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STATEMENT

UNNECESSARY COSTS OF FSLIC RECAPITALIZATION PROGRAM

September 14, 1987

The first issue of bonds to be sold by the newly established Financing Corporation to recapitalize the insolvent federal savings and loan insurance system will soon be coming to market. Analysts estimate that these bonds will carry interest rates as much as one percent over Treasury securities. This spread compensates bondholders for perceived risks that could be avoided if the Treasury were to finance the Federal Savings and Loan Insurance Corporation deficit directly. Based on the planned sale of $10 billion of these bonds at a one-percent spread, the additional cost of this indirect financing scheme would amount to $100 million per year.

While we believe that the federal government would not allow a default on these securities, the legislation establishing this program states that the bonds are not a full faith and credit obligation of the United States. Instead, investors are led to believe that they must rely on limited sources of repayment specified in the legislation.

Withholding an explicit federal guarantee has two apparent effects. First, it keeps the flow of funds to FSLIC out of the federal budget. Second, it places the formal burden for financing FSLIC wholly within the thrift industry.

However, as this Committee has stated in the past, the financial resources of the industry are not sufficient to fully cover the estimated losses in the savings and loan system, which are now estimated to exceed $40 billion. Thus, much of this burden will eventually be borne by the taxpayer, and the extra $100 million of annual interest on the bonds will increase the taxpayer's share.

We believe that $100 million per year is an excessive cost to pay for deferring recognition of the government's responsibility for meeting the losses incurred in the thrift industry. As such, it represents an inefficient use of the public's funds.