STATEMENT ON

STATE OF THE BANKING INDUSTRY AND FDIC ABILITY TO HANDLE PROBLEMS

PRESENTED TO

COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS
HOUSE OF REPRESENTATIVES

BY

IRVINE H. SPRAGUE, CHAIRMAN
FEDERAL DEPOSIT INSURANCE CORPORATION

9:30 a.m.

Tuesday, July 14, 1981

Room 2128, Rayburn House Office Building

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It is good to be here today to give you our view of the state of the banking industry and our ability to handle problems that might arise.

I can report that our nation's banking system is fundamentally sound. Americans can continue to bank with confidence. But we need to remain vigilant. There are problems, particularly in the savings banks, as you know. We must improve our capacity to respond to any eventuality.

You specifically asked me to discuss "current contingency planning efforts and a statement as to adequacy of resources available to you to respond to all predictable contingencies."

Your request is most timely. We would be derelict in not saying that this matter is uppermost in our minds too. I refer to the need to expand our powers to deal with failed bank and failing bank situations.

We have been working under virtually the same provisions of law for 31 years.

In these three decades, our insurance fund has grown from $1.2 billion to $11.5 billion. The amount of assets in the banking system has increased from $192 billion to more than $2 trillion. The total of insured deposits has risen from $91.4 billion to $948.7 billion. The statutory amount of deposit insurance has been increased from $10,000 to $100,000.

In 1950, there were 262 banks of more than $100 million in assets. In 1981 there are 1,919. Thirty-one years ago

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there were just 18 banks of more than $1 billion in assets. Today there are 228.

Banking has taken on enormous new dimensions of complexity and sophistication. Technology, including vast improvements in transportation systems, telecommunications, and computers, has revolutionized the banking industry. And there is no indication that the pace of change will slow down. To the contrary, intense, worldwide competitive pressures and the continuing volatile economic environment make it more likely than ever that precipitous change will continue.

Yet, we are being asked to monitor the banking world in the jet age with nothing more than the tools that served us in banking's horse and buggy days.

We are at present in the process of managing the phase out of interest rate ceilings as mandated in the Depository Institutions Deregulation and Monetary Control Act of 1980. The Depository Institutions Deregulation Committee three weeks ago voted to take actions effective August 1 that will make long steps in that direction. An important part of our task is to oversee the transition of thrifts to a deregulated environment, the likes of which they have never experienced.

Yet, we have had no major changes in a fundamental area of FDIC jurisdiction since the enactment of the Federal Deposit Insurance Act of 1950, which included for the first time Section 13(c) power to make capital infusions to failing banks under very restricted circumstances. The only other change in

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this area since then occurred with passage of the International Banking Act of 1978, which extended our failed and failing bank authority to insured branches of foreign banks.

FAILED OR NEAR-FAILING BANK OPTIONS

The FDIC now has seven options for handling failed or near failing banks. First, FDIC can pay off insured depositors of a failed bank. This was done, for example, earlier this year in the failure of The Des Plaines Bank, Des Plaines, Illinois, and it was done in three bank failures in 1980 and three in 1979. In the Des Plaines case, the bank had total deposits of $42.9 million in 15,000 accounts. In a payoff, depositors are paid to the statutory limit of $100,000. Account holders with deposits exceeding the limit and other creditors receive a pro rata share of the proceeds from the liquidation of the bank's assets over a period of years.

FDIC's second option is what we call a purchase and assumption (P&A) transaction between banking organizations in the same State. Healthy existing banking organizations or new organizations bid to assume the deposit liabilities of the failed bank and to purchase certain assets and the failed bank's goodwill. Such transactions have been arranged in three cases this year and seven times each in 1980 and 1979. One notable example of this procedure occurred in 1973 when the $1.3 billion United States National Bank of San Diego, California, failed. There, FDIC as Receiver of the bank, arranged a purchase and

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assumption transaction in which Crocker National Bank was the successful bidder. A purchase and assumption transaction by law must be projected to be less expensive than a payoff. In practice, such transactions have also proved to be less disruptive. Depositors and other general creditors recover all their funds, and banking service continues with little or no interruption, normally at the same location.

