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FEDERAL DEPOSIT INSURANCE
CORPORATION

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FEDERAL DEPOSIT INSURANCE CORPORATION

①
"THE PATHOLOGY OF BANKING"

BEFORE THE

SCHOOL OF BANKING OF THE SOUTH
LOUISIANA STATE UNIVERSITY

① BATON ROUGE, LOUISIANA

MAY 23, 1978 40 ①

"THE PATHOLOGY OF BANKING"

THIS EVENING, I WOULD LIKE TO DISCUSS WITH YOU SOME OF THE PATHOLOGICAL ASPECTS OF BANKING, A SUBJECT THAT IS NOT IN YOUR CURRICULUM AT THE SCHOOL OF BANKING OF THE SOUTH, BUT ONE WHICH IS RELATED TO MOST OF THE SUBJECTS IN THAT CURRICULUM. YOU KNOW PATHOLOGY IS DEFINED AS "THE BRANCH OF MEDICINE THAT DEALS WITH THE NATURE OF DISEASE, ESPECIALLY WITH THE STRUCTURAL AND FUNCTIONAL CHANGES CAUSED BY DISEASE"; OR, "ALL THE CONDITIONS, PROCESSES OR THE RESULTS OF A PARTICULAR DISEASE"; OR "ANY ABNORMAL VARIATION FROM A SOUND OR PROPER CONDITION." THIS USE OF THIS MEDICAL TERM, THEN, IS QUITE APPROPRIATE BECAUSE I WANT TO TALK TO YOU ABOUT THE FDIC ACTIVITIES DESIGNED TO SEE THAT BANKS AND THE BANKING SYSTEM REMAIN HEALTHY AND VIGOROUS. HOW DO WE DETECT WEAKNESSES OR ILLNESS IN THE INDIVIDUAL BANKS OR THE BANKING

SYSTEM? HOW DO WE HELP CURE ANY SUCH ILLNESS? HOW DO WE ARRANGE FOR THE FUNERAL IF THE ILLNESS IS FATAL? HOW DO WE DISPOSE OF THE PROPERTY OF THE DECEASED AFTER THE INTERMENT? OUR SUBJECT THEN EVEN GOES BEYOND PATHOLOGY INTO OUR ACTIVITIES AS A MORTICIAN AND A CORONER.

THE PRIMARY MISSION OF THE FEDERAL DEPOSIT INSURANCE CORPORATION IS AND ALWAYS HAS BEEN TO PROTECT THE MONEY SUPPLY AND TO SOME EXTENT TO PROTECT DEPOSITORS FROM LOSSES, TO MAINTAIN CONFIDENCE IN THE BANKING SYSTEM, AND TO CONTRIBUTE TO THE STABILITY AND GROWTH OF THE ECONOMIC SYSTEM OF THE NATION.

OVER THE YEARS WE HAVE BUILT UP A SIZEABLE DEPOSIT INSURANCE FUND AS A MEANS OF MEETING THESE RESPONSIBILITIES. LAST YEAR WE WERE ABLE TO ADD OVER \$700 MILLION TO IT AFTER REBATING TO OUR MEMBER BANKS OVER 56%, OR \$412 MILLION, OF THEIR ASSESSMENT FOR THAT YEAR. AS OF DECEMBER 31, 1977, THE DEPOSIT INSURANCE FUND HAD ALMOST \$8 BILLION IN ASSETS.

ADDITIONALLY, THE CORPORATION IS AUTHORIZED TO BORROW UP TO \$3 BILLION FROM THE U. S. TREASURY WHENEVER IT SHOULD BE NEEDED FOR INSURANCE PURPOSES.

SINCE THE FOUNDING OF THE CORPORATION, 99.8% OF ALL DEPOSITORS IN FAILED INSURED BANKS HAVE RECOVERED THEIR DEPOSITS IN FULL. NOT ONLY HAVE THE DEPOSITORS FARED WELL, BUT THE FDIC HAS RECOVERED OR EXPECTS TO RECOVER ALMOST 90% OF ALL ADVANCES MADE FOR THE PROTECTION OF DEPOSITORS. MUCH CREDIT FOR THIS VERY FAVORABLE PERCENTAGE IS DUE TO OUR EXCELLENT BANK EXAMINATION AND LIQUIDATION STAFFS. THE EXAMINERS HAVE DETECTED WEAKNESSES IN BANK ASSETS EARLY - BEFORE THE QUALITY OF THE ASSETS HAS ERODED TOO FAR -- AND THE LIQUIDATORS HAVE PURSUED ENERGETICALLY AND IMAGINATIVELY BOTH BORROWERS AND PROSPECTIVE PURCHASERS OF OTHER ASSETS.

