Lots of articles in the past few days wondering what the banks are going to do with the bailout money. Its of course a legitimate question.

The response of the banks has been that the cash goes into a pool of capital and you cant segregate the new capital from the bailout capital. Fair point. You cant look at the cash in your wallet or bank account and know what the source of each dollar was. On the other hand, if someone offers you say 10pct of your networth in the form of a loan, don't you immediately consider all you could do with the money ? Of course you do.

But you also try to figure out if it's worth taking the money, and more importantly, how you are going to pay it back. The key to understanding how banks will use the money is understanding and having complete transparency about each bank's capital structure and its impact on owners of the bank, its shareholders.

If you look at the actual TARP document for the loans to banks, it has a lot of detail about what will happen to banks capital structure. It also creates a ton of issues, that if not handled properly by the Treasury, SEC and the banks receiving funds, will lead to confusion, lawsuits and loss of investor confidence in the banks.

Here are the issues that I think will be raised over the next 24 months that are going to get people upset:

1. There are going to be questions about the timing and accuracy of traditional SEC Filings in banks. The Treasury, through its ownership of warrants attached to the TARP, effectively owns a material amount of stock in each bank that has taken the funds. **WHERE are the 13D filings ?** For bigger banks in particular, stock prices have been devastated. I haven't done the calculations for the banks, but warrant coverage is at 15pct of the loan amount. Given that the more the bank needed the cash, the further its stock price was depressed, there is possibly a better than good chance that the Treasury effectively owns more than 5pct of more than a couple of the banks it has loaned money to. Where are the 13D filings ? Where are the banks taking the conservative approach and disclosing the exact details of the warrants and their impact on the current equity structure of the bank ?

2. There are going to be questions on how the warrants granted to the Treasury are priced. The TARP says that the warrants will be priced at the "market price", which it defines as previous 20 days average price. It doesn't define the average price. Is it the closing price ? The bid or ask price ? Given the volatility of share prices and the widening spreads during this financial crisis, we are talking about enough money that shareholders could be up in arms about that definition.

3. There is the impact of the timing of the funding on shareholder dilution. There has been a significant amount of volatility in bank share prices since the first payouts. If you happened to own shares in a bank that got TARP money while the market was down, you are going to be diluted further than the investor in a bank who got funded while the market was higher. At some point, someone will make an issue of this and sue someone for not acting quickly enough or timing the loan to be more beneficial to one bank over another. If the market sees a big sell off from current levels, the accusations will get stronger and louder. Regulatory agencies should get ahead of this curve and acknowledge this issue and possibly make the pricing mechanism longer than 20 days.

4. Where are the shelf registrations ? The Treasury was smart. They told the banks that they wanted to be able to sell the shares pretty much anytime they wanted after dec 31, 2009, to anyone they choose. In order to do so, the banks are required to file shelf registrations for the shares that could be created by exercising the warrants. Where are the shelf registrations ? Maybe they are all there and have flown under the radar. Maybe the banks and regulatory agencies interpretation of "The QFI will file a shelf registration statement covering the warrants and the common stock underlying the warrants as promptly as practicable after the date of this investment and, if necessary, shall take all action required to cause such shelf registration statement to be declared effective as soon as possible" are something I don't fully understand.

Regulatory agencies should set standards on how much time banks have to get these filed and take care to make sure that these are filed so shareholders can better understand the details and impact of the warrants.

5. Where the shit will reallly hit the fan is when the Treasury decides to start exercising the warrants they own and selling the shares. No matter what, its going to upset people. No one knows what the future of stock prices will be. But starting in 2010 when the selling can start, everyone who owns shares in the same companies the Treasury owns, will be freaking out wondering when the Treasury will sell. Shareholders will be screaming that they shouldn't sell. Everyone else will want the Treasury to take what will hopefully be profits and cash out, using the money to pay down our zillion dollar budget deficit. Of course, if the warrants are in the money, our politicians will be saying the same thing. No politician will pass the chance to look like a smart investor of taxpayer money.

Once again, it all comes down to transparency. If our regulators are smart, they will proactively deal with these issues. Hopefully, at worst, they will require the Treasury to file the same forms that any other shareholder would be required to file. If this doesn't happen, it will call into question whether or not full information about the banks capital structure is available and accurate. This will create a serious lack of investor confidence in the banking sector. A loss of confidence will hinder or worse banks ability to raise private capital. If they cant raise capital, they cant buy out the preferred they sold the treasury and they can't expand their loan portfolios, which was the entire point of the TARP.