A third option takes the form of a purchase and assumption transaction involving foreign interests. This has occurred six times, the most highly publicized in 1974 after the failure of the Franklin National Bank in New York. Franklin, at the time of its failure, had over $3.6 billion in assets and $1.4 billion in deposits. It was sold to European American Bank & Trust Company, which is owned by a consortium of European banks.

A fourth option, also a variation of the purchase and assumption procedure, is to partition the failed bank's assets and liabilities and arrange for the transfer of asset-liability packages to more than one participating bank. This occurred after the 1978 failure of the $607.6 million Banco Credito y Ahorro Ponceno of Ponce, Puerto Rico. FDIC divided the bank between two assuming banks which lessened the anti-competitive effects of the transaction.

FDIC's fifth option, under very limited circumstances, is to provide assistance in order to prevent the failure of a troubled bank. This has occurred only five times since FDIC received the power in 1950, most recently last year when FDIC,

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along with 27 banks, loaned the First Pennsylvania Bank $500 million to avert its failure. As a condition to receiving FDIC assistance, all directors and principal officers serve subject to FDIC approval, and FDIC must approve their compensation. FDIC also must sanction any dividends and the bank's "plans and objectives". FDIC also received warrants for the purchase of First Pennsylvania Corporation's common stock. These are some of the key conditions which we tailored for the First Pennsylvania assistance. In another such case, we would expect to develop a similar but separate set of terms and conditions as necessary to meet the situation.

A sixth option, under Section 13(e) of the FDI Act, involves assistance to facilitate the merger of a failing bank into a healthy bank prior to actual failure, but this procedure is rarely used for a variety of reasons. The most recent instance was in November, 1975, when the Corporation authorized a loan of up to $10 million to facilitate the merger of Palmer First National Bank and Trust Company of Sarasota, Florida, into a newly formed national bank subsidiary of Southeast Banking Corporation of Miami, after written confirmations were received from the Comptroller of the Currency and the Board of Governors of the Federal Reserve System that such assistance was essential to effect the proposed acquisition and to prevent the imminent failure of the Palmer Bank.

A seventh option is a Deposit Insurance National Bank (DINB). The DINB would serve solely as a vehicle for the orderly payoff of insured deposits. In 1975 the Corporation established

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two DINB's in connection with the closings of the Swope Parkway National Bank, Kansas City, Missouri, and The Peoples Bank of the Virgin Islands, St. Thomas, Charlotte Amalie, Virgin Islands.

PROPOSED LEGISLATION

We have proposed to the Congress and solicit your active and aggressive support for legislation to provide an eighth and ninth option: to modify the statutory Section 13(c) test to enable us to make capital infusions more easily, particularly in the New York thrifts, and to permit FDIC as the Receiver of a large failed FDIC-insured bank to arrange a Section 13(e) purchase and assumption transaction with an out-of-State institution, but only if the failed bank had $2 billion or more in assets. Only 107 banks in the Nation would be eligible -- 89 commercial and 18 savings banks in 26 States, concentrated in New York, California, Ohio, Texas, Pennsylvania and Illinois. The qualifying size is indexed so inflation will not artificially increase the universe of eligible institutions. The other 15,000 smaller banks in the nation would not be affected and have no reason whatsoever to oppose our seeking a large bank solution.

Our legislation is designed to give FDIC powers which are similar to those that the Federal Savings and Loan Insurance Corporation (FSLIC) already has. Currently, FSLIC may provide assistance to an insured S&L even if the association is not essential to its community and FSLIC may assist the merger of a failing insured S&L with an out-of-State Federal S&L. The proposed legislation gives FDIC similar capabilities. Because

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of the unique nature of the various financial institutions, total comparability between FSLIC and FDIC powers probably is not desirable. Our legislation, however, will provide greater comparability between the two insuring agencies.

In the case of the failure of a bank of qualifying size, FDIC could consider this new alternative for arranging a purchase and assumption transaction, together with all the other possible courses of action. The interstate option would permit the FDIC to consider a course that would produce a meaningful purchase premium for assets, avoid anticompetitive effects and continue banking service.

