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BY THE COMPTROLLER GENERAL

Report To The Congress

OF THE UNITED STATES

Federal Banking Agencies Are Adequately Examining Net Worth Certificate Program Applications

The Garn-St Germain Depository Institutions Act of 1982 authorized capital assistance programs to savings and loan associations and savings banks--commonly called thrifts. The programs, which are administered by the Federal Home Loan Bank Board (the Bank Board) and the Federal Deposit Insurance Corporation (FDIC), are intended to increase the net worth (defined as an institution's assets less liabilities) of weakened thrifts, so that they can restructure and return to profitability. The act requires GAO to audit the programs and report to the Congress.

GAO's first report analyzed the programs' design and use of accounting principles. In this report, GAO describes the industry's performance and status of the programs during the first half of 1984 and discusses the Bank Board's and FDIC's examination and processing of applications for assistance.

While, as a whole, the thrift industry was profitable for the first half of 1984 and experienced moderate increases in its net worth, most thrifts receiving net worth certificate assistance reported losses and declining net worth. GAO's review of the programs' application process indicated that both the Bank Board and FDIC approved or disapproved applications in accordance with prescribed statutory and regulatory requirements.

UNITED STATES GENERAL ACCOUNTING OFFICE

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COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON D.C. 20548

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To the President of the Senate and the
Speaker of the House of Representatives

For the past several years, there has been national concern about the ability of the thrift industry--savings and loan associations and savings banks[1]--to operate in a high interest rate environment. In 1982, the Congress enacted the Garn-St Germain Depository Institutions Act of 1982 (Public Law 97-320) to help mitigate the industry's problems. The act was designed to help the thrift industry in two major ways. First, it authorized expanded investment and lending powers for thrifts so that they could restructure and improve the profitability of their operations. Second, it authorized the establishment of assistance programs to increase the net worth (defined as an institution's assets less liabilities) of weakened thrifts that might not otherwise survive long enough to use these new powers. The act also requires the GAO to semiannually audit these programs, known as net worth certificate programs, and report our findings to the Congress.

Implemented in December 1982, the net worth certificate programs are administered by two federal insurers of thrift institutions: the Federal Deposit Insurance Corporation and the Federal Home Loan Bank Board, with its subsidiary, the Federal Savings and Loan Insurance Corporation. The type of assistance provided by the programs involves an exchange of paper between an institution and its insurer. The institution gives the

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[1]Savings and loan associations (S&Ls) are chartered either by the state in which they operate or by the Federal Home Loan Bank Board (the Bank Board). All S&Ls chartered by the Bank Board are known as "federal" associations and are required by law to have their savings accounts insured by the Federal Savings and Loan Insurance Corporation (FSLIC). FSLIC insurance is optional for many state-chartered S&Ls, but the majority afford their savers this protection. Historically, savings banks have been chartered by states and operate under state banking laws. The Federal Deposit Insurance Corporation (FDIC) is the primary federal insuring agency for savings banks. However, some federally chartered savings banks are insured by the FSLIC.

insuring agency a capital instrument, called the "net worth certificate." In return, the agency gives back a promissory note of like amount. The certificate can be compared to a stock certificate, with the promissory note substituting for a cash payment for the stock. The promissory note and certificate are intended to increase the institution's assets and net worth, respectively. By increasing the net worth of institutions, regulatory procedures to liquidate or merge participants are forestalled, creating time for restructuring and returning to profitability. Once institutions return to profitability, they are required to redeem their net worth certificates from the applicable insurance agency.

This evaluation of the net worth certificate programs is our second. The first report analyzed the programs' design and use of accounting principles. In addition, it provided information on the industry's condition and the programs' status through December 31, 1983.[2] In this report, we summarize data on thrifts' net income and net worth performance in the first half of 1984 and on the status of assistance through June 30, 1984. We compare the financial performance of thrifts that received net worth certificate assistance to all federally insured thrifts. We also evaluate whether the Bank Board and FDIC consistently followed established legislative and regulatory requirements in processing and examining applications for assistance. Briefly, we found that:

--Collectively, federally insured thrifts, while faced with rising interest rates, were slightly more profitable during the first half of 1984 compared with the second half of 1983.

--While, as a whole, federally insured thrifts were profitable for the first half of 1984, most thrifts receiving net worth certificate assistance were still reporting losses and declining net worth as of June 30, 1984.

--Of the 26 FDIC-insured thrifts and the 74 FSLIC-insured thrifts that received assistance, none were liquidated, 6 were merged, and 1 was acquired by another thrift. FDIC granted $486 million in assistance; FSLIC, $113 million as of June 30, 1984.

