BB&T

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September 24, 2008

Congresswoman Virginia Foxx
430 Cannon House Office Building
Washington, DC 20515

Dear Congresswoman Foxx:

After reading my letter from yesterday, several senators and congressman have asked for an alternative to the Paulson/Bernanke rescue package. Attached is an alternative proposal.

In evaluating this proposal it is important to remember the context of the need for the rescue. It is critical to understand the disease, to understand the appropriate cure; treating the patient for mumps when he has chicken pox will not work. Also treating the symptom (financial market dislocation) instead of the disease (housing price deflation) will not work. In this regard, it is essential to recognize that government policies were the primary cause of the current real estate/financial industry problems. These government policies include: (1.) The politicalization and leveraging of Freddie Mac and Fannie Mae (which could not have happened without government guarantees), (2.) Affordable Housing and (3.) The Federal Reserve (government agency) mismanaging interest rates. While it is true that individual financial institutions also contributed to the problems with irrational investment decisions, markets did not fail, government policy failed.

The real problem is in the housing market. The housing market problems have impacted the financial industry, because financial institutions provide significant financing for housing. The cure needs to be in the housing market, not the financial system.

Your serious consideration of this proposal would be appreciated.

Sincerely,

John

John Allison

Alternative to Proposed Paulson/Bernanke Rescue Package

1. Implement a significant tax credit for the purchase of residential properties. This should be designed to encourage the immediate acquisition of homes. It would be broad based (not just first-time home buyers). It must be short-lived (for example June 30, 2009). The housing incentives need to be carefully designed. You probably should work with the home builders association in this regard. The goal is to clear the excess housing inventory.

   The reason this will work is because housing prices nationally need to fall approximately 10% (this varies significantly by market). This 10% fall is important, because the combination of personal incomes and rental rates will make housing economically advantaged over rental property at these prices. Ironically, the goal is to actually stimulate a 10% decline in housing (with the taxpayers absorbing part of the decline through the tax credit), but at the same time, to create a practical floor on house prices. If the market knew with certainty that house prices were only going to fall 10% more, it would clear rapidly.

   This is a "no lose" concept in the sense that a tax cut in a deflationary/recessionary environment targeted at the problem in the economy i.e., home values has to be positive. The stabilization of house prices (even at a 10% lower level) will materially increase consumer confidence and start the economy moving again.

2. The SEC should be directed to immediately issue an opinion to all accounting firms. The purpose of the opinion would be to properly define Fair Value accounting. Under the FASB rules it is clearly stated that if there is no functioning market assets should not be marked to market. Because of the combination of the SEC pressure and Sarbanes Oxley, all accounting firms are extremely conservatively and effectively misinterpreting, the FASB requirements and forcing writedowns when the market is clearly not functioning. The memo from the SEC should be threatening, in the sense of making it clear to the accounting firms that forcing a mark to market when there is not a functioning market would be a serious error on the part of the accounting firm. Bonds should be "marked to hold," which reflects their real economic value (i.e., based on rationally projected cash flows), not the panic prices today. This would substantially increase capital available to financial institutions. It would also raise bond values creating liquidity, as buyers will be able to make decisions based on economic risk not arbitrary accounting risk.

3. Reduce capital requirements for Freddie Mac and Fannie Mae mortgage backed bonds held by banks from 20% to 5%. Banks hold many Freddie Mac and Fannie Mae mortgage backed bonds. It is logical to reduce the capital holding requirement for Freddie Mac and Fannie Mae mortgage backed bonds, (not preferred stock, sub debt, etc) because the U.S. Government has guaranteed, for all practical purposes, these obligations. This regulatory decision would increase the willingness of banks to buy Freddie Mac and Fannie Mae mortgage backed debt, reducing the rates on this debt. This would also reduce the spreads over Treasury. This combination would

lower mortgage rates and incent house purchases. Banks would have more capital and they could increase lending capacity.

4. If these problems continue, the Fed should aggressively buy Freddie Mac and Fannie Mae mortgage backed securities. This action will lower spreads over Treasury to create gains in the bond portfolio of banks, therefore raising capital in the banking industry.

5. If liquidity problems continue, the Fed should aggressively buy-back 10 Year treasuries. This action would lower interest rates (supply and demand) at least temporarily. As mortgage rates are priced off treasuries, lower 10 year treasuries rates means lower mortgage rates making housing more affordable.

6. The FDIC should act quickly and aggressively to deal with problems in financial institutions. Problem financial institutions tend to distort the cost of capital for other financial institutions, by paying above market CD rates.

7. The SEC should immediately defer for at least 3 years any changes in merger accounting. Confusion on the new merger accounting guidelines is making healthy companies less willing to buy unhealthy companies.

The primary purpose of the rescue package should be to stabilize housing prices at a level which is economically efficient, i.e., based on the personal incomes and rental rates, which will allow the market to clear.

After the crisis, Freddie Mac and Fannie Mae should be broken up and privatized. No government guarantees should be given on any new debt, beginning 2 or 3 years down the road. Canada has no Freddie Mac and Fannie Mae equivalent and has an excellent housing market.

One way to pay for the proposed housing tax cuts, is to begin a few years down the road to systematically phase out tax deductions on home interest payments. This subsidy to homeownership is causing a misallocation of capital in our economic system away from production to consumption. It is also the foundation of real estate bubbles. Again, Canada has no tax subsidy for housing and therefore has a much more stable housing market. Obviously, affordable housing loans should be eliminated

Mr. Paulson and Mr. Bernanke are extremely intelligent people. However, Mr. Paulson's background is in investment banking and Mr. Bernanke is an academic. Neither one were in material decision making positions during the last real estate crisis in the early 1990's.