OUR FIRST LINE OF DEFENSE IN MAINTAINING A SAFE AND SOUND BANKING SYSTEM IS OUR DIVISION OF BANK SUPERVISION, I.E.,

THE BANK EXAMINERS. CONTINUING IN MEDICAL TERMS, THEY ARE THE FAMILY PRACTITIONERS AND DIAGNOSTICIANS OF FDIC. THEY CONDUCT THE PERIODIC EXAMINATIONS OF INDIVIDUAL BANKS TO CHECK ON THEIR SAFETY AND SOUNDNESS, AND ON THEIR COMPLIANCE WITH VARIOUS STATUTORY REQUIREMENTS. THEIR ACTIVITIES REPRESENT THE PREVENTIVE MEDICINE ASPECTS OF OUR REGULATORY ACTIVITIES. THE PRINCIPAL EXAMINERS WHO VISIT YOUR BANK ARE CAPABLE PEOPLE WHO APPLY IN AS UNBIASED A MANNER AS POSSIBLE THEIR KNOWLEDGE, EXPERIENCE AND TRAINING IN ANALYZING THE CURRENT CONDITION AND THE MANAGEMENT CAPABILITIES OF YOUR BANK. I BELIEVE THAT THE RELATIVE SOUNDNESS OF THE BANKING SYSTEM IS ATTRIBUTABLE TO THE FACT THAT MOST BANK MANagements RECOGNIZE THEIR TALENTS, GIVE CONSIDERABLE WEIGHT TO THE COMMENTS IN THE REPORTS OF EXAMINATIONS, AND USE THEM AS A MEANS OF DETECTING AND CORRECTING WEAKNESSES WHICH POTENTIALLY COULD DEVELOP INTO MAJOR PROBLEMS FOR THE BANKS. THE REPORT OF EXAMINATION ALWAYS HAS BEEN ADDRESSED TO THE BOARD OF DIRECTORS FOR USE IN CONTROLLING THE OVERALL OPERATIONS OF THE BANK, BUT THE EXAMINER MET WITH

THE BOARD ONLY IF THE BANK HAD SIGNIFICANT PROBLEMS. RECENTLY WE HAVE CHANGED THIS PROCEDURE TO HAVE HIM MEET WITH THE BOARD OF DIRECTORS AFTER EACH EXAMINATION EVEN IF THERE ARE NO SIGNIFICANT PROBLEMS. HE NOW DISCUSSES DIRECTLY AND PERSONALLY WITH THE DIRECTORS HIS OR HER OBSERVATIONS ON THE CONDITION OF THE BANK AND SUGGESTIONS FOR IMPROVEMENT.

LIKE DIAGNOSTIC INTERNISTS OUR EXAMINERS LOOK FOR CLUES THAT WILL INDICATE THE HEALTH OF THE BANK. GENERALLY SENIOR EXAMINERS HAVE GOOD PERSPECTIVE BECAUSE THEY OBSERVE, REVIEW AND ANALYZE OPERATIONS OF MANY DIFFERENT BANKS. IN THE CASE OF HEALTHY BANKS, THE EXAMINER'S COMMENTS AND SUGGESTIONS NATURALLY WILL BE BRIEFER.

WE ARE FORTUNATE THAT IN THE BANKING SYSTEM AS A WHOLE ONLY A VERY SMALL PERCENTAGE OF BANKS HAVE SERIOUS ILLNESSES. ACTUALLY AT THIS TIME, ONLY ABOUT 2½% OF ALL INSURED BANKS REPRESENT SUPERVISORY PROBLEMS. THESE ARE PLACED ON OUR PROBLEM LIST FOR MORE FREQUENT REVIEW THAN NORMAL. WE ARE

PLEASED THAT ONLY ABOUT 1/20TH OF 1% OF ALL INSURED BANKS IN THIS COUNTRY ARE IN THE MOST SERIOUS CATEGORY, WHICH WE CALL SERIOUS PROBLEM - POTENTIAL PAYOFF.

