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**A Federally Funded Restructuring: The Automobile Industry's   
Journey from Worldwide Acclaim to Bankruptcy**

A devastating financial crisis struck the United States - and most of the world - in 2008. The automobile industry, which accounts for a large percentage of the nation’s economic output, was especially affected by the turmoil that followed. The economic crisis, coupled with internal managerial issues and the ever-increasing presence of foreign automobiles in the United States, led to a financial crisis within the domestic automakers. The “Big Three” automakers that include Chrysler, Ford, and General Motors were in financial trouble and faced filing bankruptcy, possibly threatening the jobs and therefore the livelihoods of hundreds of thousands of people. In an effort to prevent the complete collapse of the automobile industry Congress moved to enact the Auto Industry Financing and Restructuring Act, which passed the House of Representatives in December of 2008 but failed to pass the Senate. However, the Emergency Economic Stabilization Act of 2008 (EESA) was passed in an effort to protect good investments that financial institutions still held and help purchase poor assets to relieve the financial burden. The Troubled Asset Relief Program (TARP), established in EESA, included funds for the two car companies that required them: Chrysler and General Motors. Ford took many steps prior to the economic crisis of 2008 – such as securing loans against its blue oval logo – that enabled the company to remain financially viable and avoid the necessity of government funding. The heads of these American automakers appeared before Congress together on two separate occasions, pleading for cash in order to keep their business going. This eventually led to the failed attempt to pass the Auto Industry Financing and Restructuring Act and the decision of then-President Bush to use TARP funds to fund the two failing automakers until they could provide a viability plan and receive more financial support from the government. This ultimately led to the “bailing out” of the two companies by President Obama’s administration. This essay will briefly describe the reason for passing EESA and the path that it carved for supplying the American car companies with taxpayer money. It will also briefly explore the decline of the auto industry in America and the eventual visit of the CEO s of the Big Three to Congress. The actual process of the bailout will be analyzed – drawing substantially from Steven Rattner’s first-hand account in *Overhaul* – as well as the effects of the government intervention. Lastly, the paper will attempt to determine whether the infusion of government funds actually worked and determine whether – if GM or Chrysler went bankrupt again – it would be wise of the government to supply the companies with money once again.

Before one can begin to examine the automobile industry bailout one must consider the history of the automobile industry itself. Many Americans know the common story of how prolific individuals such as Henry Ford were instrumental to the accessibility of automobiles in America. The brands Chrysler, Ford, and General Motors have become a staple in American culture, dating back to the early twentieth century. The recognition of these brands is still widespread but the actual reach of the companies has dwindled since the industry's peak around 1960.

During the 1960s, GM alone accounted for nearly fifty percent of American market share, with Ford ranging from 22 – 26 percent and Chrysler from 12 – 16 percent (Kenworthy, Macaulay, & Rogers, 1996). This was the era when American cars were celebrated as a source of pride and a symbol of status. Foreign competitors virtually had no market share, save a few very small car companies. Slowly but surely, however, American automakers' market share began to steadily decline. Up until the mid-1970s, the Big Three automakers enjoyed a virtually impenetrable market share.

Around the mid-1970s foreign vehicles began to make a much larger scale emergence into the American car market. This was a result of many factors, mostly because of the change in consumer demand. American car companies, especially during the 1960s, prided themselves on their big American muscle cars that came to define them. Smaller vehicles, however, were becoming more prominent. This, combined with rising fuel prices due to the scarcity of fuel, and the instability of the economy in general, caused a decline in their American automobile market share (Kenworthy, Macaulay, & Rogers, 1996).

The market share of Chrysler – which had always been a distant third in the American automakers – took a formidable hit during the 1970s, leaving it in a financially dangerous situation; so much so that the company faced bankruptcy and asked the government for a $1.5 billion loan (Ingrassia, 2010). The federal government acquiesced and supplied the company with its loan, which was paid back early, in 1983. The loan amply allowed the company to rebound, essentially due to the leadership of their then-new CEO Lee Iacocca, who successfully introduced a new automobile design, the minivan. The minivan helped Chrysler return to profitability and escape bankruptcy because of its fresh design and ability to transport many people at once.

Ford and GM were not entirely immune to the financial devastation, however. They were also submerged in red ink, only they were large enough to avoid imminent of bankruptcy. German and Japanese vehicles were the main cause of the financial woes the Big Three faced. While the first half of the 1980s were not kind to the American automakers, Chrysler and Ford were able to claw their way to profitability. Chrysler – with its introduction of the minivan – and Ford with the introduction of its Taurus model, which eventually became the best-selling car in America, displacing the Honda Accord. The Ford Taurus was considered to be a breakthrough in automobile design. These successes by Chrysler and Ford secured the companies’ record-breaking profits and sky-rocketing stocks; Ford's stock price rose 1,500 percent between 1981 and 1987 (Rattner, 2010).

Paul Ingrassia narrated the events that followed the late eighties in his book *Crash Course*. While the American automakers thwarted foreign competition through the late eighties, they found themselves recording record losses with the first two years of the 1990s (Ingrassia, 2010). The American automakers constantly found themselves competing against foreign automakers. During the late eighties and early nineties, GM (and Chrysler and Ford on a lesser scale) focused on integrating more technological advances to reduce costs and usher the companies into the 21st century (Ingrassia, 2010). Most of GM’s efforts, however, were in vain. While the overall quality had improved, many of General Motors’ projects and initiatives turned out to be dead ends, which left the company even further behind its Japanese rivals, who managed to build cars in America more efficiently than the domestic car companies. This led to a GM loss of $4.5 billion in 1991, the highest loss of any corporation at that time.