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[2]Net Worth Certificate Assistance Programs: Their Design, Major Differences, and Early Implementation (GAO/GGD-85-8, Nov. 5, 1984).

--Both agencies examined thrifts' applications for assistance sufficiently to verify their accuracy and completeness. Each consistently acted upon the applications in accordance with prescribed statutory and regulatory requirements for their respective constituent institutions.[3]

With passage of the Monetary Control Act of 1980 and the Garn-St Germain Act of 1982, the Congress expressed its desire that thrift institutions, in order to become less vulnerable to rising interest rates, should restructure their asset portfolios by making shorter-term, more interest-sensitive loans and investments. Although the federally insured thrift industry reported a $1.1 billion net income in the first half of 1984, when interest rates were rising, some federal banking regulators nevertheless caution that the thrift industry remains vulnerable to rising interest rates.

OBJECTIVES, SCOPE, AND METHODOLOGY

The objectives of this study were to

--summarize both net income data of the thrift industry for the first half of 1984, and the status of the net worth certificate programs through June 30, 1984;

--compare net income and net worth levels for thrifts that received net worth certificate assistance to the levels for all federally insured thrifts; and

--evaluate the two federal insurers' processing of net worth certificate assistance applications in accordance with prescribed statutory and reporting requirements.

With regard to the last objective, in our first report on the net worth certificate programs we pointed out that the FDIC and the Bank Board, using the discretion granted them in the Garn-St Germain Act, had imposed different eligibility requirements and operating restrictions on their applicant institutions. We reported that, in general, the Bank Board's requirements for participation were more restrictive than those imposed by the FDIC. In this report, we determined whether the Bank

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[3]According to Federal banking agencies' records, since the time of our application process review through December 31, 1984, most of the net worth certificate applications received by the insurance agencies were from participating institutions seeking additional assistance. Since September 30, 1983, 32 thrift institutions were first-time applicants for net worth certificate assistance.

Board and FDIC were each adequately examining thrifts' net worth certificate assistance applications for completeness and accuracy and were acting upon them in a consistent manner in accordance with prescribed statutory and regulatory requirements for their respective constituent institutions.

Our work was performed between August 1983 and November 1984 at the FDIC and the Bank Board in Washington, D.C.; the Federal Home Loan Banks, as well as Bank Board district offices, in Atlanta, Chicago, New York City, and San Francisco; and the FDIC regional office in New York City. The agencies' field offices were selected for our audit because, at the time of our review, the majority of thrift institutions participating in the net worth certificate programs were located within their jurisdictions. For example, our fieldwork at FDIC was limited to its New York regional office. We limited our review in this way because 83 percent of the thrifts participating in FDIC's net worth certificate program were located in New York State during the period covered in our application process review, which was from program inception through September 30, 1983.

According to the Bank Board and FDIC records, a total of 157 net worth certificate assistance applications were received and fully processed by these agencies nationwide, from inception of the programs through September 30, 1983. To test whether the Bank Board and FDIC were each sufficiently and consistently examining thrifts to verify their eligibility in accordance with established legislative and regulatory requirements, we interviewed both headquarters and regional officials of both agencies and reviewed all applications received and fully processed by the regional offices we visited. We did not review applications which were in process as of September 30, 1983, the closing date of our review period. We reviewed all 109 applications which were fully processed by the regions we visited--68 applications by the Bank Board, and 41 by FDIC--as of September 30, 1983. The 109 applications consisted of 80 that were approved, 19 that were denied, and 10 that were withdrawn by the applicants. The 19 denials (1 by FDIC; 18 by the Bank Board), represent all denials made by the agencies as of the date of our review. (See app. VII.)

To be eligible for net worth certificate assistance, an institution must meet both the requirements set out under Title II of the Garn-St Germain Act and additional regulatory requirements established by the applicable federal bank insuring agency, FDIC or the Bank Board. Our review focused on those eligibility requirements considered most significant by the agencies (see app. VIII). Because we are not authorized to examine individual financial institutions' books and records, we could not verify the accuracy of data reviewed by the two agencies in making decisions to provide or deny assistance.

For each application, we assessed how the Bank Board and FDIC determined if the applicant satisfied the statutory and regulatory requirements governing eligibility. If the agencies' files lacked documentation on whether applicants met a specific requirement, we discussed the scope of the work with the appropriate agency officials.

Unless otherwise noted, data on the condition of the thrift industry and on the programs are current as of June 30, 1984. Except for the fact that we did not verify the accuracy of individual institutions' books and records, our review was conducted in accordance with generally accepted government auditing standards.