WHICH BRINGS US NOW TO THE QUESTION OF HOW FDIC HELPS CURE ILLNESSES WHEN THE BANK'S MANAGEMENT AND ITS BOARD OF DIRECTORS DO NOT HEED ADVICE GIVEN BY OUR EXAMINERS THROUGH THEIR VISITATIONS AND REPORTS OF EXAMINATION. NORMALLY A PROBLEM BANK HAS A LARGE VOLUME OF CLASSIFIED ASSETS THAT EITHER HAVE BEEN CHARGED OFF OR SHOULD BE CHARGED OFF TO PROPERLY REFLECT THE BANK'S TRUE FINANCIAL CONDITION. BANKS MUST BE ADEQUATELY CAPITALIZED AND HENCE THE CAUSE OF THE ILLNESS (OR WEAKNESS) MUST BE CORRECTED WITHIN A VERY SHORT PERIOD. IF THE DIRECTORS AND MANAGEMENT DO NOT ACT PROMPTLY AND VIGOROUSLY WE BEGIN TIGHTENING SUPERVISION ONE NOTCH AT A TIME. WE HAVE SEVERAL TOOLS WE CAN USE TO DO THIS.

OUR CEASE-AND-DESIST POWERS UNDER SECTION 8(B) AND 8(C) OF THE FDI ACT PROBABLY WOULD BE THE FIRST USED TO GAIN COMPLIANCE IF THE CONDITION OF THE BANK IS NOT IMPROVED. SOME OF THE UNSAFE OR UNSOUND BANKING PRACTICES THAT HAVE NECESSITATED ENFORCEMENT ACTIONS BY THE FDIC INCLUDE: INADEQUATE CAPITAL, ILLIQUIDITY, FAILURE TO DIVERSIFY ASSETS, INSIDER ABUSES, HAZARDOUS OR LAX LENDING PRACTICES, AND FAILURE TO COMPLY WITH LAWS AND REGULATIONS. THIS POWER HAS BEEN USED RELATIVELY FREQUENTLY IN RECENT YEARS. THE BOARD OF DIRECTORS AUTHORIZED THE ISSUANCE OF 45 CEASE AND DESIST ORDERS LAST YEAR AND 41 SUCH ORDERS IN 1976.

ANOTHER PROTECTIVE POWER WE HAVE IS THE REMOVAL OF AN OFFICER OR DIRECTOR UNDER SOME CONDITIONS. THEY ARE: BEING GUILTY OF VIOLATING ANY LAW OR REGULATION, A BREACH OF HIS FIDUCIARY DUTY, OR ENGAGING IN AN UNSAFE AND UNSOUND PRACTICE WITH RESPECT TO THE BANK. IN ADDITION THE ACT MUST HAVE CAUSED OR THREATEN SUBSTANTIAL FINANCIAL DAMAGE TO THE BANK. HOWEVER

WE NEED ADDITIONAL AUTHORITY IN THIS AREA BECAUSE AN OFFICER OR DIRECTOR MAY CAUSE SERIOUS FINANCIAL LOSS TO A BANK WITHOUT BEING GUILTY OF PERSONAL DISHONESTY. CONSEQUENTLY, THREE YEARS AGO WE PROPOSED LEGISLATION GIVING US WIDER POWERS TO REMOVE OFFICERS AND DIRECTORS OR TO ISSUE CEASE AND DESIST ORDERS AGAINST THEM INDIVIDUALLY AS WELL AS AGAINST THE BANK WHEN THEIR ACTIONS CLEARLY ARE SERIOUSLY DAMAGING THE BANK'S FINANCIAL CONDITION.

NEXT, A SALE OR MERGER IS CONSIDERED IF THE OFFICERS AND DIRECTORS HAVE TRIED AND HAVE BEEN UNABLE TO MAKE SUBSTANTIAL PROGRESS TOWARD REHABILITATING THE BANK. OFTEN, A HEALTHY BANK IS WILLING TO PAY A PREMIUM TO OBTAIN A NEW GROUP OF ACCOUNTS, VALUABLE BRANCH LOCATIONS, OR A NEW BANK FOR THEIR HOLDING COMPANY. A BANK'S STOCKHOLDERS AND DIRECTORS GENERALLY PREFER A MERGER TO THE SPECTER OF THE LIQUIDATION OF THEIR BANK.

