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TESTIMONY OF

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ON

THE FINANCIAL INSTITUTIONS REFORM, RECOVERY
AND ENFORCEMENT ACT OF 1989

BEFORE THE

SUBCOMMITTEE ON FINANCIAL INSTITUTIONS
SUPERVISION, REGULATION AND INSURANCE
COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS
UNITED STATES HOUSE OF REPRESENTATIVES

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Room 2128, Rayburn House Office Building

Good morning Mr. Chairman and members of the Subcommittee. We appreciate the opportunity to appear today to provide our views on provisions of the Financial Institutions Reform, Recovery and Enforcement Act (FIRREA) that may require some modification and to comment on legislative initiatives to restructure the Office of Thrift Supervision (OTS) and restrict sales of subordinated debentures in financial institutions. As part of our testimony we also have attached a more complete listing of our suggested changes to FIRREA.

Today, we will address some of the more controversial issues that have arisen from FIRREA, including the leverage capital standard, purchased mortgage servicing rights and insurance coverage for 457 Plan deposits. We also will highlight other FIRREA provisions that, based on our experience to date, will need some revision. Finally, we will provide our thoughts on proposed legislation to restructure OTS and restrict the sale of securities in affiliated depository institutions.

Before focusing on those issues, we believe it is important to emphasize the numerous positive aspects of FIRREA. Without question it is one of the most significant pieces of financial institution legislation passed since the Great Depression, and it ultimately will cause sweeping changes in the operations and structure of the financial services industry. The most visible part of the legislation is the mechanism created, using a combination of private and public funding sources, to recapitalize the thrift insurance fund and resolve the crisis in the thrift industry.

However, in the long term, perhaps the more important aspects of the legislation are the provisions that are designed to control risk in the system. FIRREA has recast the structure of thrift supervision and returned the emphasis of savings association business to home lending. By establishing an independent thrift insurance fund, FIRREA has eliminated one of the basic conflicts that plagued thrift supervision and has put in place a structure that should facilitate a financially sound fund in the future. By increasing deposit insurance premiums and giving the FDIC needed flexibility to adjust premiums within specified limits based on fund experience, both deposit insurance funds ultimately will have a stronger financial base.

Supervision has been strengthened further by expanding the enforcement authority of federal regulators and requiring savings associations to comply with bank capital, accounting and supervisory standards. FIRREA also restricted allowable savings association activities and prohibited junk bond investments. The FDIC also was provided with back-up enforcement authority over savings associations, and we have established a good working relationship with OTS. We believe the back-up authority is proving to be a very good idea for protecting the insurance fund that possibly should be considered in other areas as well.

The pros and cons of individual sections of the law can be debated. From our perspective, however, FIRREA has made significant strides toward preventing a recurrence of the thrift industry's

problems. Over time, it should contribute to a stronger and sounder thrift industry and deposit insurance system. FIRREA represents a good first step toward resolving the complex problem of limiting risk to the government while maintaining a stable and efficient free market financial system. However, as with any first step solution to a highly complex problem, compromise is often necessary to balance conflicting objectives.

Based on our limited experience of only a few months, we have identified certain sections of FIRREA where changes appear necessary. We should point out that many of FIRREA's provisions have only recently become effective, and their potential impact is still not fully known. The issues we will discuss today represent only our initial efforts to identify needed changes. We expect to discover additional areas that need modification in the future as we receive public comments and as we gain more experience with the law.

FDIC BOARD SUCCESSION

One area of concern relates to the terms of the FDIC's Board of Directors. Under current law as amended by FIRREA, the terms of the FDIC's three appointive directors all expire together on February 28, 1993, and the statute is unclear on a crucial point of continuity: namely, whether the directors in office on that date will be able to continue to serve until their successors have been appointed and qualified. If they cannot, the FDIC will suffer a significant loss of continuity and -- for a period of time, at least -- of

independence, since the Comptroller of the Currency and the Director of OTS could well be the only FDIC directors then holding office. Since the appointive members all serve six-year terms, the continuity problem is likely to recur every six years.