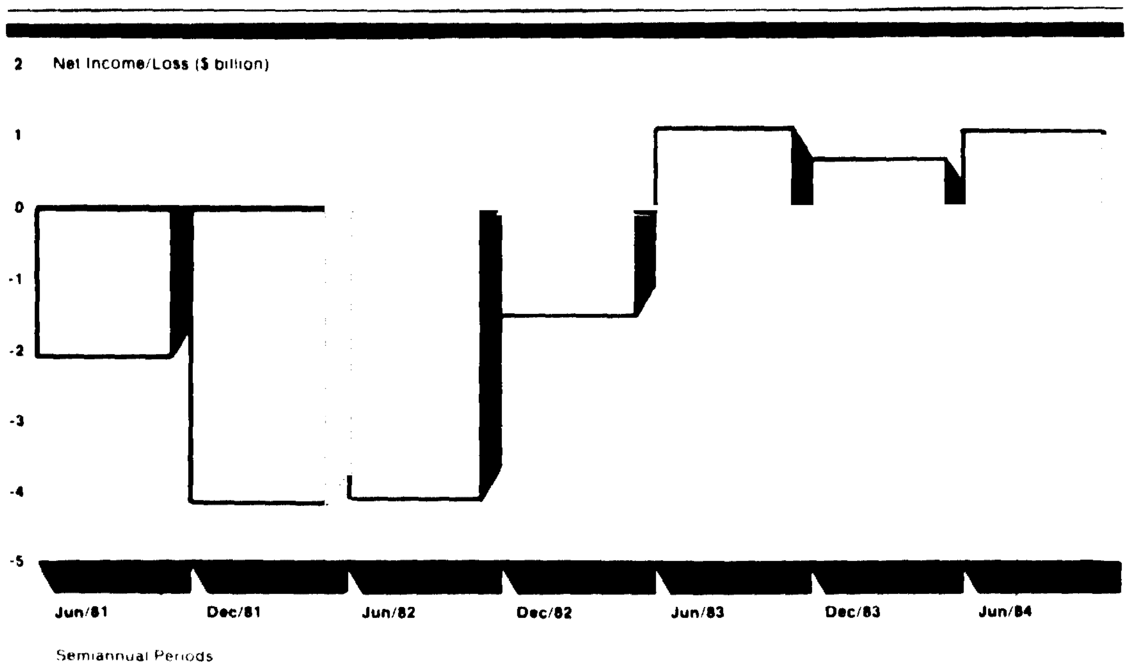
AGENCY COMMENTS

Both the FDIC and the Bank Board reviewed a draft of this report. Neither agency had any substantive comments, although they did point out some minor inaccuracies and items that needed to be clarified. We have revised the report to reflect their comments. (See apps. IX and X.)

FEDERALLY INSURED THRIFTS RETURN TO OVERALL PROFITABILITY IN FIRST HALF OF 1984

Federally insured thrifts collectively reported net income for the first half of 1984, although a sizable percentage of these thrifts continued to report losses during the period. Federally insured thrifts--both net worth certificate participants and all others--reported an aggregate net income for the first half of 1984 of $1.1 billion, up $0.4 billion from the second half of 1983. The graph on the following page shows semiannual operating results for all federally insured thrifts from 1981, when thrifts began to incur large losses, through the first half of 1984.

Semiannual Net Income/Loss
Federally Insured Thrifts



The percentage of FDIC-insured thrifts reporting losses for the first half of 1984 fell to 21 percent from 23 percent for all of 1983. FSLIC-insured thrifts report quarterly; 38 percent of FSLIC-insured institutions reported losses in the first quarter of 1984, and 24 percent of FSLIC-insured institutions reported losses in the second quarter of 1984. The average of these figures, 31 percent, is 4 percentage points lower than the percentage for all of 1983.[4]

The thrift industry was able to increase profitability during a period of rising short-term interest rates. Interest rates on 6-month Treasury Bills (an index for the industry's borrowing costs) averaged 9.75 percent for the first half of

[4]Appendix I is a table showing net income/loss of federally insured thrifts from 1981 through the first half of 1984.