IF ALL ELSE FAILS, WE MAY DECIDE TO INITIATE PROCEEDINGS TO TERMINATE INSURANCE. THIS OF COURSE IS A DRASTIC ACTION AND IS ONE THAT WE DO NOT TAKE LIGHTLY. IF THE BOARD VOTES TO TERMINATE INSURANCE THE DEPOSITORS OF THE BANK ARE NOTIFIED OF THE ACTION. THE INSURED BALANCES IN ACCOUNTS LESS SUBSEQUENT WITHDRAWALS CONTINUE TO BE INSURED FOR 2 YEARS. THIS ACTION IS TAKEN ONLY AFTER MUCH EFFORT TO REHABILITATE THE BANK AND AFTER CAREFUL DELIBERATION BECAUSE THE REMOVAL OF INSURANCE IS ALMOST CERTAIN TO BE THE DEATH KNELL OF THE BANK.

FROM 1934 TO 1977, IT HAS BEEN TAKEN AGAINST A TOTAL OF 240 BANKS. IN SLIGHTLY LESS THAN ONE-HALF OF THE CASES, CORRECTIONS WERE MADE, AND IN MOST OF THE OTHERS THE BANKS WERE ABSORBED BY OTHER INSURED BANKS OR CEASED OPERATIONS PRIOR TO THE ESTABLISHMENT OF A DATE FOR DEPOSIT INSURANCE TERMINATION. IN 13 CASES, INSURANCE WAS TERMINATED OR THE BANK CEASED OPERATIONS FOLLOWING THE FIXING OF A DATE FOR INSURANCE TERMINATION.

IN SPECIAL CIRCUMSTANCES, THE CORPORATION MAY PROVIDE ASSISTANCE TO AN OPERATING INSURED BANK. IT MAY BE IN THE FORM OF THE PURCHASE OF ASSETS, THE GRANTING OF A LINE OF CREDIT, OR THE PURCHASE OF A CAPITAL NOTE. THIS TYPE OF ASSISTANCE CAN BE PROVIDED BY US ONLY WHEN THE BANK IN DANGER OF CLOSING IS ESSENTIAL IN PROVIDING ADEQUATE BANKING SERVICES TO THE COMMUNITY. ASSISTANCE OF THIS NATURE HAS BEEN EXTENDED ONLY FOUR TIMES IN THE HISTORY OF THE CORPORATION, THE FIRST BEING IN 1971.

THE CORPORATION CAN TAKE ANOTHER STEP SHORT OF AN ACTUAL LIQUIDATION BY PURCHASING SOME OF THE ASSETS IN ORDER TO IMPROVE THE CONDITION OF THE BANK ENOUGH TO MAKE A MERGER WITH IT ATTRACTIVE TO A STRONGER BANK. WE DID THIS IN 1977 WHEN WE PURCHASED \$15 MILLION OF POOR QUALITY ASSETS FROM BANCO ECONOMIAS, SAN GERMAN, PUERTO RICO FOR \$15 MILLION IN CASH. THE PURCHASE OF THOSE ASSETS IMPROVED ITS FINANCIAL CONDITION ENOUGH FOR A SUBSIDIARY OF BANCO CENTRAL, MADRID, SPAIN TO MERGE WITH BANCO

ECONOMIAS. WE TOOK THIS UNUSUAL STEP BECAUSE THE ECONOMY OF PUERTO RICO WAS IN ESPECIALLY POOR CONDITION AT THE TIME AND WE WERE CONCERNED ABOUT THE IMPACT THE CLOSING OF THE \$170 MILLION BANCO ECONOMIAS MIGHT HAVE ON OTHER BANKS IN PUERTO RICO.

IF A BANK'S CONDITION IS INCURABLE AND IT MUST BE CLOSED WE HAVE ADDITIONAL RESPONSIBILITIES. FEDERAL LAW PROVIDES THAT THE FDIC WILL ACCEPT APPOINTMENT AS RECEIVER FOR ALL FAILED NATIONAL BANKS, AND THAT WE ALSO SHALL ACCEPT APPOINTMENT AS RECEIVER OF STATE-CHARTERED BANKS, WHENEVER AUTHORIZED BY STATE LAW AND TENDERED BY THE APPROPRIATE STATE AUTHORITY. THE ESTATE OF THE DECEASED BANK IS, BY COURT ORDER, HANDLED BY THE CORPORATION THROUGH OUR LIQUIDATION STAFF.

