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This trip is the fourth time that I have been in either Lawrence or Kansas City in the last year and a half. Already this year, I have been to six of the FDIC's eight supervisory regions talking with any banker who wanted to attend the meeting to discuss any subject on his or her mind. There has been a lot of interest in these meetings. We have scheduled similar meetings -- which are co-sponsored by the Independent Bankers Association of America and the American Bankers Association -- in our other two regions in September and November. Those meetings will complete our country-wide effort to meet with bankers this year.

Having worked on banking issues for most of my professional life -- in the private as well as the public sector -- I know that bankers value frank and candid discussion, the kind of discussion we have when we are face-to-face. So do I. We may ultimately agree to disagree, but at the end of the day I want you to be able to say that I have been straightforward with you -- that I made every effort to tell you what I thought and to hear what you have to say.

I came here today to talk with you about the problem of the Savings Association Insurance Fund (SAIF) -- which you have probably heard me discuss before. In fact, my first formal speech as Chairman of the Federal Deposit Insurance Corporation -- in December, 1994, to the ABA's Government Relations Council -- was a discussion of the SAIF problem, the need to find a mutually acceptable solution, and what would happen if the problem were not addressed.

I do not have the gift of prophecy -- what some people in rural Tennessee where I grew up called "The Sight." Nor can I tell the future from cards, tea leaves, or a divining rod.

At the FDIC we can, however, determine through analysis what the range of possible outcomes would be under various assumptions about the future -- in other words, we can forecast. In late 1994 and early 1995 we forecast, among other things, that at some point sooner rather than later, the SAIF would become nonviable.

We crafted a solution to the SAIF problem -- one endorsed by Alan Greenspan and the Federal Reserve Board and approved by both houses of Congress on a bipartisan basis, but ultimately not enacted. This solution -- which called for SAIF members to fully capitalize their fund -- has languished. There is a cost to legislative inaction -- and the longer the legislation languishes, the higher the cost is likely to be. While the legislation has languished, our forecasts have been coming true.

For example, we said that if a substantial, on-going disparity in deposit insurance premiums for identical coverage were created, institutions would find a way to shift deposits from SAIF-insured to Bank Insurance Fund (BIF)-insured affiliates. Most SAIF-insured institutions are paying 23 cents in premiums for every $100 of insured deposits. Most BIF-insured institutions are paying virtually nothing. You do not need a Ph.D. in economics to figure out which is the better deal -- you also do not need a calculator -- you do not even need a pencil.

The law generally prohibits charter conversions from SAIF insurance to BIF insurance, but thrift companies have been successful in finding ways to shift deposits by providing incentives to customers to move money from one affiliate to another. Golden West Financial Corporation owns World Savings and Loan Association -- a SAIF member, and World Savings Bank FSB, a BIF member. In the four quarters ending March 31, customers shifted an estimated $6.5 billion in deposits from the SAIF member to the BIF member. That represents about one-third of the company's total deposits of a year ago. In the process, Golden West reduced its annual deposit insurance costs by about $15 million.

When deposits migrate from the SAIF to the BIF, they do not carry reserves. With every dollar that migrates from the SAIF to the BIF, the BIF reserve ratio declines. To prevent dilution of the Bank Insurance Fund, every dollar that moves from SAIF to BIF coverage must be capitalized by all BIF members. The $6.5 billion in deposits moved from SAIF to BIF by Golden West requires about $85 million in reserves for the BIF to prevent dilution of the fund. As the pace of deposit shifting increases, the cost to all BIF members from dilution could rise, either in the form of higher assessment rates or of reduced rebates.

As you know, the FDIC recently approved two applications for BIF insurance by banks that will be affiliated with SAIF-insured institutions. Both applications presented the potential for deposit migration, and indeed one of the institutions specifically indicated that customers of its SAIF-insured affiliate would be given the option of placing maturing deposits with the new BIF-insured bank. The FDIC Board of Directors looked at whether these applications could be denied based on the prospect that deposits may be encouraged to migrate from SAIF to BIF. The Board, however, concluded that under the law there is no restriction on customers voluntarily deciding to move deposits or on an institution having a voluntary customer migration strategy in which customers are offered the opportunity to move their deposits to obtain more favorable interest rates and fees. The law restricts institutions from transferring deposits in bulk, by merger or assumption; but it does not apply to voluntary customer migration. In approving the applications, the Board of Directors stated that a migration strategy that amounts to the factual equivalent of a merger is prohibited and if it sees such a strategy -- such as the transfer of deposits without the affirmative voluntary consent of the depositors -- it will take steps to stop the practice.

Applications similar to the ones the FDIC Board approved are under review at other agencies. A shift of about $100 billion from SAIF to BIF would cause the BIF reserve ratio to fall below 1.25 percent, thus triggering higher BIF assessment rates.

