FDIC
FEDERAL DEPOSIT INSURANCE CORPORATION

NEWS RELEASE

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CHAIRMAN SEIDMAN URGES SUPPORT FOR PRESIDENT BUSH'S S&L PLAN

Federal Deposit Insurance Corporation Chairman L. William Seidman today voiced his strong support for the President's proposal for dealing with insolvent savings institutions, and urged everyone interested in U. S. financial institutions to strongly support the initiative. "President Bush and Secretary Brady deserve great credit for their leadership. In the opening moments of the presidency, they moved swiftly to provide a sound approach to this difficult, complex, and painful problem," Mr. Seidman said.

The FDIC Chairman told financial analysts meeting in New York City that the President's decision to move quickly and propose the S&L program shortly after assuming office was fortunate, for action is needed to help regulators curb losses in the thrift industry. "Speedy action will bode well for future bank and thrift profitability," he commented.

Mr. Seidman said the President's program gives both regulators and the thrift industry a workable approach for moving into a new era. "One of the important features of

-more-the President's plan is the authority it will give the insurer to protect the insurance funds of the banks and savings and loans," Mr. Seidman noted.

He commented: "The proposal authorizes the insurer to set and enforce minimum capital requirements." However, Mr. Seidman said the deposit insurer, in its role as backup supervisor of the thrift industry, will not set unrealistic standards that will put viable institutions out of business. "As the new insurer of thrifts, the FDIC will have a new interest in the viability of every member of the industry." He observed, "It will be our aim to reach agreement on standards among the agencies."

Mr. Seidman also reiterated the need for the speedy passage of the mandated cross-guarantees contained in the President's plan. "All depository institutions that receive deposit insurance will have to guarantee the insurer against costs resulting from the failure of an affiliated bank," he said.

"In blunt terms, the stronger banks would no longer be free to walk away from their failing affiliates, leaving the clean-up cost for the FDIC." Mr. Seidman pointed out that, "This problem is well illustrated by the current situation at MCorp." Mr. Seidman emphasized that, "Clearly, if we had had our cross-guarantee structure in place, the problems at MCorp could be dealt with at a significantly lower cost to the government."

Passage of the cross-guarantee proposal is another reason for strong support for the President's plan, Mr. Seidman concluded.

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Savings and loan problems and the President's plan to solve them:

Remarks by

L. William Seidman
Chairman
Federal Deposit Insurance Corporation

Before

The Bank & Financial Analysts Association
New York, NY

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It is a great pleasure to be able to join you this evening. I have high regard for the Bank and Financial Analysts Association, and for your president, Bob Albertson, who wrote to me that he was planning a conference that would be neither tedious nor self-serving. That's a welcome relief from the Washington experience!

The FDIC Quarterly is available to all of you so I'll not be reporting on banking results for 1988 tonight. I'll just mention the industry did very well and that's good news.

I'd like to speak to you about our S&L problems and the President's plan to solve them.

Solutions to problems -- especially difficult ones -- take time to develop and implement.

For example, it was way back in 1797, on this very date, that the U.S. granted a patent to one Nathaniel Briggs for a washing machine. Yet, it took more than a hundred additional years before electricity and human ingenuity produced the early models of today's machines.

You might expect it to take even longer to find answers to problems that dwarf -- at least to those in this room -- the crisis of dirty shirts and socks -- yes, I mean the thrift problem.

But I'm proud to say it took our new president only a couple of weeks after assuming office to put a comprehensive plan on the table.

President Bush and Secretary Brady deserve great credit for their leadership. In the opening moments of the presidency, they moved swiftly to provide a sound approach to this difficult, complex and painful problem.

I support the President's solution to the thrift problem. We believe everyone interested in U.S. financial institutions ought to lend strong support.

Moving to address this problem quickly will bode well for future bank and thrift profitability.

One of the important features of the President's plan is the authority it will give the insurer to protect the insurance funds for banks and thrifts. We will have the authority to establish prudent industry-wide standards.

Now there is no question that the capital standards the President's plan envisions for the thrifts will be a challenge to achieve, especially given the required write-off of goodwill.

As the insurer, we are the backup supervisor of the thrift industry. We are not going to push for capital requirements that put viable institutions out of business. And as the new insurer of thrifts, the FDIC will have a new interest in the viability of every member of the industry.

It is unlikely that our capital requirements will be different than those set by the thrift's primary regulator, the Bank Board System. It will be our aim to reach agreement on standards among the agencies. Of course, the insurer's view will be a force for conservatism so that the troubles of the past will not be repeated.

The point is that we will seek to be a force for encouraging more capital in the S&L industry, but will not seek unrealistic capital levels or timetables.

What happens if a thrift cannot meet the tougher capital standards that are established by the President's bill?

The sanction required is simple and reasonable. Institutions should not be allowed to grow until they have increased their capital to satisfactory levels. After all, it was poorly capitalized thrifts that grew and made the thrift clean up so very costly.