IN ACTING AS RECEIVER THE FDIC HAS AVAILABLE SEVERAL OPTIONS. THEY INCLUDE ENTERING INTO A PURCHASE AND ASSUMPTION TRANSACTION WITH A NEW OR EXISTING BANK, THE DIRECT PAYOFF OF DEPOSITORS, OR THE ESTABLISHMENT OF A DEPOSIT INSURANCE NATIONAL BANK, WHICH WE CALL A DINB.

IN A PURCHASE AND ASSUMPTION TRANSACTION, THE FDIC AS RECIEVER ARRANGES FOR A NEW BANK TO ASSUME THE DEPOSIT LIABILITIES OF THE FAILED BANK AND GENERALLY SELLS SOME OF THE GOOD ASSETS TO THE NEW BANK. IT THEN PAYS THE NEW BANK IN CASH THE DIFFERENCE BETWEEN THE DEPOSIT LIABILITIES ASSUMED AND THE VALUE OF THE ASSETS BEING PURCHASED PLUS THE PREMIUM BID BY THE NEW BANK FOR THE RIGHT TO ACQUIRE THE DEPOSIT BUSINESS AND THE VALUABLE BANKING LOCATIONS. AT THE SAME TIME, IN EXCHANGE FOR ITS ADVANCE THE FDIC AS A CORPORATE ENTITY OBTAINS FROM THE FDIC AS RECEIVER THE REMAINING ASSETS OF THE FAILED BANK FOR LIQUIDATION PURPOSES. FROM THE COLLECTION OF THESE ASSETS THE FDIC RECOVERS AS MUCH AS POSSIBLE OF ITS ADVANCES, COSTS OF LIQUIDATION AND ALLOWABLE INTEREST. IN SOME CASES MORE THAN THAT IS RECOVERED SO THAT THE RESIDUE OF ASSETS ARE PRO RATED AMONG SUBORDINATED CREDITORS OR STOCKHOLDERS.

PURCHASE AND ASSUMPTION TRANSACTIONS GENERALLY HAVE SOME SIGNIFICANT ADVANTAGES VIS-A-VIS A STRAIGHT PAYOFF OF INSURED DEPOSITS. THE BENEFITS INCLUDE:

REDUCTION IN LOSSES INCURRED BY FDIC OR MAXIMIZING RECOVERIES FOR SUBORDINATE CREDITORS;

IMMEDIATE AVAILABILITY OF 100% OF DEPOSITS TO DEPOSITORS;

RECOVERY OF ADDITIONAL FUNDS THROUGH THE PREMIUM PAID FOR THE ACQUISITION OF THE DEPOSITS AND LOCATIONS EXPEDITING LIQUIDATION BY THE SALE OF SOME ASSETS TO THE ASSUMING BANK;

CONVENIENCE FACTOR - THE DEPOSITOR MAY CONTINUE TO USE OLD CHECKS, DEPOSIT SLIPS AND PASSBOOKS AT THE SAME GEOGRAPHICAL LOCATION.

AND, OF SPECIAL SIGNIFICANCE, THE TRANSACTION HELPS MAINTAIN MAXIMUM CONFIDENCE IN THE BANKING SYSTEM SINCE THE IMPACT OF THE CLOSING IS GREATLY REDUCED.

WHEN THE DEPOSIT PAYOFF METHOD IS NECESSARY, THE FDIC PAYS DIRECTLY TO THE DEPOSITORS THE NET AMOUNT COVERED BY INSURANCE. THE FDIC THEN FILES A CLAIM WITH THE RECEIVER AS A GENERAL CREDITOR AND SHARES PRO RATA WITH EXCESS DEPOSITORS AND OTHER CREDITORS EVENTUAL DIVIDEND DISTRIBUTIONS FROM LIQUIDATION PROCEEDS.