To assure Board continuity, we recommend that the appointive members' terms be staggered, with termination dates coming no sooner than two years apart. If an appointive member leaves office in the last two years of his or her term, the President should be able to appoint a successor for the remainder of that term and for the succeeding term as well. In addition, the statute should make it clear that any director serving on February 28, 1993 may continue in office until a successor has been appointed and qualified. In fact, we see no reason for all appointive terms to end in 1993. Persons appointed to the Board in the next three years should be assured that they can serve for a full six-year term.

CAPITAL

Since one of the most controversial areas of FIRREA has been the capital requirements, we would like to comment on the leverage ratio, purchased mortgage servicing rights and the loans-to-one-borrower restrictions.

Capital leverage ratio. The new OTS capital standards established under FIRREA include a risk-based framework that is similar in many respects to the risk-based guidelines that were

adopted in early 1989 by the banking agencies. In accordance with FIRREA's mandate, the OTS also promulgated two other capital standards that establish constraints on how much a thrift can leverage its balance sheet assets. These leverage constraints consist of a 1.5 percent tangible capital requirement and a three percent core capital standard.

After the transition period for grandfathered supervisory goodwill ends at year-end 1994, the tangible capital of a savings association essentially will be the same as its core capital. Therefore, thrifts ultimately will need to meet a leverage ratio requirement for both core capital and tangible capital that is presently set at three percent. This three percent leverage standard is similar to the minimum leverage ratio proposed by the Office of the Comptroller of the Currency (OCC) in November 1989. The leverage standard eventually adopted by the OCC is of major significance to savings associations, since FIRREA requires the OTS to prescribe and maintain capital standards for thrifts that are no less stringent than the capital standards the OCC applies to national banks.

We agree with the establishment of a uniform minimum core capital leverage requirement for all banks and thrifts. We also support the exclusion of loan loss reserves from the definition of capital under a revised bank leverage standard. However, we are concerned about the use of a three percent core capital requirement as the <u>sole</u> minimum leverage standard.

The OCC's suggested three percent core capital constraint, in our view, should only be viewed as a subtest. That is, we believe a revised bank leverage standard should set forth a minimum total capital requirement over and above the OCC's proposed three percent core capital requirement. This additional capital could be comprised of secondary sources, similar to the manner in which the risk-based capital guidelines require both a minimum core capital standard and a higher minimum total capital requirement. The great majority of banks now meet the existing six percent total capital standard with a combination of core capital plus the allowance for loan losses. Since loan loss reserves usually do not exceed one-to-two percent of assets, most institutions presently meet the existing bank leverage standard with a minimum of four-to-five percent in core capital exclusive of the loan loss allowance.

Risks in the banking industry over the past decade have increased as deposit interest rate restrictions have been lifted and as competition has intensified. Many of these risks are not specifically captured in the risk-based capital framework. Moreover, the soundness of the risk-based capital standard is new and untested. As a result, we believe that any revised leverage standard should be maintained at a level that, in substance, is at least as stringent as the existing six percent total capital standard. Assuming loan loss reserves are excluded from total capital for purposes of a revised leverage

standard, we believe that the minimum total capital leverage standard for banks should be at least in the four-to-five percent range.

In essence, any revised minimum leverage capital standard for banks should not be allowed to materially reduce the minimum capital requirements for a significant number of institutions. Rather, the risk-based framework should function primarily as a vehicle for ensuring that certain banks -- including those with significant off-balance sheet risks -- maintain additional capital over and above a prudent leverage standard. Therefore, a leverage standard should remain a prominent part of bank capital standards and should not be relegated to a relatively obscure backstop role.