1984. This average rate was 0.61 percentage points higher than the comparable average for the last half of 1983.[5]

One reason for the improved earnings in 1984 is that the thrift industry was able to increase the margin between its mortgage portfolio yield and its cost of funds (interest and dividends paid on deposits) despite rising interest rates. Commenting on this, a Bank Board member stated that the industry is moving to a margin of 200 basis points--or 2 percent--between its earnings on assets and its cost of funds. This margin was typical for the industry before the interest rate increases of the late 1970's and early 1980's. He noted further that FSLIC-insured thrifts are building a 250 to 260 basis point margin on their newly acquired assets.[6]

Since the time that our review was completed, 1984 year end profitability data has become available for FSLIC-insured thrifts. In 1984, FSLIC-insured thrifts earned $1.7 billion; however, one in four institutions reported incurring a net loss.

INSTITUTIONS RECEIVING ASSISTANCE CONTINUE TO HAVE LOSSES AND DECLINING NET WORTH

While, as a whole, federally insured thrifts were profitable for the first half of 1984, those thrifts that have received net worth certificate assistance since December 1982 were, in the aggregate, reporting losses and declining net worth. Of the 98 thrift institutions with net worth certificate assistance outstanding as of June 30, 1984, 63 (12 FDIC-insured and 51 FSLIC-insured institutions) were program participants since program inception in December 1982. These 63 institutions, in the aggregate, incurred about $110.5 million in net operating losses for the first half of 1984, compared to a combined net income for the same period of $1.1 billion for all federally insured thrift institutions. (See app. I for historical data on net income/loss of thrift institutions.) Despite the additional net worth provided by the program, the aggregate net worth of the 12 FDIC participants and the 51 FSLIC participants decreased 19.8 percent and 8.8 percent, respectively,

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[5]Average rates on 6-month Treasury Bills for semiannual periods from 1981 through the first half of 1984 are shown in appendix II.

[6]Comments by Donald Hovde, Board Member of the Federal Home Loan Bank Board, at the U.S. League of Savings Institutions' annual convention in Washington, D.C., on October 30, 1984.

through the first half of 1984. For the same institutions, the aggregate net worth, without assistance, would have decreased 83.0 percent and 23.2 percent, respectively.[7]

NET WORTH CERTIFICATE ASSISTANCE AS OF JUNE 30, 1984

From the inception of FDIC's net worth certificate program through June 30, 1984, FDIC has exchanged its promissory notes for net worth certificates totaling $487,377,189 from 26 savings banks. The amount of promissory notes and certificates outstanding as of June 30, 1984, is less than the total amount exchanged. Two savings banks retired certificates totaling $1,840,900 as a result of mergers. After deducting the retired certificates, FDIC had net worth certificates of $485,536,289 outstanding from 24 savings banks. The outstanding net worth certificates ranged from a low of $524,090 to a high of $141,400,000, with the median at $4,993,000. Geographically, FDIC holds certificates from 24 thrifts: 20 located in New York, 3 in Pennsylvania, and 1 in New Jersey (see app. V).

In addition to the two mergers mentioned above, there were two other mergers of savings banks with outstanding net worth certificates. However, for these mergers, the outstanding certificates were not retired but were assumed by the surviving institutions.

None of the 26 thrifts which received net worth certificate assistance from FDIC were liquidated as of June 30, 1984. Consequently, FDIC has made no cash payments under its program. FDIC only makes a cash payment under its program when a thrift is liquidated. At that time, FDIC's promissory note, which is exchanged for the thrift's net worth certificate, becomes payable to satisfy the claims of the general creditors of the liquidated thrift.

As of June 30, 1984, 74 institutions had chosen to participate in the Bank Board's net worth certificate program by exchanging net worth certificates for Bank Board promissory notes totaling $113,000,000. The promissory notes and net worth certificates exchanged between the Bank Board and these institutions ranged from a low of $25,000 to a high of $20,000,000, with a median exchange of $475,000. The institutions were located in 24 states, as shown in appendix VI.

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[7]Comparisons of the net worth of the 12 FDIC and 51 FSLIC program participants with all FDIC and FSLIC thrifts from 1982 to the first half of 1984 are shown in appendices III and IV.

Because none of the institutions receiving assistance have been liquidated, the Bank Board, like FDIC, has not made any cash payments to the institutions' general creditors. However, two institutions merged and a third was acquired by another thrift institution. The net worth certificates for these three institutions were retained by the surviving institutions; none were retired.

