help ensure returns on the investments. Institutions are allowed to repay CPP investments with the approval of their primary federal bank regulator, and after repayment, institutions are permitted to repurchase warrants on common stock from Treasury.

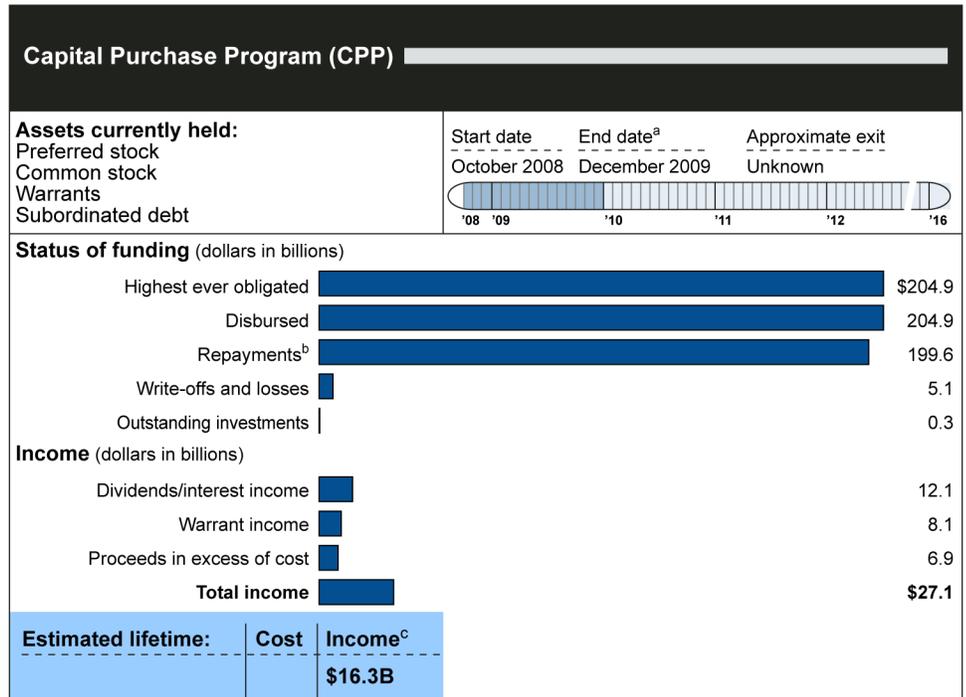
CPP Largely Has Wound Down and Program Income Surpassed Original Investments

Treasury largely has wound down its CPP investments, and as of February 29, 2016, had received \$226.7 billion in repayments and income from its CPP investments, exceeding the amount originally disbursed by almost \$22 billion. The repayments and income amounts included almost \$200 billion in repayments and sales of original CPP investments, as well as about \$12 billion in dividends and interest, almost \$7 billion in proceeds in excess of costs, and about \$8 billion from the sale of warrants (see fig.1). After accounting for write-offs and realized losses from sales totaling about \$5 billion, CPP had almost \$0.3 billion in outstanding investments as of February 29, 2016.⁹ Treasury's most recent estimate of lifetime income for CPP (as of Nov. 30, 2015) was about \$16 billion.¹⁰

⁹Write-offs and realized losses include losses sustained from investments in the 32 institutions that have gone into bankruptcy or receivership and any losses sustained when Treasury sold its investments in CPP institutions.

¹⁰Treasury, in conjunction with the Office of Management and Budget, estimates lifetime costs (or income) for CPP four times a year, using the aggregate value of investments at market prices. Estimated lifetime cost represents Treasury's best estimate of what the program ultimately will cost the taxpayer. Treasury's methodology for estimating lifetime costs includes a discount rate that reflects market risk for future cash flows. Treasury's estimate of lifetime income for CPP is consistent with an estimate by the Congressional Budget Office.

Figure 1: Status of the Capital Purchase Program, as of February 29, 2016



Source: GAO analysis of Treasury data. | GAO-16-524

^aThe end date is the date on which the program stopped acquiring new assets and no longer received funding.