If the OCC decides to adopt the three percent core capital ratio as the sole minimum leverage standard, without requiring any higher total capital leverage standard, we believe the standard should specifically indicate that such a minimum will only apply to the most well-run institutions that have very high asset quality, minimal interest rate risk and composite CAMEL ratings of 1 under the Uniform Financial Institutions Rating System. These requirements are similar to the ones set forth by the Federal Reserve Board in its December 1989 proposal for revising the bank leverage ratio. In view of FIRREA's "no less stringent test" for thrifts, we believe similar capital standards ultimately should be applied to savings associations.

The FDIC hopes to reach final agreement with the OCC and the Federal Reserve on a revised bank leverage standard by year-end 1990, the date on which a minimum risk-based capital requirement first becomes effective.

Purchased mortgage servicing rights. Although thrift capital standards under FIRREA generally are required to be no less stringent than those applied by the OCC to national banks, FIRREA made an exception for purchased mortgage servicing rights. FIRREA specifically provides that the FDIC is to prescribe the maximum amount of purchased mortgage servicing rights that savings associations can recognize when calculating the amount of regulatory capital under the OTS tangible capital standard. In addition, the OTS limitations on the amount of servicing rights that may be recognized by a savings association when calculating its core capital must be at least as stringent as the limits applied by the FDIC to state nonmember banks.

The FDIC currently has no explicit limit on the amount of mortgage servicing rights that may be recognized by a bank for regulatory capital purposes. Although the FDIC retains the right to deduct mortgage servicing rights on a case-by-case basis if they are excessive in relation to capital or the market value of the rights, at present we do not impose an across-the-board maximum limit. (The OCC has a limit of 25 percent of Tier I capital.)

In view of FIRREA's mandate, the risks associated with purchased mortgage servicing rights, and the increasing levels of servicing rights that are being acquired by state nonmember banks, the FDIC Board on January 30, 1990 issued for public comment a purchased mortgage servicing rights proposal. The proposal, if adopted, would limit the amount of servicing rights that may be recognized for regulatory capital purposes to no more than 25 percent of core capital and, for savings associations, to no more than 50 percent of tangible capital. Mortgage servicing rights acquired before August 9, 1989 would be phased-out over time, and unlimited servicing rights could be held in separately capitalized mortgage banking subsidiaries.

Due to the risks associated with purchased mortgage servicing rights, the FDIC has proposed to treat the total amount of an institution's purchased servicing rights as a single investment for determining whether excessive concentrations exist in relation to capital. Only in those instances where the concentration of mortgage servicing rights exceeds 25 percent of capital will there be a need to limit the amount of these rights recognized for regulatory capital purposes.

At the same time, we realize this proposal is controversial to some within the banking and thrift industries. As a result, we are allowing a 60-day public comment period that extends

until April 10, 1990. The FDIC will carefully consider the comment letters and the views of all affected parties before making any final determination as to the merits of the existing proposal. We wish to make it clear that we do not intend to act on a final regulation until after we have firm data on the institutions that would be affected, the amounts involved, and whether the regulation would affect the inventory of institutions that might go into the RTC. We expect it will be late Spring before this information will be available to us for analysis.

Loans-to-one-borrower. Another capital-related issue that has raised some controversy is the loans-to-one-borrower provision that now applies to savings associations. Bank supervisors traditionally have preached risk diversification, particularly in the loan portfolio. It is a fundamental principal of sound banking that should be applied to individual borrowers as well as to groups of borrowers with related direct, indirect or contingent obligations. Risk diversification is especially important for controlling risk in the thrift industry, where capital levels already are low and loan portfolio concentrations already are high. Unfortunately, it is also a principal that has been violated all too frequently in the past -- often with serious ramifications for the insurance fund.

The FDIC fully supports the FIRREA requirement that applies the loans-to-one-borrower restrictions as defined in the National Bank Act to the thrift industry. Banks have operated successfully under these or similar restrictions for years. However, over the years banks also have developed extensive participation networks that effectively diversify the risk of one borrower to more than one institution. A properly structured loan participation allows selling banks to accommodate large loan requests which would otherwise exceed lending limits, while enabling them to diversify risk, and improve liquidity or obtain additional lendable funds.