The next savior for the American automakers – as introduced by Lee Iacocca again – was the Sports Utility Vehicle (SUV). Iacocca bought American Motors in the late eighties primarily because of the Jeep brand which, he believed would appeal to many Americans, who were family-oriented during the week and liked to have adventures come the weekend. To Iacocca, the Jeep satisfied this American personality and he was right; Americans took the bait and fell in love with SUVs, despite their gas guzzling nature. It is important to note that fuel was cheap during the nineties and Americans had no reason to believe it would not remain so. As a result the American automakers were able to turn around their sales.

Once again the American automakers excelled, fulfilling consumer demand. A prime example was Chrysler's rebound from an $800 million loss in 1991 to a record profit of $3.7 billion in 1994 (Ingrassia, 2010). Ford and GM also developed their own SUVs but primarily relied on their trucks to bring themselves into the black. The two domestic rivals had a reason to compete with one another again; whose truck was better? Japanese car companies failed to recognize the growing trend of trucks and SUV s, brushing it off as insignificant. Consequently, the American Big Three enjoyed market dominance and near record profits throughout the 1990s and into the 2000s. GM, confident in the most recent surge of American motor vehicles, announced the 2000 North American Auto Show would be the biggest in history (Ingrassia, 2010). While the “good times” lasted a couple more years, soon the American automotive industry found itself in trouble again.

A savvy businessman today would look at the Big Three's business model and deduce that a car company that is primarily concerned about only trucks and SUV s is destined to run into problems. The American car companies did not have the benefit of hindsight, however. During the years of surging truck and SUV sales gas prices were low and consumers were willing to purchase the larger vehicles and spend a little extra on gas (Kenworthy, Macaulay, & Rogers, 1996). The soaring fuel prices became the Achilles' heel of the American automaker. Consumers immediately switched their demand to smaller, more fuel-efficient vehicles, leaving most American car companies behind Japanese automakers who were patiently waiting to fill the gap. This lack of foresight, coupled with the financially crippling legacy costs and poor management, led to a consistent decline of profit margins.

Since the mid-2000s the American car companies have been playing a game of catch up with Usain Bolt, the Jamaican Gold medalist sprinter, if Bolt represented Japanese automakers. Soaring fuel prices in the United States have decreased the demand for trucks and SUV s; so much so Ford eliminated the once-highly-profitable Expedition in 2005 and switched the production to mid-size and compact cars (Ingrassia, 2010). While all of these factors played a direct role in the final result of Chrysler and GM receiving large sums of money from the federal government, the final straw for these corporations was the financial crisis of 2008.

The financial crisis of 2008 is often regarded as the worst U.S. financial crisis since the Great Depression and had a devastating effect on all sectors of the economy, particularly within the manufacturing realm. Both U.S. political parties were quick to point at the policies of their opponent as the sole cause of the crisis. There are many contributing factors, however, to consider when discussing possible causes of the 2008 financial crisis. While the causes of the crisis are not vital to the examination of the bailout of the automotive industry, the aftershocks are noteworthy.

The Financial Inquiry Commission was created when the Fraud Enforcement and Recovery Act of 2009 became law. The commission was composed of ten members, six of which were chosen by the majority party, Democrats at the time, and four by the minority party, the Republicans. Of the six, three were chosen by the Nancy Pelosi, Speaker of the House, and three by the Senate majority leader. Of the four Republican choices, two were chosen by the House of Representatives minority leader and two by the Senate minority leader.

The Commission, or Financial Crisis Inquiry Commission (FCIC), as it will be referred to from this point forward, was similar to the Pecora Commission which investigated the causes of the Great Depression. Similarly the FCIC's charge was to investigate the causes of the financial crisis of 2008. An important fact to consider is that the FCIC had the ability to subpoena documents and witnesses for testimony. Therefore, the FCIC had a similar authority to that granted in Congressional committees, which often call in individuals to testify about a certain subject or topic. Overall, the FCIC spent more than a year examining the causes of the crisis. It held nineteen days of public hearings, interviewed more than 700 witnesses and reviewed thousands of documents.

The FCIC published their findings in the *Financial Crisis Inquiry Report* (2011). This essay will primarily examine Part V of the report, which compiled a comprehensive list of aftershocks endured by major businesses. The objective of this examination will be to determine some of the causes that pushed Chrysler and GM over the edge into financial oblivion. The section begins, “Panic and uncertainty in the financial system plunged the nation into the longest and deepest recession in generations” (Financial Crisis Inquiry Commission, 2011). This statement is the overarching cause of Chrysler and GM's breaking point. While there were many contributing factors, the primary problem was the deep recession.

In testifying to Congress, Bank of America CEO Brian Moynihan stated, “Over the course of the crisis, we, as an industry, caused a lot of damage. Never has it been clearer how poor business judgments we have made affected Main Street” (Financial Crisis Inquiry Commission, 2011). This statement held much truth. It was estimated that $17 trillion in household wealth disappeared within 21 months and unemployment reached 10.1 percent in October 2009 (Financial Crisis Inquiry Commission, 2011). Additionally, when the panic hit in September 2008, business financing dried up.