IN A FEW UNUSUAL SITUATIONS A NEW BANK CANNOT BE LOCATED TO ASSUME THE DEPOSIT LIABILITIES OF THE FAILED BANK AND NO LOCAL COMMUNITY OWNED BANK IS AVAILABLE TO PROVIDE BANKING SERVICES; WE THEN ARE AUTHORIZED TO FORM A DEPOSIT INSURANCE NATIONAL BANK. IN SUCH CASES, THE RECEIVER OF THE CLOSED BANK, NORMALLY THE FDIC, IMMEDIATELY TRANSFERS TO THE DINB ALL INSURED AND ALL FULLY SECURED DEPOSITS IN THE CLOSED BANK. THOSE FUNDS ARE AVAILABLE TO THEIR OWNERS TO THE SAME EXTENT THAT THEY WERE

AVAILABLE BEFORE THE BANK CLOSING. IN 1975 WE HANDLED TWO BANK CLOSINGS IN THIS MANNER, NAMELY, THE SWOPE PARKWAY NATIONAL BANK IN KANSAS CITY, MISSOURI AND THE PEOPLES BANK OF THE VIRGIN ISLANDS.

UNTIL THE PAST FEW YEARS, MOST FAILING BANKS WERE SMALL -- SAY, ONE TO TEN MILLION DOLLARS -- GENERALLY LOCATED IN RURAL SETTINGS. FOR THE PAST 32 YEARS FOLLOWING WORLD WAR II BANK FAILURE HAVE AVERAGED ABOUT SIX INSURED BANKS EACH YEAR. AS A RESULT, THE ACTIVITIES OF OUR DIVISION OF LIQUIDATION WERE MODEST IN SCOPE.

BEGINNING IN THE EARLY 1970'S, THE RATE OF FAILURES INCREASED AND FOR THE FIRST TIME LARGER BANKS WERE INVOLVED. PRIMARILY AS A RESULT OF THE POOR ECONOMIC CONDITIONS IN 1974 AND 1975 AND THE UNUSUALLY SEVERE AND PROLONGED REAL ESTATE PROBLEMS OF RECENT YEARS, WE HAVE EXPERIENCED 43 INSURED BANK FAILURES DURING THE PAST 44 MONTHS, ALMOST ONE A MONTH. THOSE FAILURES INVOLVED BANKS HAVING ASSETS TOTALING APPROXIMATELY

\$6.7 BILLION. THEY WERE LOCATED IN 25 STATES PLUS THE VIRGIN ISLANDS AND PUERTO RICO. ACTUALLY, THE 11 LARGEST BANK FAILURES IN OUR HISTORY HAVE ALL OCCURRED SINCE OCTOBER OF 1973.

THESE FIGURES ARE VERY SUBSTANTIAL BUT THEY SHOULD BE MEASURED AGAINST THE HEALTHY BANKS WITHIN OUR BANKING SYSTEM. IN 1976, THE WORST YEAR SINCE 1942 IN TERMS OF NUMBER OF FAILURES, THERE WERE 16 INSURED BANK FAILURES. EVEN IN THAT YEAR THE FAILURES AMOUNTED TO ONLY ABOUT ONE PER 1,000 BANKS, OR 1/10 OF 1% SINCE THERE ARE ABOUT 15,000 INSURED BANKS. THREE OF THEM WERE LARGE, THOUGH, AND THE RESOURCES OF THE 16 TOTALED APPROXIMATELY \$1 BILLION, WHICH ALSO WAS ABOUT 1/10 OF 1% OF THE RESOURCES OF ALL INSURED BANKS AT THE END OF THAT YEAR.

WHAT HAPPENS THEN TO THE ASSETS ACQUIRED BY FDIC AS INSURER FROM ITSELF ACTING AS RECEIVER? AS YOU WOULD EXPECT, MOST OF THE ASSETS WHICH WE ACQUIRE FOR LIQUIDATION ARE WORTH LESS THAN THEIR BOOK VALUE OR THE AMOUNT OF THE LOAN SECURED