^bThe total amount of repayments includes approximately \$363 million from institutions that transferred to the Community Development Capital Initiative and \$2.2 billion from institutions that transferred to the Small Business Lending Fund.

^cAmount is as of November 30, 2015.

As of February 29, 2016, 16 of the 707 institutions that originally participated in CPP remained in the program (see fig. 2).¹¹ Of the 691 institutions that had exited the program, 261 repurchased their preferred

¹¹The information on CPP in this report is as of February 29, 2016, unless otherwise noted. As of April 19, 2016, 14 institutions remained in CPP, as 2 institutions recently exited the program—US Metro Bank of Garden Grove, California, on March 23, 2016 and HCSB Financial Corporation of Loris, South Carolina, on April 11, 2016.

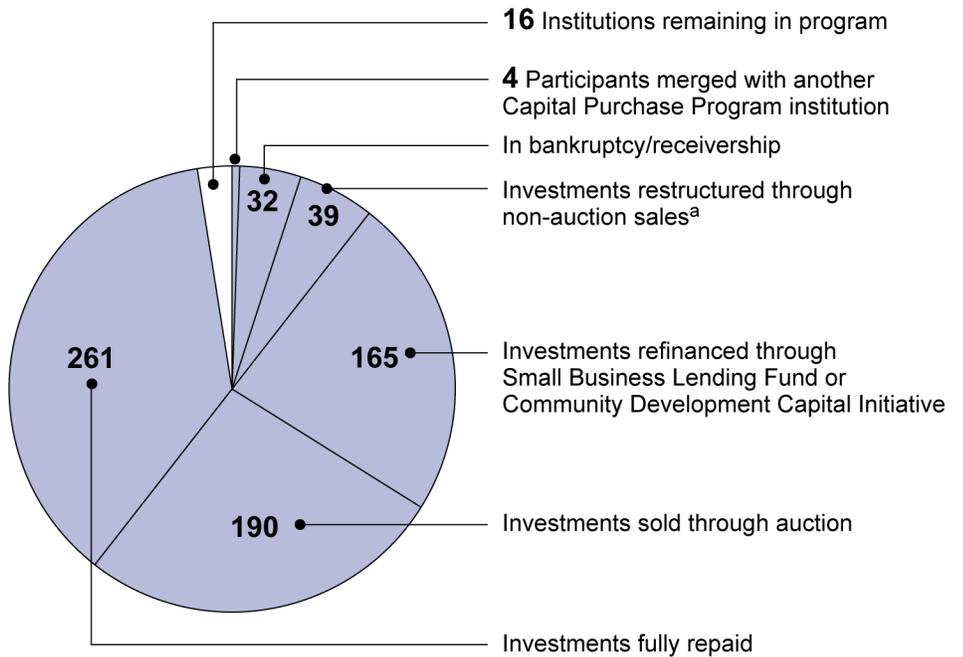
shares or subordinated debentures in full.¹² Another 165 institutions refinanced their shares through other federal programs, 28 through the Community Development Capital Initiative (CDCI) and 137 through the Small Business Lending Fund (SBLF), another Treasury fund that was separate from TARP.¹³ An additional 190 institutions had their investments sold through auction, 39 institutions had their investments restructured through non-auction sales, and 32 institutions went into bankruptcy or receivership.¹⁴ The remaining 4 merged with other institutions.

¹²Preferred shares give the stockholder priority dividend and liquidation claims over common stockholders. Subordinated debentures are a form of debt security that rank below other senior claims on assets but have priority over all preferred and common shareholders.

¹³Twenty-eight of the institutions refinanced investments through CDCI, a TARP program that provides capital to Community Development Financial Institutions that have a federal depository institution supervisor. CDCI is structured like CPP, but it provides more favorable capital terms, and also covers credit unions. The other 137 institutions refinanced their shares through SBLF. SBLF, which closed in 2011, was a \$30 billion program that provided capital to qualified community banks and community development loan funds with assets of \$10 billion or less.

¹⁴When investments are restructured, Treasury receives cash or other securities, which generally can be sold more easily than preferred stock, but Treasury's investments are sometimes sold at a discount.