Large firms were forced to exhaust their cash balances. Overall, businesses took a serious toll. In 2006, roughly 20,000 American companies filed for bankruptcy protection while that number jumped to nearly 61,000 in 2009 (Financial Crisis Inquiry Commission, 2011). The trend for these businesses would ultimately be that of Chrysler and GM as well. The threat of bankruptcy forced companies to reevaluate their long-term plans and, in most cases, contract rather than expand.

By mid-2007, banks had begun to restrict access to credit even for large and medium size businesses. Because of the restricted access to credit, increased burning of cash reserves, and uncertainty in the economy, corporations laid off workers, cut investments, or both. This was especially true for Chrysler and GM who, without access to new credit, increased the amount of lay-offs, burned through their reserves, and began to sell their assets (Rattner, 2010). All of these factors prevented Chrysler and GM from advancing their respective companies.

The restriction of credit was widespread. A survey of chief financial officers found that 57 percent of U.S. Companies were “somewhat or very affected” by credit constraints, leading to cuts somewhere in their respective companies (Financial Crisis Inquiry Commission, 2011). A paragraph within the report summed up the situation well: “News headlines chronicled the problems: scarce capital forced midsize firms to pare back investments and shutter offices, while industrial companies including Caterpillar, Corning, and John Deere; pharmaceutical companies such as Merck and Wyeth; and tech companies alike laid off employees as the recession took hold” (Financial Crisis Inquiry Commission, 2011, p. 395). While Detroit and the automotive industry was not explicitly mentioned in the FCIC's report, their situation epitomized that of many large companies nationwide.

Another cause of the automobile industry crisis was that there was a miniature bubble that occurred for a brief period in 2006 (Rattner, 2010). At one point during 2006 buyers could borrow more than 100 percent of a new vehicle. Loans were extremely easy to attain and ninety percent of consumers financed their vehicles. This caused U.S. Vehicle sales to stay around seventeen million a year until gas prices began to go up (Rattner, 2010). Also, vehicles began to last longer, which tightened the amount of new car purchases. All of these factors forced the CEO s of the Big Three automobile companies to fly to Washington to plead for cash to tide them over until the economy recovered.

Many people remember this scenario: the CEO s of the three major American car companies and the CEO of the UAW testified before Congress, expressing their dire need of funds to continue their day-to-day operations. People also remember the dismal atmosphere of the hearings that occurred on Capitol Hill. The three CEO s were anything but humble and often failed to admit their own shortcomings.

The CEO s appeared before Congress – both the House Financial Services Committee and the Senate Banking Committee. More specifically General Motors CEO Rick Wagoner , Chrysler CEO Robert Nardelli, Ford CEO Alan Mulally, and United Autoworkers' (UAW) leader Ron Gettelfinger showed up in their multi-thousand dollar suits (some pin striped) and testified before the House Financial Services Committee on November 18, 2008. Congress' reception was anything but warm. Immediately the CEO s faced scrutiny because of their chosen method of travel: private jets, three of them. Ron Gettelfinger – head of the UAW – flew commercially however. Representative Gary Ackerman (D – NY) stated, “It's almost like seeing a guy show up at a soup kitchen in a high hat and tuxedo” (Wutkowski, 2008). This statement accurately assessed the situation; the CEOs, who were present to plead a case for a loan, made the trip one of the most expensive manners of travel possible. The actual costs of using the private jets would not alone push the companies off the financial cliff, but was in poor taste. This lack of principle started the first hearing on a sour note. Also, the timing was less-than-ideal since Congress had just bailed out the banks and received much criticism from the public.

The CEOs were also grilled about their personal paychecks. Ford CEO Alan Mulally, the highest paid CEO of the three, was asked whether he thought his annual salary of $22 million – as recorded for 2007 – should be reduced. Ford was considered the healthiest of the three automotive companies, and presented only in attempt to help their competitors stay in business; since Chrysler and GM's demise would likely be Ford's as well. Despite Ford's fortunate state, it was not prudent for him to respond, “I think I'm OK where I am” (Wutkowski, 2008). Many Congressional leaders were taken aback by the executives' lack of personal sacrifice. This point was highlighted when there were asked by Representative Brad Sherman (D-CA) if they would be willing to sell their private jets and fly back to Detroit on a commercial flight. After silence Sherman stated, “Let the records show no hands went up” (Wutkowski, 2008).

Both Ford CEO Mulally and Chrysler CEO Nardelli blamed their current dismal state on the poor economy and a radical decrease in overall vehicle sales. GM's CEO made similar claims and stressed that all of their problems were out of the company's control (which was a false statement) stating in front of the Senate Banking Committee:

“Mr. Chairman, I do not agree with those who say we are not doing enough to position GM for success. What exposes us to failure now is not our product lineup, is not our business plan, is not our employees and their willingness to work hard. It is not our long-term strategy. What exposes us to failure now is the global financial crisis, which has severely restricted credit availability and reduced industry sales to the lowest per-capita level since World War II” (Rattner, 2010, p. 28).