Under the interstate option the FDIC would be required to inform the State banking superintendent in advance whenever the FDIC determines that the interstate option might be used. This is true whether a national or State-chartered bank is involved. If the State superintendent objects to an out-of-State transaction and FDIC agrees with the superintendent's reasons, then FDIC would abandon the interstate option and attempt to arrange an in-State purchase and assumption transaction or proceed with an insurance pay off. The FDIC can go forward with the interstate option, the superintendent's objections notwithstanding. However, before any out-of-State transaction may be made, the Board of Directors of the FDIC must unanimously agree on the decision. The Board also must provide the superintendent with a written certification of its determination.

Under the interstate option, FDIC as the Receiver of a failed bank of qualifying size would solicit offers from any

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bank and bank holding companies in the country that the FDIC determines are qualified and capable of acquiring assets and liabilities of the failed bank. If the highest acceptable bid is from an out-of-State bank or bank holding company, the FDIC must provide the highest in-State offeror an opportunity to make a higher offer. If the in-State offeror offers more, then FDIC must accept. If the in-State offeror does not, FDIC must give the same opportunity to the highest offeror from a State adjoining the State in which the closed bank was located. If the adjacent State offeror also declines, then the FDIC may accept the high bid, regardless of the location of the bidder.

This section of the bill would provide that a winning out-of-State bidder may reopen a closed bank only as a subsidiary so that no interstate branching will result. State banking law will prevail in the operation of the subsidiary. The section would authorize operation of the subsidiary, the Douglas Amendment notwithstanding. The section also would require that before any sale may be accomplished, appropriate State and Federal approvals must be obtained. For instance, a bank holding company must have approval of the Federal Reserve to acquire assets of a closed bank as a subsidiary. The section would prohibit FDIC from making any sale that would have serious anti-competitive results. Finally, the section has a five-year sunset provision.

The other basic change in our law would enable the FDIC to provide assistance to institutions whose problems stem principally from such causes as the interest rate squeeze.

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Currently, the FDIC can provide assistance to a bank only when it is in danger of failing and its continued operation is essential to provide adequate banking services in the community. The bill would modify FDIC powers to permit it also to act when it finds that severe financial conditions exist which threaten the stability of a significant number of insured banks and it is probable that any assistance to one of these threatened banks will substantially reduce the risk of loss or avert a threatened loss to the FDIC. This new test for assistance provides the FDIC with the needed flexibility to react to severe financial conditions as they arise. Unlike the current test which focuses exclusively on the essentiality of a single failing institution, the proposed new test focuses on severe financial conditions affecting the stability of a significant number of insured banks. Significance may be measured not only in terms of the total number of institutions, but also in terms of the total resources of the threatened institutions. In every instance, FDIC could provide assistance only where such action "will substantially reduce the risk of loss or avert a threatened loss to the Corporation". Essentially, this means that to qualify for assistance a bank must be among a significant number of banks whose stability is threatened by severe financial conditions, there must be a clear threat that without assistance the bank will fail, and it is probable that assistance will be "substantially" less expensive to the FDIC than other methods of handling the potential failure.

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In addition to the two basic FDIC provisions, the proposed legislation makes related changes in our law to make the total process more workable. These are:

(A). A provision that would clarify that foregone earnings resulting from FDIC loans to insured institutions are insurance losses. Currently, FDIC may deduct from assessments received from insured banks any insurance losses it experiences before calculating the proportion of the assessments to rebate to the banks. For example, in a typical purchase and assumption transaction, that portion of projected losses not recovered by the purchase premium would be established as a reserve account and charged against assessment income. In other words, the FDIC would experience an insurance loss that may be deducted from assessments. A below-market-rate loan also would result in a loss to the FDIC of the difference between what FDIC could earn on the funds if left in FDIC's portfolio and what it is earning from the loan. This opportunity loss is no different from a loss arising from a P&A. The structure of the transaction should not determine whether a loss can be recognized for insurance fund purposes. The FDIC seeks to clarify that this opportunity loss also is deductible from assessments. The FDIC is totally self-funded -- that is, funded by bank assessments and interest income rather than by public monies. This amendment will facilitate that result continuing.

(B). A provision that would broaden the field of institutions which may purchase the assets and assume the liabilities of a failed bank. In addition to FDIC-insured banks, under the

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proposal associations or banks insured by the Federal Savings and Loan Insurance Corporation would become eligible bidders.