While we see no reason why thrifts cannot operate successfully under these restrictions, we recognize that full and immediate implementation of these restrictions may place a short term hardship on the industry. The building of such a loan-sharing network requires time to develop and mature if thrift institutions are to continue to service their largest borrowers. For this reason, a transition rule is needed to phase in the restrictions.

MERGERS AND ACQUISITIONS

Insubstantial conversion transactions. One of the ways FIRREA attempts to attract capital into the thrift industry and enhance the overall value of individual savings associations is

by eliminating many of the prior impediments to mergers and acquisitions, especially for bank holding companies. The law, however, discriminates against the ability of smaller institutions to participate in deposit sales and transfers during the 5-year period when conversion transactions are prohibited.

Under FIRREA, conversion transactions (i.e. transfers of deposits between insurance funds -- BIF to SAIF or SAIF to BIF) are generally prohibited for five years. However, FIRREA permits one institution to acquire the deposits of another institution and convert them to a different insurance fund if the acquired deposits do not represent more than 35 percent of the selling institution's deposits. In addition, the acquired deposits cannot represent more than 35 percent of the acquiring institution's deposits. When the test is applied to the selling institution, it has the intended effect of keeping the bulk of the deposits of the selling institution in its current insurance fund. However, when applied to the acquiror, the test has the effect of discriminating against small institutions. Because of their size, these institutions may not be able to buy branches without exceeding the 35 percent restriction. Small, well-managed and well-capitalized institutions should have the opportunity to participate in this activity in the same way as larger institutions. Therefore, we believe the 35 percent test should not be applied to the acquiring institution.

Emergency State law override. When Congress addressed emergency mergers, it transferred the emergency thrift-merger statute from the National Housing Act to the Federal Deposit Insurance Act. As now constructed, the wording of the statute's branching provisions could raise a barrier to the FDIC's emergency assistance process in unit-banking states.

The provisions were designed to allow a surviving institution to retain the branches of a thrift acquired under the emergency procedures. Prior to FIRREA, the survivor was always a thrift since either the acquiring institution was a thrift or the troubled thrift continued to survive. Today, banks are encouraged and stand ready to take over troubled thrifts. However, their enthusiasm for such acquisitions is based in large part on their ability to retain the thrift's branching network.

Unfortunately, a federal court in a unit-banking state has read this provision so as to limit the FDIC's ability to transfer thrift branches when the acquiror is a bank. The court has indicated that when a bank acquires a troubled thrift in a unit-banking state, the resulting entity is subject to the state's bank branching laws and, thus, the bank may not retain the acquired thrift's branches. We believe the court improperly construed this provision and the construction is at odds with the policy, structure and language of the emergency-merger

statute as a whole. Nevertheless, the practical effect is that the decision reduces the value of thrifts to the banking sector, and thereby impairs the FDIC's and the RTC's ability to arrange mergers for them. When the FDIC or the RTC provides assistance for an emergency merger involving a troubled thrift, the surviving institution should be allowed to retain the troubled thrift's branches regardless of to whether the survivor is a thrift or a bank.

QTL TEST

FIRREA imposed a revised Qualified Thrift Lender (QTL) test that will require savings associations to carry at least 70 percent of their portfolio assets in qualified investments by July 1, 1993. This test will have a substantial impact on savings association operations. While recognizing the intent of the test, our concern is that interest rate risk in the thrift industry, which is already high, could become even worse. The result could be a further deterioration of the thrift franchise value. In our view, the full impact of the QTL test should be carefully reviewed to ensure that such an unwanted result is avoided.

SAVINGS ASSOCIATION POWERS

In conjunction with the QTL test, FIRREA also imposes certain restrictions on savings association powers. The objective of these restrictions is to establish parallel

regulation of state and federally chartered savings associations in many areas and to prevent state savings associations from engaging in activities not authorized to federal associations. The FDIC, however, is authorized to grant exceptions to these restrictions. But, FDIC approval of exceptions is permitted only if an institution is in compliance with its fully phased-in capital standards. There is no flexibility in that requirement. Institutions not in compliance with the capital standards cannot apply for a waiver to engage in or continue certain activities, even when such a waiver would be clearly beneficial to both the institution and the insurer.