GM had many other failures besides the financial crisis, such as its lack of foresight and dependence on SUV s and trucks, as well as other shortcomings that will be addressed in depth. A common theme among the executives was that they did not take responsibility for the current state of their company, blaming it instead on uncontrollable circumstances. Most importantly, the executives proved to be inept at effectively presenting a detailed case as to why they deserved and needed their loan. Their combined requested loan was for $25 billion, no small amount of money, especially when compared to the funds already received by some of the financial institutions. They asked that Congress open up funds from the Troubled Assets Relief Program (TARP) and direct the Treasury to provide $25 billion in emergency bridge loans (Rattner, 2010). Despite the large amount being requested, the companies did not have a well-thought out proposal of the specifics; they did not even expand on how the loan would be divided between the companies. If the executives would have been a group of entrepreneurs asking for a loan for a new business with a vague proposal, they would have been sent packing. Similarly, Congress – mostly Democratic leaders – told the CEO s, “If you want the money, show us how you'll restructure to stay viable” (“Ford Exec,” 2008). The CEO s of the Big Three would have to make a return trip with better reasoning.

On December 3, 2008 the American automotive executives made their return trip to Capitol Hill to testify before the Senate Banking Committee (the House Financial Services Committee hearing would be later that week). This time around, however, they arrived (still clothed in their thousand dollar suits) in hybrid cars instead of private jets and had a more detailed proposal. The request was for $34 billion this time compared to the $25 billion that was initially requested in November (“Congress Eyes Big Three,” 2008). Therefore, it can be deduced that once the automobile companies were compelled to evaluate their viability, they discovered their financial predicament was worse than originally thought. Each company submitted its own viability plan – this time with amounts for each company – which was reviewed by Congressional leaders.

During this visit, Chrysler and GM informed Congress that they required an immediate infusion of federal funds in order to survive past New Year's (“Congress Eyes Big Three,” 2008). While some initially thought the failing of Chrysler and GM would lead to Ford picking up the slack in production and sales, they were mistaken. Although the American automakers were competitors, they essentially required the existence of each other because they used many of the same suppliers. If one company failed it could have caused suppliers to go bankrupt, leaving the remaining car companies without the necessary parts to build their product. Because of this, Ford did not request any immediate funds but asked for a $9 billion line of credit to hold them over *if* one of their competitors went under (“Congress Eyes Big Three,” 2008). Chrysler, however, requested $7 billion by the end of 2008 to keep their day-to-day operations going. GM requested an immediate $4 billion as the first part of a $12 billion loan, plus a $6 billion line of credit in case the economic conditions worsened (“Congress Eyes Big Three,” 2008). The automakers often mentioned the possibility of massive job loss and further plant closures. Some truth emerged from the second visit when Mark Zandi of Moody's Economy.com predicted that the automakers would not need $34 billion but $75 – $125 billion in the next two years (Rattner, 2010). The prediction was eerily prescient.

Congress considered the viability plans of each company and called a special lame-duck session which would focus solely on the aid of the automotive industry. The Auto Industry Financing and Restructuring Act, H.R. 7321, was introduced and passed in the House of Representatives on December 10, 2008 by a 237-170 vote. The bill died, however, in the Senate leaving the rescue of the automobile industry to the executive branch. Under usual circumstances a bill that died in either house would not see its purpose fulfilled. However, because of the severe condition of the automotive industry the President and the Treasury Secretary thought it appropriate to use their executive power to aid the car companies.

When Congress failed to enact the Auto Industry Financing and Restructuring Act, the executive branch had to take action. Driven by the fact that he did not want to have the closure of two iconic companies during his last months, President Bush confirmed the Treasury's plan to establish the Automotive Industry Financing Program (AIFP) through TARP (OMB, 2012). President Bush agreed upon the terms that the Treasury laid out for Chrysler and GM - who required the infusion of cash. Steven Rattner, one of President Obama's appointees for the automotive industry assignment, helped explain the complex process of how the Obama administration took up the challenge of turning around the automobile industry laid out in his inside account, *Overhaul* (2010).

The Emergency Economic Stabilization Act of 2008 (EESA), made the “bail out” of the automotive industry possible. EESA was passed on October 3, 2008 in response to the financial crisis that had resulted in the abrupt shutdown of Lehman Brothers and the lack of financial stability in various other large banks in the United States. The act enabled the U.S. Treasury to purchase troubled assets in order to bolster the troubled financial institutions. Specifically the Secretary of the Treasury was given immediate authority of $350 billion to be used to purchase troubled assets of financial companies (H.R. 1424, 2008). The second installment of $350 billion permitted by EESA – a total of $700 billion for the program – would be granted upon a request to Congress (H.R. 1424, 2008). A large reason that many of these financial institutions had an abrupt shock was because of the imploding of the housing market bubble. Furthermore, the act effectively authorized the Secretary of Treasury to designate financial institutions as financial agents of the federal government and establish vehicles to purchase and sell toxic assets and issue obligations. It also directed the Secretary to prevent unjust enrichment of participating financial institutions including and sale of any troubled asset (with certain exceptions) to the Secretary at a price higher than the price which it was originally purchased (H.R. 1424, 2008).