BUDGETARY PROBLEMS

We are fully aware of the budget problems facing our government and we believe our proposed legislation will minimize the budgetary impact of future bank failures. While we have a separate fund, every expenditure of the FDIC represents a Federal expenditure and has a budgetary impact. We believe the powers we are asking for will result in a smaller outlay and lower cost to the FDIC than if we are forced to use only the alternatives now available to us. By minimizing FDIC's costs, we will, in turn, minimize the potential budgetary impact of future failures.

NEED TO ACT NOW

We are talking today about emergency legislation to meet a specific need. The Congress will also be considering broad, comprehensive and certainly controversial legislation to greatly expand the authority of thrift institutions with commercial bank powers and to address such questions as due on sale clauses, insurance limits, usury ceilings, plus possibly export trading companies and other matters.

We urge you to keep the issues separate: act now on the limited emergency bill needed now; deliberate and act later on the more comprehensive long term legislation.

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THE STATE OF THE FDIC

Both the financial and human resources of the FDIC remain strong, and we believe capable of dealing with any foreseeable eventuality, given the requisite statutory flexibility. Net income to our $11.5 billion insurance fund last year topped the billion dollar mark for the first time with a record $1.2 billion gain. This year we project net income of $1.3 billion. We also are entitled to borrow $3 billion from the Treasury if needed, although we do not anticipate it will be.

Our major resource is our corps of 3,500 skilled and dedicated employees who remain committed to fulfillment of our statutory mandate of promoting the safety and soundness of the banking system while at the same time continually seeking ways to do our job more efficiently. The Corporation is well managed. In 1979 our administrative expenditures increased just 3.4 percent, compared to 9.5 percent Government-wide. In 1980 our increase was 10.7 percent, compared to 17.3 percent throughout Government. Our 1981 outlays are well below our budget. One example of the effort of our people to improve efficiency is in the area of travel expenditures. Our staff will travel an estimated 16 million miles to carry out their bank examination duties in 1981, a reduction of 12 percent from 1980, which was itself a reduction of nine percent from 1979. We are able to achieve these savings by more careful scheduling of examinations and by more efficient car pooling, and a spirit of cooperation from our work force.

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Supervisory Innovations: Some examples of supervisory innovations we have undertaken in recent years are as follows: (a) our Division of Bank Supervision and the Division of Management Systems and Financial Statistics developed a computerized system, which we call our Integrated Monitoring System, for the primary purpose of monitoring the activities of banks between examinations to help us decide where best to allocate our examiner time and resources. With this system we have been able to reduce the number of examinations conducted. (b) the development of a modified examination concept, which provides for the review of the safety and soundness essentials of a well managed bank without requiring the comprehensive detail of a full-scope examination. This program has enabled us to reduce the time required to perform most examinations. (c) in cooperation with individual States, we have significantly expanded the divided examination program so that we presently participate with 20 States in divided examination arrangements covering 3,400 banks, just over one-third of all insured State nonmember banks with resultant substantial savings. (d) last year our Division of Bank Supervision developed streamlined common application forms. These are now in joint use by the Corporation and 22 States, thereby requiring a bank to complete only one form -- a form that requires only essential information for any particular application. This effort, together with closer cooperation with the State in the processing of applications, has enabled us to

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render more expeditious decisions on these applications and reduced the time required by banks to complete the application.

Bank examination is the heart of our supervisory program to promote the safety and soundness of the banking system. The FDIC will continue to exercise a strong bank examination function. In 1981 we expect to conduct 5,800 safety and soundness examinations.

Recent economic circumstances have created new and serious problems for thrift institutions, including the insured mutual savings banks which we supervise. Late last year we established an ongoing project team to monitor conditions in the thrift industry and develop strategies and policies for addressing the situation. We have increased our supervision of these institutions through increased examinations and visitations, more timely and thorough reporting of financial developments by the banks to the FDIC, and more frequent meetings and discussions with the trustees of those institutions experiencing difficulties. This has placed added burdens upon our resources; however, we are able to meet the challenge largely because of our efforts to develop a total supervisory program which has the built-in flexibility to handle such situations when they arise.