BY THEM. FURTHERMORE THEY HAVE CONSIDERABLE DIVERSITY. AT ONE TIME OR ANOTHER, WE HAVE ACQUIRED AT LEAST ONE OF ALMOST ALL TYPES OF TANGIBLE COMMODITIES THAT ENTER INTO TRADE -- ALONG WITH THE HEADACHES AND CHALLENGES OF TAKING CARE OF THEM UNTIL THEY CAN BE DISPOSED OF. SOME ARE UNIQUE AND INTERESTING. ONE OF OUR LOANS, FOR EXAMPLE, WAS SECURED BY TWO RACE HORSES. HOWEVER, ONE HAD A BAD KNEE AND THE OTHER A BAD HIP. WE RECENTLY HAD TO ABANDON OUR INTEREST IN A MORTGAGE BECAUSE THE REFRIGERATION SYSTEM BROKE DOWN -- ONE MILLION POUNDS OF MEAT SPOILED AND THE RAT INFESTED BUILDING WAS CONDEMNED BY HEALTH AUTHORITIES. WE JUST ACQUIRED A FIRST MORTGAGE INTEREST ON A COAL MINE; UNFORTUNATELY, THE MINE WAS ON FIRE AND THE ENVIRONMENTAL PROTECTION AGENCY WAS DEMANDING CORRECTIVE ACTION. WE HAVE ACQUIRED AN INTEREST IN A CUBAN GOLD COIN COLLECTION AND A COLLECTION OF 125 STUFFED WILD ANIMALS. WE HAVE HAD DISTRESSED LOANS ON TAXI CAB FLEETS IN NEW YORK, CALIFORNIA AND ARIZONA. ONE OF OUR LOANS IS COLLATERALIZED BY A COPY OF THE KORAN VALUED IN SEVEN FIGURES, BUT, AS YOU CAN IMAGINE, THE MARKET IS A BIT THIN.

WE ALSO HAVE OPERATED A SIZABLE NAVY WITH A FLEET CONSISTING OF TUNA BOATS, SHRIMP BOATS AND OIL TANKERS. RUNNING A NAVY IS A COMPLICATED BUSINESS. WE HAVE EVEN HAD DIFFICULTY KEEPING OUR BOATS AFLOAT. WE HAD AN OIL TANKER RUN AGROUND OFF HAVANA, AND WE HAD A SHRIMP BOAT BLOWN INTO THE MAIN STREET OF ARANSAS PASS, TEXAS, BY HURRICANE CELIA. ONE LOAN WE ACQUIRED WAS TO A DISTRIBUTOR OF MOVIES, AND PART OF THE COLLATERAL IS A MAJOR X-RATED FILM. OUR PROSPECTS FOR ULTIMATE COLLECTION OF THAT LOAN DEPEND ON GOOD ATTENDANCE AT THAT FILM. THEN, WE BECAME CREDITOR OF AN INDIVIDUAL WHOSE MAIN SOURCE OF INCOME TO REPAY OUR LOAN WAS RENTAL PAID FOR THE USE OF A PROPERTY AS A BAWDY HOUSE. TALK ABOUT CONFLICTS OF INTEREST!

WE ALSO HAVE HAD TO OPERATE SOME OF OUR ASSETS -- MORE PROSAIC THAN SOME I HAVE MENTIONED BUT NEVERTHELESS CHALLENGING -- SUCH AS HOTELS, APARTMENTS, CONDOMINIUMS, RESTAURANTS, A BAKERY AND A KENNEL.

THE LIQUIDATION DIVISION IS BIG BUSINESS. AS OF MARCH 31,

1978, IT WAS ADMINISTERING APPROXIMATELY 79,000 ASSETS HAVING A BOOK VALUE OF APPROXIMATELY \$2.5 BILLION. IN TERMS OF ASSET SIZE, OUR LIQUIDATION DIVISION ALONE IS COMPARABLE TO THE 45TH LARGEST BANK IN THIS COUNTRY AND WOULD RANK AS THE 59TH LARGEST INDUSTRIAL CORPORATION AS REPORTED BY THE FORTUNE 500 LISTING: LARGER FOR EXAMPLE, THAN ALLIED CHEMICAL, GENERAL FOODS, AMERICAN CAN OR COCA-COLA.

DESPITE THE UNUSUAL NUMBER AND THE SIZES OF RECENT FAILURES, OUR DEPOSIT INSURANCE FUND HAS NEVER BEEN LARGER OR MORE LIQUID. THIS HAS BEEN ACCOMPLISHED THROUGH THE USE OF PURCHASE AND ASSUMPTION TRANSACTIONS WHEREVER FEASIBLE. AND IT ALSO IS A RESULT OF THE OUTSTANDING COLLECTION RECORD ACCOMPLISHED BY OUR DIVISION OF LIQUIDATION. ACTUALLY LIQUIDATORS - OUR MORTICIANS - HAVE COLLECTED OVER \$2 BILLION IN THE THREE YEARS OF 1975-1977.

