FDIC
FEDERAL DEPOSIT INSURANCE CORPORATION

NEWS RELEASE

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STATEMENT OF THE FDIC

(Note: The following statement by the FDIC is occasioned by the release of two reports by the House Subcommittee on Commerce, Consumer, and Monetary Affairs. These reports address two issues: (1) attempts by the FDIC and the FHLBB to fashion effective responses to the large and growing threat to the deposit insurance funds posed by brokered deposits, and (2) the regulatory agencies' performance in identifying and pursuing criminal misconduct and insider abuse in banks.)

Fully-insured brokered deposits are one of the most serious problems in banking today and represent a clear and present threat to the deposit insurance system. They are a major source of funding for troubled banks and thrifts.

The Subcommittee's principal finding is that a majority of problem institutions that grew at a rapid rate in the first quarter of 1984 did so without relying on brokered deposits. This finding ignores the fact that there was a great deal of uncertainty during that period regarding the insurability of brokered deposits because of the then-pending rule to limit their insurance coverage. Moreover, abuses were spotlighted and measures to curb them were initiated. Despite these efforts, brokered funds in troubled banks grew from \$6.5 billion to \$8.5 billion -- approximately half the deposit insurance fund -- during the period in question. Moreover, a study of 110 recent bank failures reveals that 55 had more than \$1.0 billion in fully-insured brokered funds.

The Subcommittee report contains a number of recommendations. The FDIC is in full agreement with the first four of these and, in fact, has already taken such steps. The FDIC's efforts to deal forcefully with unsound lending practices are best illustrated by the initiation last year of 259 formal

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enforcement actions, compared to 111 in 1982 and 43 in 1981. The majority of these actions dealt specifically with unsound lending practices.

Minimum capital standards were first imposed by the FDIC in a 1981 policy statement, and in July 1984 the FDIC proposed a regulation which would increase minimum capital requirements. Increased public disclosure by banks has been an ongoing FDIC effort since 1982. In 1983 the FDIC issued a report to Congress recommending major deposit insurance reforms and submitted a bill which would accomplish many of these reforms. To date, Congress has not held hearings on the bill.

The fifth recommendation is at the heart of the issue. It suggests complete reliance on a regulatory solution to a problem that legitimately can and should be controlled to a greater extent by the markets. Rate-sensitive purchased liabilities are largely institutional funds. For the most part, these institutions have the capability to assess risk. However, many of them have found a much easier, risk-free way to place their funds. They simply pass the entire risk to the FDIC and sell their funds to the highest bidder. The highest bidder all too often is a troubled bank or thrift.

The issue is not whether brokers should be able to place such funds. They FDIC believes they should. The problem the FDIC's brokered funds regulation addresses is the ability of brokers to pass the risk, which should legitimately be borne by the broker or the investor, entirely to the FDIC.

It's incongruous that the same subcommittee that has levelled unsupported criticism against the regulatory agencies for being too lax in dealing with insider abuse has chosen not to support the FDIC's efforts to curtail a major source of funding for abusive practices, namely brokered funds.

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