EXAMINATION OF NET WORTH CERTIFICATE APPLICATIONS MEETS LEGISLATIVE AND REGULATORY CRITERIA

Title II of the Garn-St Germain Act provides specific eligibility criteria that institutions must meet to obtain assistance and, at the same time, allows the Bank Board and FDIC to use their discretion in prescribing additional eligibility requirements. While providing this discretion, the Congress expressed its intent that each agency was not to treat "similarly situated institutions" differently.[8] Given the act's specific eligibility criteria and Congress' concern for consistency, we reviewed the Bank Board's and FDIC's programs to determine whether each agency was consistently applying its own eligibility requirements in granting thrifts net worth certificate assistance. According to our review of 109 applications (80 approved, 19 denied and 10 withdrawn), the Bank Board and FDIC thoroughly verified the accuracy and completeness of the applications; furthermore, they based their decisions on prescribed statutory and regulatory eligibility criteria.

Under both agencies' programs, much of the responsibility for deciding whether an institution is entitled to receive assistance and in what amount rests with the agencies' field offices. The Bank Board has delegated the authority for deciding on applications to supervisory agents of the District Federal Home Loan Banks in consultation with Bank Board District

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[8] House of Representatives Conference Report No 97-899, (p. 86) and Senate Conference Report No. 97-641, (p. 86) on the Garn-St Germain Depository Institutions Act of 1982.

Directors.[9] In addition, the Bank Board's Washington staff reviews the applications for accuracy and completeness and prepares and issues the FSLIC promissory note to the institution. At FDIC, decisions to grant or deny assistance rest with headquarters and are based upon recommendations made by FDIC regional directors.[10]

In January 1983, each agency issued guidelines to assist its field offices in processing net worth certificate applications. These guidelines helped ensure the uniform processing of applications. Both agencies require their field offices to verify the accuracy and completeness of the data on which assistance is being sought. The field offices verify application data either by conducting examinations at the applicant institution's place of business or by relying on a recently completed bank examination. After application data are verified as accurate and complete, examiners determine whether the institution meets the act's eligibility requirements as well as additional program eligibility requirements established by each agency (see app. VIII).

For the 80 applications that were approved for assistance in the regions we visited, the agencies conducted sufficient work, in our judgment, to ascertain that the applications met each statutory and regulatory requirement governing eligibility. For all 80 approved applicants, the Bank Board and FDIC conducted special net worth certificate examinations or relied on a recent examination to verify the applications' accuracy and completeness. Similarly, for the 19 applicants that were denied assistance, the agencies did sufficient work to ascertain that the applicant did not meet one or more requirements for eligibility. Further, the denials were generally reviewed at a high

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[9]There are 12 Federal Home Loan Banks (called district banks) located nationwide that are owned by, and serve as a central credit bank for, member thrift institutions. Officers of the 12 district banks are designated as agents of the Bank Board. Known as supervisory agents, they represent the Bank Board to member thrift institutions and act on behalf of the Bank Board. In addition, the Bank Board has examiners organized in 12 autonomous districts corresponding to the district banks. The 12 District Directors are responsible for all examinations of thrifts. The District Directors work closely with the supervisory agents.

[10]FDIC has 12 regional offices responsible for supervising and examining approximately 15,000 commercial banks and about 300 savings banks. Only FDIC's New York and Philadelphia regional offices are currently involved in the net worth certificate program.

management level within both agencies. The most frequent reasons for denying assistance were

--the thrifts not having at least a 0.5 percent net worth-to-asset ratio after considering the effect of net worth certificate assistance (a statutory eligibility requirement);

--the thrifts not submitting an application within the filing deadline (a regulatory eligibility requirement);

--the existence of a pending merger offer, which would reduce or eliminate the need for net worth certificate assistance (a regulatory eligibility requirement); and

--the thrifts not having a net worth-to-asset ratio of 3 percent or below after the agency disallowed operating losses attributable to mismanagement (a statutory eligibility requirement).

According to our review of 10 withdrawn applications, net worth certificate applicants voluntarily withdrew their applications for various reasons, including reluctance to agree to the operating terms and conditions required by the Bank Board or FDIC as a condition for assistance.

In summary, we saw no indications of either agency departing from established statutory and regulatory eligibility criteria. Thus, we concluded that each agency was consistently applying its own eligibility requirements in granting thrifts net worth certificate assistance.

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Copies of this report are being sent to the Director, Office of Management and Budget; the Chairman, Federal Home Loan Bank Board; the Chairman, Federal Deposit Insurance Corporation; and interested members and committees of the Congress.