NATURALLY WE PERFORM AUTOPSIES ON FAILED BANKS TO DETERMINE THE CAUSE OF THEIR DEMISE. I BELIEVE YOU WILL BE SURPRISED BY THE FINDINGS. ACCORDING TO OUR ANALYSES 57% OF

THE FAILURES OF THE PAST 17 YEARS WERE DUE PRIMARILY TO ABUSIVE INSIDER TRANSACTIONS, COUPLED IN SOME CASES TO OUT-OF-TERRITORY BORROWERS. TWENTY-FIVE PERCENT OF THE FAILURES WERE DUE TO EMBEZZLEMENT OR MANIPULATION OF BANK RECORDS AND 18% WERE DUE TO MANAGERIAL WEAKNESSES OF ONE FORM OR ANOTHER.

MANY CLOSINGS ARE A DIRECT RESULT OF BANK DIRECTORS' FAILURES TO USE REASONABLE OR ORDINARY CARE IN DISCHARGING THEIR DUTIES OR IN ALLOWING VIOLATIONS OF BANKING LAWS. IT IS A NORMAL PRACTICE FOR THE CORPORATION, IN ITS LIQUIDATION CAPACITY, THEREFORE, TO LOOK FOR POTENTIAL NEGLIGENCE AND TO FILE CLAIMS AGAINST MEMBERS OF THE BANK'S BOARD OR THEIR INSURANCE COMPANY WHEN SUCH ACTION IS WARRANTED. FOR EXAMPLE, LAST YEAR WE COLLECTED \$350,000 AS A SETTLEMENT OF A DIRECTORS' LIABILITY CLAIM AT THE BIRMINGHAM BLOOMFIELD BANK LIQUIDATION, MOSTLY FROM THE INSURANCE CARRIER.

WHENEVER IT IS DETERMINED THAT THE BANK HAD SUFFERED LOSSES DUE TO THE FRAUDULENT AND DISHONEST ACTS OF ITS EMPLOYEES,

THE CORPORATION ALSO PURSUES A CLAIM AGAINST THE BANKERS' BLANKET BOND CARRIER. AGAIN, LAST YEAR WE RECOVERED APPROXIMATELY \$3.4 MILLION FROM THE COMPANY WHICH INSURED THE STATE BANK OF CLEARING IN CHICAGO.

THE DECISIONS MADE IN BANK LIQUIDATION MATTERS ARE BASED ON OUR RESPONSIBILITY AS A FIDUCIARY. WE ARE OBLIGATED TO RECOVER AS MUCH AS IS REASONABLY POSSIBLE WHEN LIQUIDATING THE ASSETS OF A BANK.

IN SUMMARY, WE HAVE SKETCHED A NUMBER OF TOOLS WHICH ARE USED IN CARRYING OUT THE PRIMARY MISSION OF THE FDIC TO PROTECT THE MONEY SUPPLY AND TO SOME EXTENT TO PROTECT DEPOSITORS FROM LOSSES, TO MAINTAIN CONFIDENCE IN THE BANKING SYSTEM, AND TO CONTRIBUTE TO THE STABILITY AND GROWTH OF THE ECONOMIC SYSTEM OF THE NATION. WE USE ALL OF THEM TO MINIMIZE LOSSES TO DEPOSITORS AND TO FDIC. FROM 1934 THROUGH 1977, THE ENTIRE OPERATING HISTORY OF THE CORPORATION, 99.8% OF ALL DEPOSITORS IN FAILED INSURED BANKS HAVE RECOVERED THEIR DEPOSITS IN FULL.

DURING THAT TIME THE CORPORATION HAS DISBURSED APPROXIMATELY \$3.0 BILLION TO PROTECT DEPOSITORS IN 545 INSURED BANKS WITH AGGREGATE DEPOSITS OF ABOUT \$6.4 BILLION. WE HAVE RECOVERED OR EXPECT TO RECOVER APPROXIMATELY 90% OF THAT \$3.0 BILLION. IN MY OPINION THIS IS AN EXTRAORDINARY RECORD.