There is another cost to legislative inaction. As migration continues, leaving weaker thrifts and the banks that own SAIF-assessable deposits to cover future insurance losses -- the result will be a smaller, weaker SAIF that is less able to diversify its risks. In other words, as deposits shift, the SAIF will become more and more vulnerable to the failure of one large institution or several smaller ones. We have not predicted such failures, but they are possible.

I have yet to touch on one last element of the SAIF problem -- the declining portion of the SAIF assessment base available to service Financing Corporation (FICO) obligations. As you know, approximately $793 million of SAIF assessment revenue each year goes to fund interest payments on FICO bonds. BIF-member Oakar institutions and SAIF-member Sasser institutions are excluded from FICO assessments. That leaves only SAIF-member savings associations available to fund FICO obligations. If SAIF funds available to FICO shrink $118 billion -- about 26 percent -- the total would drop below the $333 billion necessary to fund FICO payments. Those bonds would go into default. That could conceivably happen as early as next year -- even the ABA's numbers show that, when corrected for an error in their 1995 projections of the SAIF assessment base.

Of course, the FICO obligation has been the sticking point in the legislative solution to the SAIF's problems -- the legislation would have BIF members contribute a pro-rata share of the payment -- about $600 million annually -- and many banks have opposed making this contribution. While the potential FICO default is more a concern of the U.S. Treasury than it is a concern of the FDIC, a potential default raises the specter of legislating in a crisis atmosphere -- precisely the situation that led to the current funding difficulties of the SAIF.. Chairman Leach of the House Banking Committee has proposed legislation that would call on Government Sponsored Enterprises (GSEs) to contribute funds to pay half of the FICO obligation -- about $395 million annually. The enterprises named in the legislation -- the Federal National Mortgage Association (Fannie Mae), the Federal Home Loan Mortgage Corporation (Freddie Mac) and the Federal

Home Loan Banks -- could certainly afford to do so. Together, they made about $4.5 billion in net income last year. They would benefit directly from protecting FICO from default because -- just as FICO obligations do not carry the full faith and credit of the U.S. government -- neither do GSE obligations. I applaud Chairman Leach's continuing efforts to find a solution to the SAIF problem. His proposal deserves serious consideration.

The SAIF problem is knotty. There are two approaches to dealing with a knot. One is to untie it -- separating the different threads and working with each individually. That is the approach we took in crafting a legislative solution last year. The other is to give up on the details and cut through to a simple solution. I have heard some talk in Washington of legislation to merge the funds and have every member then pay a pro-rata share of everything. The combined fund would be strong. It would be an actuarially sound insurance fund, it would have a larger membership and a broader distribution of geographic and product risks, and it would have a broad assessment base available to meet FICO interest payments, all but eliminating the possibility of a default.

While a merger of the two funds is the best way to assure the long-term viability of deposit insurance, I have not proposed the immediate merger of the funds because BIF members would have to pay not only a share of FICO but also for significant dilution of the BIF without the benefit of more than $5 billion that SAIF members would pay under the interagency plan to capitalize the SAIF. Nevertheless, such an immediate merger of the funds could be a legislative reaction to the current stalemate.

If the funds were to be merged today without the special assessment the thrifts have pledged, the combined reserve ratio would be $1.10 for every $100 of insured deposits -- and the fund would be about $4 billion short of the amount needed to meet the reserve ratio required by law of 1.25 percent of every $100 of insured deposits.

Assessment rates would have to be increased by 13 basis points to raise the reserve ratio to the target within one year, which the law requires. Moreover, banks would still have to pay the pro-rata share of the FICO obligation. When Congress gave the FDIC the responsibility for the SAIF, the fate of BIF and SAIF became inextricably linked. No insurance fund managed by the FDIC has failed. As long as I am Chairman, no insurance fund managed by the FDIC will fail -- for the simple reason that such a failure would call into question the confidence that the public has placed in banking over the last 60 years. We will not allow the time and effort that went into building that confidence go to waste.

I believe there is now increasing willingness on the part of all of the banking trade groups to discuss an effective and acceptable solution to the SAIF problem -- a solution that would include putting in place a process for assuring that charter issues are addressed before there is a merger of the funds. I will be meeting with representatives of all the trade groups next week to discuss these issues. I hope everyone will come to the table prepared to talk seriously about how to get the SAIF's problem behind us.

There is an old saying: where you stand depends on where you sit. Because of where I sit, I stand ready to talk with anyone, anytime, about a solution to the SAIF problem. We have a legislative solution pending in Congress that would work, but it could be modified to resolve some of the concerns that trade groups have expressed. Continued inaction can only drive the ultimate costs for bankers higher and lead to less acceptable solutions. It is in all our interests to get the problem resolved and to move on to other issues of common concern -- such as relieving regulatory burden and assuring that banks operate on a fair, competitive footing with other financial institutions.

Thank you for letting me speak with you today. I look forward to continuing to work with you.

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