Charles A. Bowsher

Comptroller General
of the United States

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ABBREVIATIONS

FDIC	Federal Deposit Insurance Corporation
FSLIC	Federal Savings and Loan Insurance Corporation
GAO	General Accounting Office
NWC	net worth certificate
S&L	savings and loan association
T-Bill	Treasury Bill
the Bank Board	Federal Home Loan Bank Board

Net Income/Loss of Federally Insured Thrifts from January 1981 Through June 1984

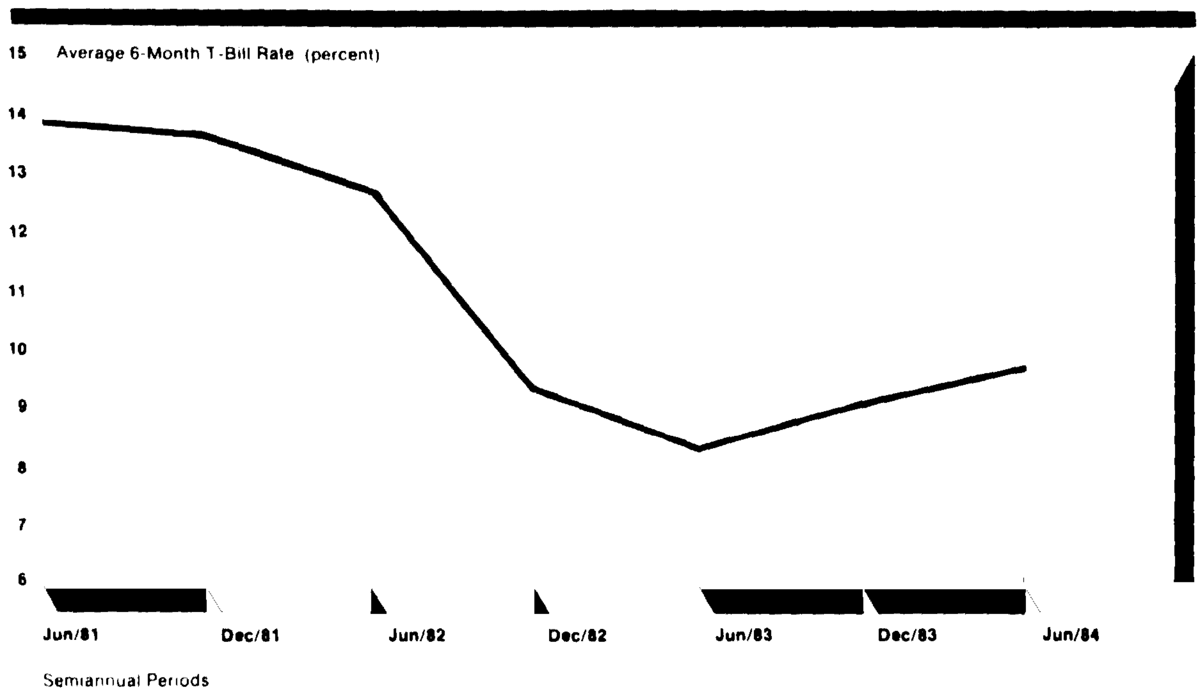
Semiannual period	FDIC-insured savings banks		FSLIC-insured institutions		Federally insured (FDIC and FSLIC) thrifts	
	Number	Net income ($ millions)	Number	Net income ($ millions)	Number	Net income ($ millions)
1st half 1981	336	-519	3951	-1517	4287	-2036
2nd half 1981	331	-929	3779	-3132	4110	-4061
1st half 1982	325	-762	3573	-3284	3898	-4046
2nd half 1982	315	-467	3343	-994	3658	-1461
1st half 1983	302	50	3248[a]	1089	3550	1139
2nd half 1983	294	-179	3183[a]	916	3477	737
1st half 1984[b]	292	139	3177[a]	984	3469	1123

[a]Prior to 1983, substantially all FSLIC-insured institutions were savings and loan associations (S&Ls). However, since 1983, some FSLIC-insured S&Ls have converted to savings banks but retained FSLIC insurance. According to a Bank Board official, this has occurred, in part, because of the favorable federal tax treatment available to savings banks with high housing related loans and the public image value associated with having the word "bank" in an institution's name. For the periods indicated below, FSLIC-insured institutions were composed of the following:

	Savings banks	S&Ls
1st half 1983	87	3161
2nd half 1983	143	3040
1st half 1984	180	2997

[b]Included in the figures for this semiannual period are 63 institutions (51 FSLIC-insured and 12 FDIC-insured institutions) with net worth certificate assistance outstanding since program inception. Also, these 63 institutions have incurred $110.5 million ($22.9 million for FSLIC net worth certificate (NWC) participants and $87.6 million for FDIC NWC participants) in net operating losses.

Average Semiannual U.S. T-Bill Rate
January 1981 Through First Half, 1984



Sources: Federal Reserve Bulletins dated January 1982, January 1983, January 1984, and July 1984.

