

An Open Letter to Dept of Treasury II

Dear Mr. Henry Paulson

Your recent actions indicate you strongly agreed with the themes I proposed in my last letter to you dated August 27, 2008. You did accomplish one of your key goals of lowering the consumer mortgage rate. However, now we need to address the fundamental issue of the Financial Markets.

The Financial Markets operate on Trust; Trust that your counterparty will fulfill their obligations. This is why the earlier FED actions of lowering rates did NOT help. In fact, those actions actually contributed to the nervousness: The Curve steepened, Spreads widened, and Equities declined. It was only after the creation of the TAF, TSLF and PDCF facilities that markets calmed down. This alphabet soup of functions added confidence (Trust) to the system. However, the recent deterioration in the Financial Markets now requires further action on your part to address the Trust issue.

What we are experiencing now is a repeat of the 1920s style "Bear Raids" where large pools of "dark capital" overwhelmed the markets. Just notice this week's insanity. LEH stock declines so the Rating Agencies place them on "Credit Watch" for a downgrade. Then, the stock price declines further; a self-fulfilling prophecy. Or ABX/CMBS is shorted extensively inducing dealers/banks to liquidate to maintain Capital Ratios. Once again, a self-fulfilling event.

It was precisely these sorts of shenanigans that preceded the original creation of the SEC in the 1930s. And, if you recall, the first Chairman of the SEC was Joseph Kennedy who purportedly was one of the leading Exchange manipulators. In this light, we need immediate Government action that will in effect call a "time out" for the Financial Markets so that the medicine you and Mr. Bernanke have already supplied will have time to work.

What I recommend:

- 1) Publicly announce that you are going to examine the Short Interest of the Equity of all the major financials with the stated purpose of determining if there is collusion. You should also strictly enforce the "naked short" rule for all listed securities.
- 2) Publicly demand the disclosure of which entities are "short" the major Financial Indices, including ABX, CMBX, CDX, etc. Limits should then be created for non-hedging purposes that are similar in function to current CFTC limits for non-commercials.
- 3) Lower the Risk Weighted Capital requirements for all GSE Senior Debt and MBS securities to zero.
- 4) Allow the reclassification of some AFS assets into Held-to-Maturity.
- 5) Support the reclassification of Level 2 assets (mark-to-market) to Level 3 assets (mark-to-model).

There is no question that there are parties engaged in actions for short-term gain that are incongruent to the National Interest. There is certainly precedent for all the above actions. These actions do not involve the expenditure of Taxpayer dollars, nor do they involve the creation of Moral Hazard. What they do is eliminate the "gaming of the system" by currently stronger market participants.

Your most recent actions will work, they just need time. My recommendations above are a method to provide the required time.

Best Regards,
Harley S. Bassman

PS: As a reminder, this letter solely represents my personal opinion

September 12, 2008

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