Figure 2: Status of Institutions That Received Capital Purchase Program Investments, as of February 29, 2016



Source: GAO analysis of Treasury data. | GAO-16-524

^aWhen investments are restructured, Treasury receives cash or other securities that generally can be sold more easily than preferred stock, but Treasury's investments are sometimes sold at a discount.

As shown in figure 3, as of February 29, 2016, the remaining \$257.1 million in outstanding CPP investments was concentrated in half of the remaining 16 institutions. The institutions with the eight highest amounts of outstanding CPP investments accounted for 88 percent (\$225.5 million) of the outstanding investments, while one institution accounted for 49 percent (\$124.97 million). The remaining \$31.6 million (12 percent) was spread among the other eight institutions.

Figure 3: Remaining Capital Purchase Program Investments, as of February 29, 2016



Source: GAO analysis of Treasury data. | GAO-16-524

Most of the Remaining CPP Institutions Continue to Exhibit Signs of Financial Weakness

Our analysis of financial condition metrics over the past 4 years indicates that among the 16 institutions remaining in CPP as of February 29, 2016, several have continued to face challenges.¹⁵ Although the median return on average assets—a key indicator of a company’s profitability—was higher in the fourth quarter of 2015 than in 2011, 9 of the 16 institutions had negative returns in 2015.¹⁶ Furthermore, 6 of the 16 institutions had a lower return on assets in 2015 than they did at the end of 2011. The remaining institutions also had varying levels of reserves for covering losses, as measured by the ratio of reserves to nonperforming loans.¹⁷ For example, 6 of 15 institutions had lower levels of reserves for covering

¹⁵We analyzed financial and regulatory data from SNL Financial. All financial information in the analysis generally reflects quarterly regulatory filings as of December 31, 2015.

¹⁶The median return on average assets measure shows how profitable a company is relative to its total assets and how efficiently management uses its assets to generate earnings.

¹⁷Generally, a higher ratio of reserves to nonperforming loans demonstrates an institution’s ability to cover losses from nonperforming loans.

losses in 2015 compared to 2011, while 9 institutions had higher levels.¹⁸ Treasury officials stated that the remaining CPP institutions generally had weaker capital levels and worse asset quality relative to institutions that had exited the program. They noted that this situation was a function of the lifecycle of the program, because stronger institutions had greater access to new capital and were able to exit, while the weaker institutions had been unable to raise the capital needed to exit the program.

Many of the remaining CPP institutions were on the “problem bank list” of the Federal Deposit Insurance Corporation (FDIC) and most have been delinquent on their dividend payments for several years. The problem bank list contains banks with demonstrated financial, operational, or managerial weaknesses that threaten their continued financial viability; the number of problem banks is publicly reported on a quarterly basis. Specifically, as of December 31, 2015, 11 of the then 17 remaining CPP institutions (65 percent) were on FDIC’s problem bank list.¹⁹ The percentage of remaining CPP institutions on the problem bank list is higher than the number we reported for the previous 2 years: 47 of 83 (57 percent) in 2013 and 20 of 34 (59 percent) in 2014.²⁰

Of the 16 CPP institutions remaining as of February 29, 2016, 1 of the 14 required to pay dividends made the most recent scheduled dividend or interest payment.²¹ The 13 institutions that are delinquent have missed an average of 23 quarterly dividend payments, with the fewest missed

¹⁸Our analysis of reserves to nonperforming assets included 15 of the 16 remaining institutions because one bank produced “not meaningful” results as defined by SNL Financial. The calculated ratio was above SNL Financial’s “meaningful” threshold of 1,000. Similar to prior TARP reports, “not meaningful” results were not included in the analysis.

¹⁹FDIC’s problem bank list does not include bank holding companies. Bank holding company recipients of CPP funds were accounted for if one or more of their subsidiary depositories were designated as problem banks.

²⁰See [GAO-15-367R](#).