EXPERIENCE OF 1980

The year 1980 was marked by substantial turbulence in the nation's economy and credit markets. Output and employment declined substantially in some vital sectors of the economy. The housing and auto industries were particularly

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hard hit. Inflation, as measured by indexes of consumer and producer prices, continued to soar at double-digit rates. These developments in the economy contributed to instability in the financial sector, as reflected most notably in the movement of interest rates.

The pattern of interest rate changes last year was unprecedented in recent history, both with respect to the magnitude and frequency of change. The prime rate, for example, rose from 13.25 percent to a record 20 percent, declined to less than 11 percent and ended the year at a new record level of 21.5 percent. These wide fluctuations and the unprecedented levels to which interest rates rose imposed stresses on the economy and the banking industry. The high interest rates contributed to a substantial growth in money market mutual funds during the year.

During the first half of this year, we have seen a slight reduction in the inflation rate and, during the second quarter, some evidence of a slowing in the rate of economic activity. Nevertheless, interest rates have remained at or near record levels, thereby providing an uncomfortable environment for some commercial banks and most thrift institutions.

MUTUAL SAVINGS BANKS

The mutual savings banks problem is centered in New York City but not limited to that city. Higher interest rates have significantly increased the cost of savings bank deposits. While yields on savings bank earning assets have risen, they

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have done so much more slowly than deposit costs. Assets are heavily concentrated in long-term, fixed-rate mortgages and bonds which turn over slowly. The problem has been exacerbated by slow deposit growth resulting from such causes as a low personal savings rate and increased competition from money market funds and market instruments. These conditions have severely limited savings banks' ability to acquire higher-yielding assets. Indeed, many savings banks are forced to use funds generated from mortgage amortization payments to finance deposit outflows and operating losses with little left over to invest in higher yielding assets available in today's market.

Last year, FDIC-insured mutual savings banks in the aggregate lost money. The loss amounted to about 0.17 percent of average assets compared with net income of about 0.45 percent of assets in 1979 and 0.59 percent in 1978. The loss was not evenly spread throughout the country. New York City savings banks, which account for about 40 percent of the deposits of FDIC-insured thrift institutions, lost about 0.62 percent of average assets last year. However, the rest of the industry had net income of about 0.17 percent. The weaker performance of many of the New York City savings banks reflects a combination of factors, the most significant being inflation and the resultant high interest rates, but also including past restrictions on permissible lending, past restrictive usury ceilings, unfavorable State and city tax treatment, relatively low mortgage activity, and a high degree of competition from large money center institutions and money market funds.

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During the first half of this year, savings bank earnings have further deteriorated -- that is, losses have increased. The FDIC has been collecting monthly income and deposit data from those savings banks with deposits of $500 million or more in order to monitor their performance closely. These 79 institutions account for about 75 percent of all savings bank deposits. During the first five months of 1981, only 14 of the large savings banks had positive net income and by May only 11 had positive operating income. Overall, these 79 savings banks lost a net $400 million even after taking account of Federal tax credits and security gains from very selective asset sales. If this loss were annualized, it would amount to 0.82 percent of assets. Savings banks in New York City accounted for much of the loss. On an annualized basis, their loss for the first five months of this year was over 1.3 percent of assets and for the month of May, the annualized loss was 1.55 percent of assets. It should be noted that smaller savings institutions not included in our monthly survey generally are doing better than the larger institutions though their performance has also deteriorated this year.

Interest rate and deposit flow data for June suggest that savings bank performance that month was at least as bad as in May. Savings bank earnings during the balance of the year will be importantly affected by interest rates. If rates remain constant, or if they decline only slightly, deposit costs will continue to rise as low-cost passbook accounts and

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7-1/2 and 7-3/4 percent certificates shift into higher-cost deposits or leave institutions altogether.

There still remains an extremely large pool of mutual savings bank capital available to sustain the industry for a considerable period of years, although individual institutions may well be troubled earlier if the present inflation and interest rate environment continues.