Many Americans found it odd that a Republican president began the initiative of an automobile industry bailout. President Bush, however, responded to a question about the automotive industry at the American Enterprise Institute, a conservative think-tank: “under ordinary circumstances failed entities, failing entities, should be allowed to fail. I have concluded these are not ordinary circumstances” (Rattner, p. 41, 2010). They, indeed, were not ordinary circumstances. GM was the second largest industrial company, only to General Electric, and it was widely accepted that the failure of the company could have done much to further diminish an already fractured economy. Therefore, President Bush announced that the Treasury would bail out two of the American automakers with a combined $17.4 billion of TARP money. This was made possible through the aforementioned EESA which established the Troubled Assets Relief Program (TARP) and permitted the Treasury Secretary to use federal funds to aid failing financial institutions. As previously mentioned, AIFP was created to stretch the jurisdiction of the TARP money to the automotive industry. The money was designed as a loan that incrementally dispersed to automakers based on meeting certain required deadlines (Rattner, 2010). This effectively, and efficiently, allowed for a transition to an Obama White House. A new administration took on one of the greatest challenges the United States had faced in recent history.

To show the magnitude of the operation Rattner (Obama's “car czar”) reported in his book *Overhaul*, “with nearly $100 billion in assets, GM alone was larger than all the U.S. Airlines that had gone bankrupt in the past fifteen years, combined” (Rattner, 2010). On January 15, 2009 the Senate agreed to giving the second installment of $350 billion to the control of the Treasury Secretary through TARP, easing the way for the costs associated with the automotive industry bailout. By mid-January, however, GM missed its first deadline when they failed to satisfy certain reporting requirements of their current financial state. This stalled their second installment of $5.4 billion for five days, until they could gather the necessary information (Rattner, 2010). GM's accounting department's inability to finalize the information needed in time, highlighted a significant problem within the organization.

The end of January brought bad news: January automobile sales were terrible. GM's sales were down 49 percent, Ford down 40 percent, and Chrysler down 55 percent. Also, GM's cash reserve was getting close to the $11 billion minimum it required to operate. Furthermore, Chrysler said it was on track to go below its minimum operating requirement before the end of March (Rattner, 2010).

The next deadline for Chrysler and GM was to provide signed term sheets from their respective stakeholders proving cuts reducing liabilities like debt and legacy health care obligations and lowering operating costs, including labor (Rattner, 2010). Those were the essential components required for the companies' viability plans. Because of this requirement, both companies earnestly begun negotiations with unions, debt holders, suppliers, and dealers but to no avail. The unions wanted shared sacrifice from the lenders, who were relentless in their resolve to regain their lent money. Chrysler’s lenders specifically were unwilling to reduce the $6.9 billion of outstanding debt. All the while, GM attempted to win support of its public bondholders to reduce their public debt. That effort was equally unsuccessful. GM predicted an additional need of $2 billion to get them through March 31. The automotive rescue team (Auto Task Force) at this point predicted the bailout would cost them – therefore the American taxpayer – around $50 billion total.

Bankruptcy was in the back of everyone's mind. As the days went by, members of President Obama's Auto Task Force realized that bankruptcy may be the only viable option of successfully restructuring the companies. There were many setbacks to bankruptcy, however. The main concern was that, because of the product of the company, bankruptcy threatened to destroy the demand for automobiles. Demand would diminish because automobiles were heavily tied to their warranty. For example, if there is a hint that an automotive company might go out of business and not be able to fulfill their warranties, the customer would be extremely cautious about buying their vehicles. The two automakers proved to be less viable in their current state than ever. They were burning through cash and faced substantial amounts of debt. The only way to successfully restructure would be to get the creditors, bondholders and other stakeholders to willingly accept pennies on the dollar for their share. As one might expect no entity is ever overjoyed about receiving less than anticipated.

The viability reports – submitted on February 17, 2009 – did not show any positive signs of financial stability either. In fact, upon submission Chrysler and GM indicated they would need another immediate $14 billion (Rattner, 2010). However, both plans were overly optimistic in their projections, specifically GM. Both companies were required to submit their worst-case scenarios. For GM, a twenty percent market share gain was the worst-scenario. For a company that had consistently lost market share for twenty years, it appeared to be delusional about their own situation. Chrysler, on the other hand, had begun acquisition negotiations with the Italian automaker, Fiat, but could not get an affirmative response that would allow them to include extensive plans of the merger in their viability report. Also, JP Morgan refused to let Chrysler factor in any reduction in their debt. (Chrysler, as the largest lender of Chrysler, spoke for all lenders at this point.)

Simultaneously, during the first couple of months of 2009, automotive suppliers were going out of business and filing for bankruptcy. To combat this problem, the Auto Task Force announced a $5 billion receivables guarantee program for suppliers on March 19, 2009. The Supplier Support Program was well received as it made funds available for automotive suppliers. Senator Carl Levin (D-MI) called the program “good news” and Governor Jennifer Granholm (D-MI) announced, “Today's action will minimize unnecessary job losses” (Rattner, p. 125, 2010). Many automotive suppliers did not take advantage of the program since the money was made very expensive through high interest rates. Because of this, only $413 million of the $5 billion was actually utilized by suppliers. However, financial markets opened just enough to provide debtor-in-possession (DIP) loans, which allowed the suppliers to operate while going through normal Chapter 11[[1]](#footnote-1) bankruptcy proceedings. The automakers were also encouraged by the Auto Task Force to provide loans to their most critical suppliers, when the banks refused. The Treasury quietly funded this initiative (Rattner, 2010), but the program was simply a means to slow down the inevitable. The automakers were still in the straits. Each additional month of funded operation for Chrysler cost the taxpayer $500 million to $1 billion and $2 billion for each month GM was funded (Rattner, 2010). As a result, the American automotive companies decimated a substantial amount of taxpayer money in a few months.