In our view the law is too restrictive in this respect. It inhibits positive, creative ideas that could aid in an institution's recovery or in a meaningful restructuring or divestment plan. We believe that a provision is needed allowing more flexibility where an activity will clearly benefit an institution and poses no risk to the insurance fund.

INSURANCE OF "457 PLAN" DEPOSITS

FIRREA requires the FDIC to issue uniform deposit insurance regulations applicable to all insured depository institutions. On December 21, 1989, we issued a proposed rule to implement FIRREA's mandate in this area. In doing so, we had to resolve existing differences between FDIC insurance rules and those of the FSLIC. One of the most controversial and significant of

those differences involves so-called "457 Plans." This aspect of our proposed insurance regulation is the most frequently mentioned issue in the many public comments we have received on the rule.

A "457 Plan" is a deferred compensation plan established by a state or local government or a non-profit organization for the benefit of its employees, which qualifies under Section 457 of the Internal Revenue Code. Although there is no specific provision in the FDIC's current regulations, the FDIC staff has taken the longstanding position that, unlike other pension plans, deposit accounts maintained by a "457 Plan" with an insured bank are not entitled to pass-through insurance coverage for the beneficiaries of the plan. The staff's position is based on the fact that, under Section 457 of the Internal Revenue Code, the funds of 457 Plans are required to remain solely the property of the employer. This provision enables the employer to utilize 457 Plan funds for its own purposes and makes those funds subject to the claims of the employer's creditors. The employer, rather than the employees, is thus deemed to be the sole owner of the funds until they are distributed.

On this basis, the FDIC legal staff has maintained that the employees (the plan participants) do not have any ownership interest in the funds upon which insurance coverage could be

based. Thus, the funds are not insured on a pass-through basis. Consequently, deposit accounts at FDIC-insured banks which are comprised of 457 Plan funds have been added together and insured up to $100,000 in the aggregate. In contrast, FSLIC regulations insured 457 Plan deposit accounts at savings associations up to $100,000 per participant. The FSLIC regulation was based on the theory that 457 Plan deposits should, as a matter of policy, be accorded the same insurance provided for most other trusteed employee benefit plan deposits.

We know of no economic or policy reasons why the deposits of 457 Plans should not be afforded the same pass-through insurance coverage that is provided for the deposits of most other trusteed employee benefit plans. However, our legal staff's analysis of existing law indicates that it does not authorize insurance to plan participants.

We are currently considering whether we can and should expand insurance coverage to 457 Plans. We have extended the public comment period on our proposed insurance regulation until March 23rd and are holding a public hearing today on the 457 Plan issue to ensure that we have all the facts at our disposal. While there may be policy considerations favoring the insurance of these accounts, if our final determination is that we do not have the legal authority, we will not be able to continue coverage for future deposits. If there is a strong

congressional interest in providing insurance, we suggest that Congress consider providing specific authority for deposit insurance to 457 Plan participants.

ADVERTISING OF INSURANCE

Prior to FIRREA, the FDIC had express statutory authority to regulate the way in which insured banks advertise their FDIC insurance, as well as to prescribe the official FDIC sign and regulate the manner of its use and display. Under our authority to regulate advertising of FDIC membership, the FDIC required all insured banks to include the legend "Member FDIC" or equivalent language in their advertisements.

In prescribing the new official sign for SAIF members and authorizing the FDIC to regulate its use and use of the existing FDIC sign, FIRREA inexplicably eliminated our authority to regulate the way in which insured depository institutions advertise their insurance. This has led to an emotional and heated debate over, for example, whether insured savings associations may advertise themselves as "FDIC-insured" and the extent of the FDIC's authority to resolve such disputes.