If interest rates decline quickly and markedly and remain low for a sustained period, most savings banks should be able to adjust portfolio returns to bring them into line with the market and make appropriate adjustments to attain a profitable position. Savings banks then would have the opportunity to take advantage of the broadened lending powers authorized under the Depository Institutions Deregulations and Monetary Control Act of 1980 and State laws to reduce their exposure to future interest swings. Thus far, prevailing financial market conditions and other factors have made it difficult for savings banks to take advantage of these broadened powers to any significant degree. If unfavorable conditions persist in financial markets for a prolonged period, then some savings banks are likely to need assistance if they are to continue to operate.

Since we cannot predict the future course of interest rates or other variables, we are unable to predict, as you requested, if any large savings banks face the prospect of failure or when such a prospect might begin to materialize.

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CONDITION OF INSURED COMMERCIAL BANKS

Despite the conditions that prevailed in financial markets throughout last year and the sharp drop in economic activity during the second quarter of the year, most commercial banks performed quite well in 1980. In the aggregate, net income and assets grew by 10 percent.

Despite our earlier concerns and those of many financial market observers regarding the position of smaller commercial banks, most small banks -- those with deposits of less than $100 million -- performed quite well in 1980.

We should note, however, that smaller banks have experienced a sizable transfer of funds from low-cost deposits to money market certificates and other more expensive deposits. Also, many small banks hold large amounts of mortgages and other long-term assets that would prevent them from raising their return on assets sufficiently in the short run to compensate for increased money costs. Apparently, however, this was not a problem in 1980.

For 1981, in addition to the rising costs of time and savings deposits, universal NOW accounts have also put pressure on bank costs. Smaller banks, with a larger concentration in retail deposits, seem more vulnerable to the increased costs and competition associated with NOW accounts. Another factor that has become increasingly important is competition from money market funds. Growth in retail time and savings deposits at commercial banks has slowed markedly this year, although not as dramatically as at thrifts, and competition

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from money market funds undoubtedly played a very important role in this development. Again, small banks with a greater emphasis on retail deposits may be more affected by this development.

In assessing developments thus far in 1981, we are handicapped by the availability of data, particularly for small banks. We are just beginning to process mid-year reports which should give us a better reading on their performance thus far in 1981. We are able to make some general observations based on income reports for the first quarter of 1981, which are filed by banks with assets of $300 million and over, and from published financial statements of banks, although these tend to be more available for the larger, publicly traded institutions.

First quarter data for the larger banks suggest that they were able to maintain net interest margins despite the rising costs of deposits. Returns on assets appear to approximate those realized in 1980 and published financial reports indicated that year-to-year earnings improvement between the first quarter of 1980 and the first quarter of 1981 approximated increases in assets.

For the second quarter of 1981, we look for a mixed performance for larger commercial banks. Comparing the second quarter of 1981 to the second quarter of 1980 may well show almost as many minuses as pluses. To some degree, this appears to reflect the fact that the second quarter of 1980 was a very strong quarter for large banks. When interest rates declined rapidly in the second quarter of 1980, reduced money costs

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actually widened interest margins at the money center banks. That appears to be showing up now in the form of unfavorable year-to-year comparisons.

As I indicated, we do not have as precise a reading on the performance of smaller commercial banks. Weaker deposit performance and some of the other developments that I have mentioned suggest that 1981 may not be quite as good a year for small banks as 1980. However, the information we have received, including the comments from our various regional offices, indicates that most small banks continue to be performing well. They apparently have been less vulnerable to interest rate risk, at least as a group, than anticipated.

We must remain alert to any continued instability in the economy, further competition for bank and thrift funds from the unregulated sector of the financial markets, and the weakened condition of other types of financial institutions which will test the capabilities of bank managers, regulators, and legislators throughout the year.

CONCLUSION

The banking scene today is fast-changing. We at the FDIC remain firm in our commitment to the people in monitoring the safety and soundness of the banking system. We believe that the situation today warrants the revision in the tools of our trade that we have outlined. We urge your quick action.

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97th Cong.
1st Sess.