As March 31 (the deadline for deciding the fate of the companies) approached, the Auto Task Force diligently worked to resolve the problem. There were still many questions to be answered about the rescue of the two iconic American companies. (Remember, although Ford requested a $9 billion line of credit they attempted to face their financial problem without direct government entanglement.) At this point the Auto Task Force considered letting Chrysler fail and liquidate. Some argued that while jobs would be lost through the liquidation of Chrysler, the two larger automobile companies would pick up the slack. Others steadfastly argued that the economy would not remain resilient to the slightest shock. Even the liquidation of Chrysler, the smallest of the three, surely would have caused a sizable economic shock. Because of this, opposition argued, Chrysler must be saved. Ultimately, President Obama heard both sides of the argument and made the decision to save Chrysler. He gave Chrysler an additional thirty days and GM an additional sixty to submit their viability plans, from the original date of March 31.

Ultimately, most believed a merger with Fiat to be the only realistic option for Chrysler because of its small size, lack of market demand, and need for new innovative marketable technology. The task force identified GM's main problem as management. The Auto Task Force did something unprecedented to solve the problem of GM's management crisis. GM's CEO Rick Wagoner had many admirable qualities but was viewed as expendable because of his lack of foresight, inability to move the company forward, neglect to take the difficult steps necessary, and repeated denial about GM's dire situation. Therefore, the Auto Task Force took it upon itself to remove Wagoner from his position and replace him with the president of GM, Fritz Henderson. This highlighted a stark difference between the bailout of the auto industry and the bailout of the financial institutions; in the bailout of the automotive industry, the government took an active role in changing the culture of the company, including its leaders. That was not the case for any of the financial institutions, however, some of which received much more money. Meanwhile Chrysler made steps toward a financially sound future.

The good news for Chrysler was that by the time President Obama gave the company thirty days, the Fiat-merger plan had already been outlined. The bad news, however, was that not all parties involved in the plan had agreed to the terms. The party with the most leverage was the lenders which included forty-six banks, hedge funds, and pension funds that had lent Chrysler money as a part of its acquisition by Cerberus in 2007 (Ingrassia, 2010). On top of Chrysler's $6.9 billion owed to the creditors, it had pledged $10 billion to the Voluntary Employee Beneficiary Association (VEBA) which was an independent trust established to pay health care benefits for retirees for each of the automobile companies. Rattner and the CEO of JP Morgan, Jimmy Lee, battled over what could be done about the debt owed. Rattner said that the creditors had the legal right to seize control of the company and liquidate it. That was not an attractive offer, however, because the estimated liquidated value of Chrysler, sold around eighteen cents on the dollar, was worth about $1 billion; far less than the $6.9 billion owed (Rattner, 2010). Consequently, the Auto Task Force had leverage, and they and Jimmy Lee knew it. The conversation subsided for the time while Ron Bloom, a member of the Auto Task Force, approached Fiat.

Bloom's proposal for Fiat included giving VEBA a majority equity in the company (Ingrassia, 2010). Fiat, primarily CEO Sergio Machionne, acquiesced on the conditions that they would attain management control and a majority of the board. The agreement signaled great progress in negotiation but the lenders remained steadfast in their resolve.

Meanwhile Fiat and the UAW agreed on wages and work rules. The union agreed that workers would not get overtime unless they worked forty hours a week. While those conditions may seem like common sense most everywhere else, the union had a strong presence in Detroit; so much so, that automotive companies considered their wage workers as fixed costs, as opposed to variable costs like most industrial companies. Wage workers were fixed costs because the automakers had to essentially pay them their full wages (some 95 percent) whether they worked or not (Rattner, 2010). Overall, the union had to make major concessions that undo decades of what was fought for. However, an argument can be made that their extreme conditions caused many of the problems themselves.

Overall, it was decided in a Fiat-Chrysler alliance that the UAW's VEBA trust would receive fifty-five percent ownership of Chrysler as a substitute for $5 billion of the $10 billion. The remaining $5 billion was paid in cash. Fiat would receive twenty percent ownership in the company – while maintaining management control and majority board control – and an opportunity to increase their ownership to thirty-five percent dependent on deliverance of meaningful contributions of product plans and technology. Fiat did not have to put up any cash in the plan, which showed the desperate state Chrysler was in. Chrysler and the Auto Task Force essentially had no leverage power with Fiat (Ingrassia, 2010).

Rattner returned to his debate with JP Morgan and offered Jimmy Lee $1 billion compensation for the $6.9 billion owed. Not surprisingly Lee rejected the offer but eventually settled on a $2.25 billion payoff. However, in order to avoid bankruptcy, Lee had to convince all other creditors to accept the lesser amount before the deadline. Even after extending the deadline, Lee could not deliver forty-six affirmatives (the number of lenders), therefore the foreseen bankruptcy was imminent (Ingrassia, 2010). On April 30, 2009 Chrysler's attorneys filed a Chapter 11 petition with a federal bankruptcy court in Manhattan, where they listed $39 billion in assets and $55 billion in liabilities (Ingrassia, 2010).