Net Worth for All FDIC-Insured Savings Banks Compared to 12 FDIC NWC Savings Banks for Year End 1982 and First Half 1984

	Year end 1982 ($ millions)	First half 1984 ($ millions)	Percent change
Net worth			
All FDIC-insured savings banks	7,433	8,470	13.9
NWC savings banks[a]	557	447	-19.8
Net worth (without NWC assistance)			
All FDIC-insured savings banks	7,258	8,014	10.4
NWC savings banks[a]	401	68	-83.0

[a]Includes only those 12 FDIC-insured savings banks with NWC assistance outstanding as of June 30, 1984, and which have participated in FDIC's program since its inception in December 1982.

Regulatory Net Worth[a] for All FSLIC-Insured Institutions
Compared to
51 FSLIC-Insured NWC Institutions
for Year End 1982 and First Half 1984

	Year end 1982 ($ millions)	First half 1984 ($ millions)	Percent change
Regulatory net worth			
All FSLIC-insured institutions	25,386	35,491	39.8
NWC institutions	260	237	- 8.8
Regulatory net worth (without NWC assistance)			
All FSLIC-insured institutions	25,312	35,378	39.8
NWC institutions[b]	211	162	-23.2

[a]This is the sum of all reserve accounts, retained earnings, permanent stock, and any other nonwithdrawable accounts of an insured institution. In November 1982, the Bank Board changed the term "net worth" to "regulatory net worth" to include, in addition to the items previously mentioned, appraised equity capital and amounts of net worth certificates. Appraised equity capital is the difference between the appraised fair market value and the net book value (cost at acquisition less depreciation, where applicable) of an institution's office land, buildings, and improvements. FSLIC-insured savings institutions are permitted to include these items in financial reports which are submitted to the Bank Board.

[b]Includes only those 51 FSLIC-insured institutions with net worth certificate assistance outstanding as of June 30, 1984, and which have participated in the Bank Board's net worth certificate program since its inception in December 1982.

FDIC's Promissory Notes and Net Worth Certificates Outstanding, by State, As of June 30, 1984

Location	Number of savings banks	Amount of notes and certificates outstanding[a]
New York City	12	$436,689,937
Other New York State	8	13,170,547
All New York State	20	$449,860,484
Pennsylvania	3	31,105,005
New Jersey	1	4,570,800
Total	24	$485,536,289

[a]Amounts shown represent NWC assistance actually granted to participating institutions and still outstanding as of June 30, 1984.

The Bank Board's Promissory Notes and Net Worth Certificates Outstanding, by State, As of June 30, 1984

State	Number of institutions	Amount of notes and certificates outstanding[a]
California	2	$ 1,125,000
Georgia	3	2,000,000
Illinois	15	18,175,000
Indiana	3	1,625,000
Iowa	2	1,625,000
Kansas	2	575,000
Kentucky	1	975,000
Louisiana	3	775,000
Maryland	1	75,000
Massachusetts	1	150,000
Michigan	2	1,075,000
Minnesota	1	300,000
Mississippi	1	400,000
Missouri	4	2,350,000
Montana	1	175,000
Nebraska	3	7,275,000
New Jersey	8	6,425,000
New York	14	56,200,000
North Carolina	1	1,225,000
Ohio	1	3,800,000
Rhode Island	1	825,000
Texas	2	1,550,000
Virginia	1	2,775,000
Wisconsin	1	1,525,000
Total	74	$113,000,000

[a]Amounts shown represent NWC assistance actually granted to participating institutions and still outstanding as of June 30, 1984.

GAO Review of
Net Worth Certificate Applications
Processed by the Bank Board from Program
Inception Through September 30, 1983

	Applications			
	Approved	Denied	Withdrawn	Total
Total applications Bank Board processed	73	18	17	108
No. of applications GAO reviewed	43	18	7	68
Percent applications GAO reviewed	59	100	41	63

GAO Review of
Net Worth Certificate Applications
Processed by FDIC from
Program Inception Through
September 30, 1983

	Applications			
	Approved	Denied	Withdrawn	Total
Total applications FDIC processed	44	1	4	49
No. of applications GAO reviewed	37	1	3	41
Percent applications GAO reviewed	84	100	75	84

Eligibility Criteria GAO Examined In Reviewing Net Worth Certificate Applications

Statutory requirements that FSLIC- and FDIC-insured thrifts must meet:

--maximum net worth is 3 percent;

--operating losses were incurred in the two prior quarters;

--losses were not due to mismanagement, speculation, or excessive operating expenses;

--all regulatory requirements must be obeyed;

--minimum net worth after aid is 0.5 percent; and

--at least 20 percent of investment portfolio is in residential mortgages or securities backed by such mortgages.