July 14, 1981

TEXT OF LEGISLATION TO ACCOMPANY STATEMENT ON STATE OF BANKING INDUSTRY AND FDIC ABILITY TO HANDLE PROBLEMS

A BILL

To provide flexibility to the Federal Deposit Insurance Corporation to deal with financially distressed banks.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

ASSISTANCE TO INSURED BANKS

SEC. 1. Section 13(c) of the Federal Deposit Insurance Act (12 U.S.C. 1823(c)) is amended to read as follows:

"(c)(1) In order to reopen a closed insured bank or, when the Corporation has determined that an insured bank is in danger of closing, in order to prevent such closing, the Corporation, in the discretion of its Board of Directors, is authorized to make loans to, or purchase the assets of, or make deposits in, such insured bank, upon such terms and conditions as the Board of Directors may prescribe, when in the opinion of the Board of Directors the continued operation of the bank is essential to provide adequate banking service in the community.

"(2) Whenever severe financial conditions exist which threaten the stability of a significant number of insured banks, the Corporation, in the discretion of its Board of Directors, is authorized to make loans to, or purchase the assets of, or make deposits in, any insured bank so threatened, upon such terms and conditions as the Board of Directors may prescribe, if it is probable such action will substantially reduce the risk of loss or avert a threatened loss to the Corporation.

"(3) Any loans and deposits made pursuant to the provisions of this paragraph may be in subordination to the rights of depositors and other creditors.".

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PURCHASES OF INSURED BANKS

SEC. 2. (a) Section 13(e) of the Federal Deposit Insurance Act (12 U.S.C. 1823(e)) is amended to read as follows:

"(e)(1) Whenever in the judgment of the Board of Directors such action will reduce the risk of loss or avert a threatened loss to the Corporation and will facilitate a merger or consolidation of an insured bank with another insured depository institution or will facilitate the sale of the assets of an open or closed insured bank to and assumption of its liabilities by another insured depository institution, the Corporation may, upon such terms and conditions as it may determine, make loans secured in whole or in part by assets of an open or closed insured bank, which loans may be in subordination to the rights of depositors and other creditors, or the Corporation may purchase any such assets or may guarantee any other insured depository institution against loss by reason of its assuming the liabilities and purchasing the assets of an open or closed insured bank. Any insured national bank or District bank, or the Corporation as receiver thereof, is authorized to contract for such sales or loans and to pledge any assets of the bank to secure such loans.

(2)(A) Whenever an insured bank that had total assets equal to or greater than 0.12 percent of aggregate assets in domestic (U.S.) offices of insured banks (as determined from the most recently compiled Reports of Condition filed by insured banks) is closed and the Corporation is appointed receiver, then, the Receiver may, in its discretion and upon such terms and conditions as it may determine, and with such approvals as may elsewhere be required by any State or Federal courts and supervisory agencies, sell assets of the closed bank to and arrange for the assumption of the liabilities of the closed bank by an insured depository institution located in the same State as that in which the closed bank was chartered but owned by an out-of-State bank or bank holding company. Notwithstanding subsection (d) of Section 3 of the Bank Holding Company

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Act of 1956 or any other provision of law, State or Federal, the acquiring institution is authorized to be and shall be operated as a subsidiary of the out-of-State bank or bank holding company; except that an insured bank may operate the assuming institution as a subsidiary only if specifically authorized by law other than this paragraph.

(B) In determining whether to arrange a sale of assets and assumption of liabilities of a closed insured bank under the authority of this paragraph (2), the Receiver may solicit such offers as is practicable from any prospective purchasers it determines, in its sole discretion, are both qualified and capable of acquiring the assets and the liabilities of the closed bank.

(i) If, after receiving offers, the highest acceptable offer is from a subsidiary of an out-of-State bank or bank holding company, the Receiver shall permit the highest acceptable offeror of any existing in-State insured depository institutions and subsidiaries of in-State bank holding companies to submit a new offer for the assets and liabilities of the closed bank. If this institution reoffers a greater amount than the previous highest acceptable offer, then the Receiver shall sell the assets and transfer the liabilities of the closed bank to that institution.

(ii) If there is no acceptable offer received from an existing in-State depository institution or subsidiary of an in-State bank holding company, or if there is no reoffer greater than the highest acceptable offer, then the Receiver shall permit the highest acceptable offeror of the subsidiaries of the

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insured banks chartered in States adjoining the State in which the closed bank was chartered and bank holding companies whose banking subsidiaries' operations are principally conducted in States adjoining the State in which the closed bank was chartered (if its offer was not the highest received by the Receiver) to make a new offer for the assets and liabilities of the closed bank. If this subsidiary reoffers a greater amount than the previous highest acceptable offer then the Receiver shall sell the assets and transfer the liabilities of the closed bank to that institution.