Chrysler's plan, submitted to the bankruptcy court, called for cutting 6,500 more jobs, eight more factories, and twenty-five percent of the company's 3,200 dealers (Ingrassia, 2010). The U.S. Treasury pledged $8 billion to keep Chrysler functioning throughout the process until Fiat could revive the company. To the surprise of many bankruptcy experts, Chrysler went through bankruptcy court in forty-two days, a lightning fast speed.

General Motors took a different path to bankruptcy. There was never a question that GM was “too big to fail,” or that the economy would not have withstood an implosion of the company. General Motors bankruptcy, therefore was a simpler process in some respects because it did not require intricate business negotiations. However, GM, unlike Chrysler, was a public company which caused additional problems. Not to mention that GM was massive; at least five times larger than Chrysler having more than ninety thousand employees, ten retirees for every active employee and nearly as much in liabilities ($172 billion) as Mexico's national debt (Ingrassia, 2010). Because of these monumental challenges, the Auto Task Force, with Harry Wilson as lead, collaborated with the leadership of GM to prepare a realistic viability plan; something GM leadership had proven they could not do on their own.

The collaboration began debate was anything but simple. Many GM executives were too proud to accept advice from a group of financiers who had no previous experience with the automotive industry. By April 22 GM had to borrow another $2 billion from the Treasury on top of the $13 billion already borrowed (Ingrassia, 2010). Since vehicle sales had not rebounded for the less-than-dismal numbers of January, GM was once again in need of immediate cash. On April 27 GM announced a public offering to exchange $27 billion in debt for GM stock (Ingrassia, 2010). GM needed to reduce its debt. The task force determined GM could not avoid bankruptcy if they could not shred ninety percent of their debt. Since GM was a public company its debt-holders ranged from large mutual funds to average citizens. As one would suspect, GM could not get ninety percent of its debt holders to willingly exchange its bonds for stock. Investors were further discouraged when the company posted a $6 billion loss for the first quarter of 2009. This meant that GM had burned through $10 billion in one quarter which amounted to $113 million every day (Ingrassia, 2010). As expected, the equity-for-debt exchange closed some weeks after the opening with hardly any takers.

General Motors had a poor hand which forced it to make more drastic employee cuts. The plan permitted the elimination of an additional 21,000 jobs on top of the 20,000 union jobs that had been eradicated since mid-2008 (Ingrassia, 2010). Meanwhile, both car companies began to take steps toward the reduction of their respective dealerships.

When Chrysler was in their bankruptcy process, they had to eliminate many of their dealerships. A common tradition of American car companies of the time was to have a multitude of dealerships instead of dealers in strategic positions throughout the country. Normally, a car company refrained from closing dealerships because there were a slew of associated costs that came with it because of contract agreements and state franchise laws (Rattner, 2010). The bankruptcy, however, trumped the state franchise laws and allowed Chrysler to notify certain dealerships that they were no longer an entity of the company. GM, who had not yet declared bankruptcy, also begun notifying dealers of their closure when Chrysler did.

The notification of closures came as a shock to those outside of the inner-circle of GM executives and the Auto Task Force because GM would be obligated to award the dealers damages (Ingrassia, 2010). Dealerships recognized the fact that GM was not in a position to pay them (unless it was borrowed from the Treasury) therefore they expected GM was close to entering bankruptcy. Another concern for General Motors was the excess of brands. In 2009, GM had seven brands comprised of Buick, Cadillac, Chevrolet, GMC, Hummer, Pontiac, and Saab. This had blossomed from their initial goal to provide a vehicle for every stage of a person's life, mostly based on their status and wealth. That goal had careened out of control, however, and GM found itself with too many brands; most of which were unprofitable. Through negotiation it was decided to keep Buick, Cadillac, Chevrolet, and GMC intact. Despite the efforts to cut costs, GM had to borrow yet another $4 billion on May 22, bringing the total at that time to $20 billion borrowed since December 2008 (Ingrassia, 2010). Therefore, the next step was bankruptcy.

GM filed for bankruptcy on June 1, 2009. GM's restructuring plan was to be formed quite differently than Chrysler's. This was mainly because GM was a public company and there were no takers for shares plus there was no buyer lined up – as there was in the case for Chrysler with Fiat. Just as with Chrysler, the UAW wanted cash for its VEBA instead of receiving stock. Eventually, however, the UAW agreed to $6.5 billion in preferred shares – which would pay dividends immediately – and the rest of its pledged $20 billion in common equity (Ingrassia, 2010). Unlike Chrysler, GM's creditors received their full $6 billion because they were secured debt-holders and GM would have had enough money to pay them had they liquidated. GM's unsecured debt-holders (most of which were small investors), however, received around 12.5 cents on the dollar (Ingrassia, 2010). GM emerged from bankruptcy court as “New GM” - containing Buick, Cadillac, Chevrolet, GMC, and other valuable assets – and the “Old GM” - which included those brands that were discarded, some property, and other liabilities. Old GM's components were sold off and, if buyers were not found, liquidated. Following the formation of New GM about $39.3 billion of the Treasury's initial investment was converted into common equity representing a 60.8 percent stake in the company (Congressional Oversight Panel, 2011). The Treasury also received $2.1 billion in New GM preferred stock, gave a loan of $7.1 billion to New GM and another loan of $986 million to Old GM (Congressional Oversight Panel, 2011). Additionally the Canadian government would get 12.5 percent for its contributions, the UAW would receive 17.5 percent and unsecured debt-holders would receive 10 percent (Ingrassia, 2010). GM came out of bankruptcy court with $17.6 billion debt, which was one-third of its previous total. However, through the restructuring plan, it cuts its number of employees from roughly 91,000 to less than 69,000; a substantial loss of American jobs. Overall, GM's bankruptcy case took a mere forty days to resolve; much shorter than the year that many predicted it would take.

