

**Shadow Financial
Regulatory Committee**

Administrative Office:
Mid America Institute
3220 South Harper Street
Suite 407
Chicago, Illinois 60615
(312) 493-9800

For information contact:
Paul M. Horvitz
(713) 749-1126

Statement of the Shadow Financial Regulatory Committee
on FSLIC Handling of Insolvent Thrift Institutions

November 13, 1987

Committee Members:

LAWRENCE CONNELL
Co-Chair
Prather, Seeger, Doolittle
& Farmer

GEORGE G. KAUFMAN
Co-Chair
Loyola University of Chicago

RICHARD C. ASPINWALL
Chase Manhattan Bank

GEORGE J. BENSTON
The University of Rochester

FRANKLIN R. EDWARDS
Columbia University

ROBERT A. EISENBEIS
University of North Carolina
at Chapel Hill

JOHN D. HAWKE, JR.
Arnold & Porter

PAUL M. HORVITZ
University of Houston

EDWARD J. KANE
Ohio State University

ROGER W. MEHLE
Royer, Shacknai & Mehle

ALLAN H. MELTZER
Carnegie-Mellon University

KENNETH E. SCOTT
Stanford Law School

The Shadow Financial Regulatory Committee is concerned about the continuing slow pace of the Federal Savings and Loan Insurance Corporation in resolving cases of insolvent S&L's. FSLIC has already received \$600 million in proceeds from the first sale of its recapitalization bonds and is in the process of acquiring additional resources to resolve a significant number of cases.

The Committee recognizes that deciding which institutions are the first to be closed or sold is difficult. Nevertheless, it is clear that the continued operation of insolvent institutions is in general costly to FSLIC because of (1) the exceptionally high operating expenses of the insolvent institution, (2) the premium rates of interest that must be paid by these institutions to attract deposits, and (3) the possibility that the insolvent institution may take excessive risk in the hopes of returning to solvency, particularly where it is still stockholder-controlled.

We are encouraged by the recent statement of Chairman Wall that FSLIC will resolve a case a week for the next year. We view that as a minimum goal -- cases should be resolved as rapidly as funds permit.

Part of the difficulty is the cumbersome nature of FSLIC procedures for acting on bids. These procedures have discouraged many potential bidders, who incur significant costs to prepare bids on cases that drag on without a decision. While a competitive bidding process may be desirable under the Garn-St Germain Act, we believe that substantial improvements are possible.

The Committee also notes the FHLBB's announcement of a year's delay in implementing GAAP accounting for all S&L's. Although this decision is not of crucial significance, since GAAP accounting itself has some unrealistic elements (such as treatment of goodwill as an asset and carrying restructured loans under FASB 15 at a value greater than fair market value), the Committee hopes that this delay in implementation of GAAP does not signal a return to regulatory attempts to paper over the extent of thrift problems by misleading accounting.

Such a policy would only work to the detriment of healthy institutions, as the market would be suspicious of all savings and loan financial statements. Rather, prompt resolution of the problems of insolvent savings and loans and accurate accounting will benefit the healthy institutions.