We believe it should be made clear that the FDIC can continue to regulate deposit insurance advertising by restoring our express authority to do so. This authority should be broad enough to allow the FDIC to deal with any related advertising

issues. In addition, the official sign an institution is allowed to use should depend on whether the institution is a SAIF member or a BIF member, rather than on whether it is a savings association or a bank (as the law now is drafted), since some banks may be members of SAIF and some savings associations may be members of BIF.

CROSS GUARANTEES

One of the positive aspects of FIRREA is the new cross guarantee liability of affiliated banks and savings associations. This provision was designed to keep multi-institution holding companies from abandoning failing insured affiliates. Insured affiliates were made guarantors because they are the direct beneficiaries of deposit insurance.

The law is a significant addition to the FDIC's resolution arsenal, but it has not proven to be as effective as originally expected for a variety of reasons. First, and most importantly, the cross guarantee only applies to institutions affiliated at the time of failure. This creates an incentive for holding companies to sell or otherwise separate the healthy insured institutions prior to a failure. We believe the insurance fund should be able to reach assets of formerly affiliated insured institutions that are separated from common control relationship within a certain amount of time prior to the failure of an insured affiliate. Therefore, we recommend that once a

financial institution is identified as in danger of failing, formal notice of that determination to the holding company could serve to legally obligate the failing institution's affiliates under the cross guarantee provisions whether or not they are commonly controlled at the time of actual failure.

We also have found that the required process for determining losses delays reimbursement and therefore cannot be used in conjunction with the resolution of the failing affiliate. In addition, because the cross guarantee only applies to insured affiliates, even in situations where default is of little or no concern, holding companies are finding it advantageous or prudent to transfer traditional banking activities and assets (such as data processing and trust operations) to nonbank subsidiaries in order to remove assets from the potential scope of the cross guarantee provisions. While we do not have a ready solution to these two areas of concern, we believe a rule that requires a bank to be able to operate under existing rights when a bank holding company fails should be required for safety and soundness.

REPUDIATION OF CONTRACTS/"GOLDEN PARACHUTES"

FIRREA confers upon the FDIC, in its role as conservator or receiver, the power to disaffirm or repudiate any contracts that are burdensome, and which the FDIC determines "will promote the orderly administration of the institution's affairs." We expect

this power will be an important tool for the FDIC and the RTC, as we carry out our responsibilities as conservator or receiver. It will be particularly helpful in repudiating some employment contracts commonly known as golden parachutes.

While the general contract repudiation provisions in FIRREA are very helpful, they may not be sufficient to deal with all abusive golden parachutes. These powers may need to be enhanced to provide the FDIC with the necessary tools to deal with such contracts. Creative lawyers and bank management can devise deferred benefit arrangements, or time them, so that our ability to repudiate them is made more difficult. Further, our contract repudiation authority is of little value in attacking golden parachutes before an institution fails. Specific legislation empowering the FDIC to prohibit or limit excessive or abusive golden parachutes, in whatever form they may take, would be helpful.

APPRAISAL REFORM

FIRREA also took positive steps with respect to real estate appraisals by mandating major reforms in the real estate appraisal industry. The FDIC and the other Federal financial institution regulators have begun the process of improving the quality of appraisals used at federally insured institutions. However, one anomaly that arises under FIRREA is that all federally related transactions must have licensed or certified

appraisals by August 9, 1990, while the states have until July 1, 1991 to install a certifying and licensing process.

Further, in our view, there is a good possibility that the deadlines for full implementation of all aspects of the appraisal process may not be realistic. The expected increase in the demand for complex appraisals, at a time when fewer individuals may be qualified to perform those appraisals, could delay a large number of real estate transactions and result in a substantial cost to the FDIC and the RTC. While lawyers, doctors, accountants and other professions have had decades to set up their self-regulatory professional organizations, FIRREA gives the appraisal industry only two years to create the same type of regulatory infrastructure. Passing the necessary state laws, establishing the necessary federal guidance, and then licensing or certifying thousands of appraisers is a tall order to complete by July 1, 1991. To eliminate or at least reduce this problem, some type of phase-in program should be designed. The phase-in could decrease the initial demand for certified appraisals and at the same time increase the number of available certified appraisers.