Overall, the Treasury, through TARP, supplied Chrysler, GM, automotive finance companies, and parts manufacturers and suppliers $84.8 billion through loans and equity investments (OMB, 2012). Chrysler was extended many small loans by the Treasury; amounting to a total of $12.4 billion in aid. TARP held a $3.5 billion dollar loan with Old Chrysler as well as other investments in New Chrysler (OMB, 2012). When Old Chrysler offered a $1.9 billion payment in 2010, the Treasury wrote off the additional $1.6 billion owed since it had recovered more than initially expected. On May 24, 2011 – six years ahead of schedule – New Chrysler repaid the $5.1 billion in TARP loans (OMB, 2012). This payment terminated the remaining $2.1 billion in TARP loans. Furthermore, on June 2, 2011, the Treasury reached an agreement to sell its six percent equity interest in New Chrysler to Fiat for $560 million (OMB, 2012). Overall, Chrysler repaid $11.1 billion of the $12.4 billion in aid provided. Chrysler, for the second time in its history, proved it could receive government assistance and successfully repay its debt. The first time Chrysler did this, as previously mentioned, was in 1979 when the company received a $1.5 billion loan and paid it back ahead of schedule. Because Chrysler managed to repay its debt almost entirely, it can be said that the infusion of cash into the company was successful in getting the company financially sound. This is likely a direct cause, however, of Fiat’s management and supplementation of technology within Chrysler. Since the bankruptcy Chrysler has posted profits and avoided the headlines. GM’s prospects did not show the same promise.

As of May 31, 2012 the Treasury had recovered nearly fifty percent of its investments in GM and fully exited its involvement with Chrysler (OMB, 2012). New GM paid its $7 billion loan in April 2010 and held its first Initial Public Offering (IPO) in November 2010, where the Treasury sold nearly 359 million shares at $33.00 per share, and another 53.7 million in December at the same price (OMB, 2012). In total, the Treasury’s ownership of GM was reduced to 32 percent. As of May 31, 2012, TARP had recovered $24.1 billion of the $51.03 billion extended to GM (OMB, 2012). The largest concern is that the government still has stake in the company. The Treasury still holds about 500 million shares of GM, which is about 26 percent of the company (Woodhill, 2012). In order for the Treasury to regain its initial investment it must sell its remaining stock around $53.00 a share. However, as of November 23, 2012 GM’s stock price was only around $25.00; far short of the $53.00 needed for the Treasury to recoup its investment. Another aspect to consider is that if the price of GM stock did rise to the necessary level the Treasury could not sell all of its common stock immediately without likely causing a shock to the market. All things considered, the Treasury’s involvement in GM looks to be ongoing.

While both Chrysler and GM have made quite remarkable comebacks, many columnists have begun to question the sustainability of GM. GM, while remaining profitable, has shown a progressive decline in many key areas including revenue, net income to common, and overall cash flow (Muller, 2012). Therefore, one can deduce that the Treasury will have hard luck in recouping their investment in the coming years. Some contributors to weeklies such as *Forbes* have suggested that GM is on its way to bankruptcy again as a result of its ever-declining stock price and inability to compete with competitors’ products (Woodhill, 2012). Others, however, from the same magazine suggest that the company is not headed toward bankruptcy but admits second-quarter numbers are not promising; a result of poor leadership (Muller, 2012). One common theme that can be extracted from both views, however, is that it would not be prudent for the government to fund the company again. As has been proven in the past few years with the Treasury’s substantial stake in GM, the company has neglected to make significant changes that would allow for exponential growth within the company. Chrysler, on the other hand, has avoided headlines because of its new leadership in Sergio Machionne – the CEO of Fiat.

Overall, the U.S. government’s involvement in the rescue of Chrysler and GM in late-2008 and 2009 offered many new conundrums in regards to federal entanglement. While the effort was initially supported by a Republican president – and eventually executed by a Democratic administration – there has been praise and criticism offered by a multitude of financiers, political scientists, and economists. A major governmental precedent was established, showing that the Executive branch would come to the aid of failing companies if their downfall was detrimental to the economy, despite Congress not passing specific legislation. Other dangerous precedents were also established, however. One of which is the fact that those companies that are determined to be “too big to fail” may be rescued from financial instability by the U.S. government. In addition to this concept, as was exhibited in this case, the government showed its ability to drastically change the culture of a company when it effectively fired the CEO of GM. This raises the question: If the U.S. government provides support to an independent entity, where does its jurisdiction end? However, Chrysler proved once again that it could take a loan from the federal government and pay it back early; while GM exemplified the notion that government entanglements in large industrial companies such as General Motors are complicated. Whether one believes that the U.S. government should have federally funded Chrysler and GM’s bankruptcy or not, it was a landmark intercession of the federal government into the business world.

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1. Chapter 11 is a chapter of the U.S. Bankruptcy Code which enables any business (corporation, sole proprietorship, or individual) to reorganize. [↑](#footnote-ref-1)