Furthermore, as the insurer, we have flexibility under the President's bill to set insurance premiums within limits. It seems obvious that an insurer will not use this power to jeopardize industry stability. But the insurer certainly will try to build the fund to acceptable levels as rapidly as possible.

Let me turn now to another aspect of the President's Proposal -- which in many ways is a direct result of the problems and lessons of 1988.

As part of the President's proposed legislation dealing with the thrift problem, the deposit insurer would be given an important new power to help control costs. All depository institutions that receive deposit insurance will have to guarantee the insurer against costs resulting from the failure of an affiliated bank. In other words, in multi-bank holding companies, losses to the insurance fund caused by one subsidiary must be underwritten by all subsidiaries.

In effect, these mandated cross-guarantees would eliminate -- for purposes of deposit insurance -- the distinction between multiple bank structures and multiple branch banking structures.

In blunt terms -- the stronger banks will no longer be free to walk away from their failing affiliates -- leaving the clean-up cost for the FDIC.

This problem is well illustrated by the current situation at MCorp, with its 25 bank subsidiaries.

As I'm sure you have all heard, MCorp announced yesterday that it plans to seek protection from its creditors under Chapter 11. This action came in response to a petition filed by three creditors last week to place MCorp into involuntary liquidation under Chapter 7.

Not all of MCorp's banks are insolvent. Thus we can not take all of MCorp's bank resources to support the losses in its insolvent bank subsidiaries. We can't treat MCorp's banks as a single operating unit.

Further we can't sell all these banks as a single franchise.

Clearly, if we had had our cross-guarantee structure in place, these problems at MCorp could be dealt with at a significantly lower cost to the government.

Congress needs to act quickly on the President's proposal so we can more effectively keep the deposit insurer's costs down.

With the proposal in place it will be clear that bank holding companies can not leave the insurer holding the bag.

We understand the Bank Holding Company Association opposes this provision. Why? Because it will prevent holding companies from leaving their problems to the FDIC, and that will make funding for holding companies more difficult. Is that sound public policy?

Another subject of importance in the President's bill is the new liquidation corporation called the Resolution Trust Corporation, or "RTC."

The RTC will be a separate entity charged with handling the thrift resolution. It will be headed by a three person board -- the Secretary of Treasury, the Chairman of the Fed, and the Attorney General.

This body will receive at least $70 billion of funding from the Treasury and from S&L insurance premiums. It will use these funds to deal with currently insolvent thrifts, and those thrifts that become insolvent over the next three years.

This will be a monumental task -- indeed one unprecedented in the history of our government.

Including the problems dealt with by the FSLIC in 1988, about $400 billion dollars in deposits may have to be handled. This may involve $100 billion or more of real estate related-assets other than 1-to-4-family loans.

The RTC's board will select its CEO and determine its strategy for addressing this substantial undertaking.

It will have the authority to contract with the FDIC for assistance in the RTC's task. It is not clear exactly what role the FDIC will play.

As I said, that's RTC's call. Of course, we stand ready to help, and we expect to be heavily involved. But the new CEO of the RTC will be in charge.

As now planned, at the end of 5 years the RTC is scheduled to go out of business -- leaving it's unfinished works to the FDIC.

A central issue in how the RTC deals with the thrift problem is how it plans to handle the billions of dollars of real estate it will end up controlling.

I can only speak to what the FDIC's current policy is concerning the disposition of real estate -- the policy <u>we</u> would recommend if asked.

All real estate we control <u>is for sale.</u>

Importantly, we try and sell these properties at current fair market values. We do <u>not</u> engage in dumping. If we can't obtain today's fair price, we'll hold on.

To give you an example of that policy in action, earlier this month we offered some of our largest properties at auction. We succeeded in selling over half the properties offered -- for a total of over $40 million -- and at an average of 99 percent of current appraised values.

When offers were below our reserve price, we said no. I wouldn't call that "dumping" by any stretch of the imagination.

It is important that we pursue this policy. Government subsidized holding of properties off the market for higher prices actually can be detrimental to the real estate market and the local economy.

Large amounts of property overhanging the real estate market, under asset maintenance agreements, creates uncertainty because no one knows when the government might open the flood gates. And this retards economic recovery.

Incidently, the FDIC is moving to make the sale of real estate easier by accepting terms. That includes all cash bids. So come in and see us. We have lots for sale.

There are many more reasons to support fast action on the President's proposal.

1. Every day we wait will increase the cost of the thrift problem.
2. The uncertainty in the financial system caused by the operating insolvent institutions adversely affects <u>all</u> institutions.
3. The President's plan provides new supervision, controls, and penalties necessary to control the potential damage that deposit insurance can do by reducing depositor discipline.

As I've said, deposit insurance is like a nuclear energy plant. It can prove useful and produce benefits. But without proper controls, it can meltdown and endanger our financial system.

The President's bill provides the needed control system. Let's help the Congress put it in place.

Thank you.