²¹This excludes those institutions that made payments towards a past-due amount or payments made by institutions that exited the program as of February 29, 2016. CPP dividend and interest payments are due on February 15, May 15, August 15, and November 15 of each year, or on the first business day after those dates. The reporting period ends on the last day of the calendar month in which the dividend or interest payment is due. Therefore, payment data as of February 29, 2016, represent the most recently available information for this report. Two of the remaining CPP institutions are not required to pay dividends because Treasury exchanged its preferred shares in those institutions for common shares.

payments at 16 and the most missed payments at 29.²² Institutions can elect whether to pay dividends and may choose not to pay for a variety of reasons, including decisions they or their federal or state regulators make to conserve cash and capital. However, investors may view an institution's ability to pay dividends as an indicator of its financial strength and may see failure to pay as a sign of financial weakness. Treasury officials told us that they regularly monitor and have direct and substantive conversations with the remaining 16 institutions, including discussions about their plans to exit the program.

Treasury Expects Most Remaining Institutions to Exit through Restructurings

Treasury officials expect most of the remaining CPP institutions to exit through restructurings but do not have a specific end date for exiting all their CPP investments and winding down the CPP program. EESA does not require Treasury to set a specific date on which the program will expire. Although Treasury has not changed its exit strategy, which consists of repayments, restructurings, and auctions, the extent to which each approach has been used has shifted over time.²³

- **Repayments.** Repayments allow financial institutions, with the approval of their regulators, to redeem their preferred shares in full. Institutions have the contractual right to redeem their shares at any time. As of February 29, 2016, 261 institutions had exited CPP through repayments. Institutions must demonstrate that they are financially strong enough to repay the CPP investments to receive regulatory approval to proceed with a repayment exit.
- **Restructurings.** Restructurings allow troubled financial institutions to negotiate new terms or discounted redemptions for their investments. Raising new capital from outside investors (or a merger) is a prerequisite for a restructuring. With this option, Treasury receives cash or other securities that generally can be sold more easily than preferred stock, but the restructured investments are sometimes sold at a discount to par value. According to Treasury officials, Treasury facilitated restructurings as an exit from CPP in those cases in which

²²Under CPP terms, institutions pay cumulative dividends on their preferred shares—except for banks that are not subsidiaries of holding companies, which pay noncumulative dividends. Some other types of institutions, such as S corporations, received their CPP investments in the form of subordinated debt and pay interest rather than dividends.

²³Treasury announced its CPP exit strategy in May 2012. See [GAO-13-630](#), [GAO-14-388](#), and [GAO-15-367R](#).

new capital investment and redemption of the CPP investment by the institutions otherwise was not possible. Treasury officials said that they approved the restructurings only if the terms represented a fair and equitable financial outcome for taxpayers. Treasury completed 39 such restructurings through February 29, 2016.²⁴

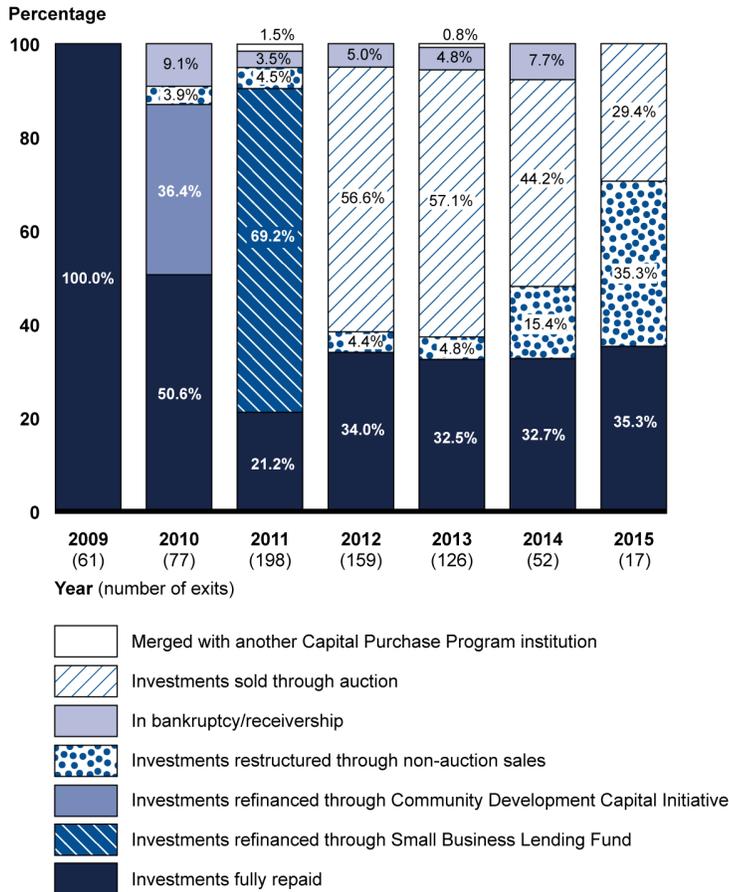
- **Auctions.** Treasury conducted the first auction of CPP investments in March 2012, and has continued to use this strategy to sell its investments. As of February 29, 2016, Treasury had conducted a total of 28 auctions of stock from 190 CPP institutions. Through these transactions, Treasury received about \$3 billion in proceeds, which was about 80 percent of the investment's face amount. As we previously reported, Treasury has sold investments individually to date, but noted that combining smaller investments—into pooled auctions—remained an option.²⁵ Whether Treasury sells stock individually or in pools, the outcome of this option will depend largely on investor demand for these securities and the quality of the underlying financial institutions.

