FDIC
FEDERAL DEPOSIT INSURANCE CORPORATION

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FDIC CHAIRMAN OUTLINES THREAT TO INSURANCE FUND POSED BY BROKERED DEPOSITS

The Federal Deposit Insurance Corporation testified today that the indiscriminate placement of fully insured brokered funds in troubled banks and thrifts continues to pose "a clear and present threat to the deposit insurance system."

FDIC Chairman William M. Isaac, in testimony before a subcommittee of the Senate Banking Committee, noted that 69 of the FDIC-insured banks that failed during 1982-84 held over $1 billion in fully insured brokered deposits, increasing the FDIC's losses by hundreds of millions of dollars.

Mr. Isaac also cited an earlier survey that showed that of $24 billion in both insured and uninsured brokered funds in all FDIC-insured institutions, more than $9 billion was held by those rated as problem or marginal institutions. He said that troubled banks are twice as likely as all banks as a group to hold significant amounts of brokered deposits.

"It is a simple fact that troubled banks and thrifts use brokered funds more frequently and more extensively than well-rated institutions," Mr. Isaac noted. "These institutions tend to pay the highest rates, and brokered funds flow to the highest bidders."

The FDIC Chairman pointed out that a bank or thrift's strength or weakness is of only secondary concern to a broker, because there is no risk to the broker or its customers. "The investor merely has to look to the FDIC for repayment if something goes wrong," he said. "How many other business enterprises in the United States have their money market borrowings backed by the federal government in this fashion? Clearly,

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this is not what Congress intended when it crafted the deposit insurance system more than 50 years ago to protect the life savings of working men and women."

Mr. Isaac identified the 25 largest suppliers of brokered deposits to weak and risky banks, noting that Merrill Lynch and Dean Witter were at the top of the list, placing hundreds of millions of dollars in such institutions and substantially increasing the FDIC's exposure to loss. He said credit unions represented the largest single aggregate suppliers of insured brokered deposits, followed by commercial banks and savings and loan associations.

Mr. Isaac charged that the deposit insurance agencies "have received virtually no help from the Congress" in attempting to contain this serious threat to the insurance system. He noted that a House subcommittee has issued two "studies" contending there is no problem despite overwhelming facts to the contrary. He also noted that the Senate last year passed a bill that "would have literally tied both hands behind our back as we attempt to deal with misuse of brokered funds."

Mr. Isaac said regulatory initiatives to control the problem have helped, but additional measures are needed because a bank or thrift can purchase a massive volume of funding overnight, radically and precipitously altering its character and its risk to the insurance fund. He expressed continued support for a regulation, now being challenged in the courts, to limit insurance coverage of brokered deposits to $100,000 per broker per bank. He also called for enactment of legislation denying deposit insurance coverage to credit unions, banks and savings and loans placing their funds directly in other insured institutions.

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