Finally, the funding and operational rules for running the Appraisal Subcommittee are proving difficult to determine. An extension of time to draw on the $5 million funding line from the Treasury and clarification of the terms of repayment may be necessary.

RESTRUCTURING OTS

We have been asked to comment on legislative initiatives that would abolish or restructure OTS. So far, there seem to be two basic models. One, proposed by Congressman Schumer, would have the OCC supervise all thrifts -- both state and federally chartered -- and the Federal Reserve supervise thrift holding companies. The other, recommended by Congressman Leach, would have federal thrifts under the OCC, state-chartered thrifts under the FDIC, and thrift holding companies under the Federal Reserve. As we understand the "Leach approach," the regulatory and supervisory structure would mirror the existing system for banks.

We are not convinced that the thrift supervision structure should be changed at this time. It has only recently been changed and should be given a chance to work. Further changes at this time could result in unnecessary confusion, uncertainty, and further disruption to the thrift industry.

However, if restructuring is undertaken, we strongly favor following the bank model in which federally chartered thrift institutions would be regulated by the OCC and state-chartered institutions by the FDIC. The fundamental reason for our position is that we want to preserve the dual banking system. From our country's earliest beginnings, states have been engaged in the chartering and regulation of banks. Using that

authority, states have been able to develop banking structures that best meet their needs and that permit reaction to changing local circumstances. Moreover, the dual banking system has provided an effective avenue for introducing major innovation to the marketplace.

By placing all thrifts under the regulation and supervision of the OCC, the incentive to remain a state-chartered institution will vanish. Since state supervisors depend largely on examination fees for revenue, any significant decrease in the number of state-chartered institutions will affect their revenue and result in cutbacks in their supervisory programs.

Overall, it would be our recommendation that Congress resist the temptation to make further changes to the Federal supervisory structure at this time. We should first gain a better perspective on how the FIRREA-created structure is actually operating. Continual reorganization can be self-defeating.

RESTRICTIONS ON SALES OF SECURITIES

The FDIC has been analyzing the need to restrict sales of securities on bank premises. We are now working on a regulation that would prohibit the sale of securities of an insured depository institution, its holding company, or other affiliates on the premises of the insured institution. The main purpose of

the regulation is to prevent abusive practices that confuse customers into thinking they are purchasing an insured deposit, when in fact they are buying an uninsured, unsecured instrument. Such a regulation would protect consumers, as well as preserve confidence in the industry. Legislation might help to more clearly define our authority to regulate this activity.

While there are clear benefits to regulating these practices, and we are inclined to believe they should be regulated, there are a number of issues that we are still in the process of examining. Our preliminary findings indicate that such abusive practices are not necessarily widespread and therefore may not warrant an additional regulatory burden. We are continuing discussions with other federal regulators to be sure we ascertain the extent of the problem.

The legislation introduced by Congressman Schumer would explicitly prohibit this practice. What is already recognized as an unsound activity would be made specifically illegal. While strengthening federal regulation in this area is probably a good idea, we would strongly recommend that any bill grant definitional authority to the federal banking agencies. Rigid, inflexible statutory definitions of such terms as "ownership interest," "banking office" and "security" could lead to unintended results, particularly as the marketplace and products and services evolve. The agencies should be authorized to

define the statutory terms as the changing supervisory environment may dictate.

CONCLUSION

In conclusion, the FDIC believes that the changes made by FIRREA have been very positive. However, there are areas that could benefit from additional changes and fine tuning. We believe that the thrift regulatory structure put in place by FIRREA should be given time to work before it is altered again.

Thank you Mr. Chairman and members of the Subcommittee. I am prepared to answer any questions.