(iii) If no offer under subparagraphs (i) or (ii) is received which exceeds the original highest acceptable offer, then the Receiver shall sell the assets and transfer the liabilities of the closed bank to the highest acceptable offeror.

(C) In making a determination to solicit offers under subparagaraph (B), the State bank supervisor of the State in which the closed insured bank was chartered shall be consulted. The State bank supervisor shall be given a reasonable opportunity, and in no instance a period of less than twenty-four hours, to object to the use of the provisions of this paragraph (2). If the State supervisor objects, the Receiver may use the authority of this paragraph (2) only by a unanimous vote of the Board of Directors. The Board of Directors shall provide to the State supervisor, as soon as practicable, a written certification of its determination.

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(D) The Receiver shall not make any sale under the provisions of this paragraph (2) — (i) which would result in a monopoly, or which would be in furtherance of any combination or conspiracy to monopolize or to attempt to monopolize the business of banking in any part of the United States; or (ii) whose effect in any section of the country may be substantially to lessen competition, or to tend to create a monopoly, or which in any other manner would be in restraint of trade, unless it finds that the anticompetitive effects of the proposed transaction are clearly outweighed in the public interest by the probable effect of the transaction in meeting the convenience and needs of the community to be served.

(E) Nothing contained in this paragraph (2) shall be construed to limit the Corporation's powers in paragraph (1) to assist a transaction under this paragraph.

(3) As used in this subsection -- (i) the term "Receiver" shall mean the Corporation when it has been appointed the receiver of a closed insured bank; (ii) the term "insured depository institution" shall mean an insured bank or an association or bank insured by the Federal Savings and Loan Insurance Corporation; (iii) the term "existing in-State insured depository institution" shall mean an insured depository institution that is chartered in the same State as the State in which the closed bank was chartered; (iv) the term "in-State bank holding company" shall mean a bank holding company whose banking subsidiaries' operations are principally conducted in the same State as the State in which the closed bank was chartered; and (v) the term "out-of-State bank or bank

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holding company" shall mean an insured bank having its principal place of banking business in a State other than the State in which the closed bank was chartered or a bank holding company whose banking subsidiaries' operations are principally conducted in a State other than the State in which the closed bank was chartered."

(b) The provisions of paragraph 2 of section 13(e) of the Federal Deposit Insurance Act shall cease to be effective five years from the date of its enactment. The expiration of the effectiveness of section 13(e)(2), however, shall have no effect on the continued legality of any sale or operation authorized while it was effective.

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AGREEMENTS DIMINISHING THE
RIGHTS OF THE CORPORATION

SEC. 3. Section 13 of the Federal Deposit Insurance Act is amended by adding at the end thereof the following new subsection:

"(h) No agreement which tends to diminish or defeat the right, title or interest of the Corporation in any asset acquired by it under this section, either as security for a loan or by purchase, shall be valid against the Corporation unless such agreement (1) shall be in writing, (2) shall have been executed by the bank and the person or persons claiming an adverse interest thereunder, (3) shall have been approved by the board of directors of the bank or its loan committee, and (4) shall have been, continuously, from the time of its execution, an official record of the bank."

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FDIC ASSESSMENTS

SEC. 4. The third sentence of section 7(d)(1) of the Federal Deposit Insurance Act (12 U.S.C. 1817(d)(1)) is amended --

(a) by striking out "and" the second place it appears; and

(b) by inserting before the period at the end thereof the following: "; and (4) any lending costs for the calendar year, which shall be the difference between the rate of interest earned, if any, from each loan made by the Corporation pursuant to section 13 after January 1, 1981 and the Corporation's average investment portfolio yield for the calendar year.".

THE BANK HOLDING COMPANY ACT OF 1956

SEC. 5. Section 3(d) of the Bank Holding Company Act of 1956 (12 U.S.C. 1842(d)) is amended by adding after the word "application" the following:

> "(except an application filed as a result of a transaction to be accomplished under section 13(e)(2) of the Federal Deposit Insurance Act (12 U.S.C. 1823(e)(2))".

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