The method by which institutions have exited the program has varied over time. As shown in figure 4, from 2009 through 2011, the majority of institutions exiting CPP did so through repayment or refinancing their shares through CDCI and SBLF. From 2012 to 2014, auctions were the predominant exit strategy. During that same period, restructurings also increased. For example, in 2012, 4 percent of exits (7 of 159) were restructurings. In 2014, 15 percent (8 of 52) used restructuring as an exit strategy. In 2015, restructurings remained a common strategy, representing 35 percent (6 of 17) of exits, while auctions dropped from 44 percent (23 of 52) in 2014 to 29 percent (5 of 17) in 2015.

²⁴This number does not include two additional investments that were restructured when Treasury exchanged its preferred shares for common shares because these institutions remained in CPP.

²⁵Unlike Treasury's auctions of individual CPP preferred stock investments, in which multiple bidders could receive an allocation of the preferred stock at a single clearing price, Treasury's pooled auctions likely would allow the single highest bidder to purchase all of the securities included in the pool. See [GAO-13-630](#).

Figure 4: Exits from the Capital Purchase Program, as of December 31, 2015



Source: GAO analysis of Treasury data. | GAO-16-524

Treasury officials told us they expected restructurings to be the primary exit strategy in the future, but as noted earlier, auctions remain a possible exit strategy. Treasury expects to rely on restructurings and auctions because the overall financial condition of the remaining institutions makes full repayment unlikely. At this time, Treasury does not have any plans to fully write off any investments. Treasury officials anticipate that the current strategy to restructure or auction the remaining investments will result in a better return for taxpayers. According to officials, any savings achieved by writing off the remaining CPP assets and eliminating costs associated with maintaining CPP would be limited, because much of the TARP infrastructure will remain intact for several years to manage other TARP programs. Treasury officials also noted that writing off the

remaining assets could be seen as diminishing the equitable treatment of institutions across the program. That is, writing off the remaining assets, (and thereby not requiring repayment from the remaining institutions) would be unfair to the institutions that already had repaid their investment and exited the program.

Agency Comments

We provided Treasury with a draft copy of this report for review and comment. Treasury provided technical comments that we have incorporated as appropriate.

We are sending copies of this report to the appropriate congressional committees. This report will be available at no charge on our website at <http://www.gao.gov>.

If you or your staff have any questions about this report, please contact me at (202) 512-8678 or garciadiazd@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report.



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Director, Financial Markets and Community Investment

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Appendix I: GAO Contact and Staff Acknowledgments

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Staff Acknowledgments

In addition to the contact named above, Karen Tremba (Assistant Director), Anne Akin (Analyst-in-Charge), Bethany Benitez, William R. Chatlos, Lynda Downing, Risto Laboski, Marc Molino, Barbara Roesmann, Christopher Ross, and Max Sawicky have made significant contributions to this report.

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