Regulatory requirements that FSLIC-insured thrifts must meet:

--appraised equity capital is fully included in net worth;

--at least 6 months remain to insolvency after exchange of net worth certificates;

--a business plan must be submitted; and

--a merger that would reduce the need for assistance is not available.

Regulatory requirements that FDIC-insured thrifts must meet:

--senior management contracts longer than 1 year must be terminated;

--severance payment plans exceeding 6 months' salary must be rescinded; and

--a business plan must be submitted.

FEDERAL DEPOSIT INSURANCE CORPORATION, Washington, D.C. 20429

OFFICE OF DIRECTOR · DIVISION OF BANK SUPERVISION

April 3, 1985

Mr. William J. Anderson
Director
General Government Division
United States General Accounting Office
Washington, D.C. 20548

Dear Mr. Anderson:

This responds to your letter of March 20, submitting for our review and comment your draft report entitled, "Federal Banking Agencies Are Adequately Examining Net Worth Certificate Program Applications." The report discusses primarily the Federal Deposit Insurance Corporation's and the Federal Home Loan Bank Board's handling of thrifts' applications for capital assistance under Title II of the Garn-St Germain Depository Institutions Act of 1982.

We note the report concludes that both the Federal Deposit Insurance Corporation and Federal Savings and Loan Insurance Corporation have been following established statutory and regulatory eligibility criteria in granting net worth certificate assistance to thrifts and that the report contains no recommendations to either agency.

We are pleased to learn of the GAO's conclusions and have no comment other than to point out several technical inaccuracies. Footnote 10 on page 10 of the report states that the FDIC has six Regional Offices and only the New York Regional Office is currently involved in the net worth assistance program. In fact, the FDIC still has 12 Regional Offices and both our New York and Philadelphia Regional Offices are currently involved in the net worth assistance program. The GAO should be aware as well that in August 1984 the FDIC issued (see GAO Note 1) in net worth certificates to the (see GAO Note 1) in New York City and permitted the bank to back date the certificates to June 30, 1984. Recognition of the June 30 date would affect the totals of FDIC assistance reflected on pages 2 and 8 and in Appendix V of the report.

Sincerely,

Robert V. Shumway
Director

GAO Note 1: Information on an open bank was deleted pursuant to 31 U.S.C. 714(c)(1), which prohibits disclosure in a GAO report of any information identifying specific customers of banks or specific open banks or bank holding companies, except as otherwise provided in that section.

GAO Note 2: Page references have been changed to correspond to page numbers in the final report.

Federal Home Loan Bank Board

1700 G Street, N.W.
Washington, D.C. 20552
Federal Home Loan Bank System
Federal Home Loan Mortgage Corporation
Federal Savings and Loan Insurance Corporation

EDWIN J. GRAY
CHAIRMAN

April 23, 1985

Mr. William J. Anderson
Director
General Government Division
United States General Accounting Office
Washington, D.C. 20548

Dear Mr. Anderson:

Thank you for the opportunity to review the draft of your report entitled "Federal Banking Agencies Are Adequately Examining Net Worth Certificate Program Applications". I am pleased to note that the report concluded that the Bank Board is consistently applying its own eligibility requirements in granting Net Worth Certificate assistance, and that there are no indications that the Bank Board has departed from established statutory and regulatory eligibility criteria. I am also pleased that the draft report did not contain any adverse comments concerning the Bank Board's administration of its Net Worth Certificate program.

Review of the draft report disclosed several minor items that I believe should be clarified in the final report. First, page 2 of the report states that the FSLIC provided $113 million in Net Worth Certificate assistance as of June 30, 1984. This amount represents assistance actually granted to participating institutions through June 30, 1984, and does not include assistance for the semiannual period ended that date.

Also, the last paragraph on page 9 states: "The Bank Board has delegated the authority for deciding on applications to (S)upervisory (A)gents of the District Federal Home Loan Banks in consultation with Bank Board District Directors". While this is true, I believe it would be appropriate to add that all Net Worth Certificate applications are reviewed by the Bank Board's Washington staff for accuracy and completeness, and that the FSLIC notes are prepared and issued to participating institutions by the Washington headquarters.

GAO Note: Page references have been changed to correspond to the page numbers in the final report.

APPENDIX X

In addition, the first paragraph on page 10 states: "(E)xaminers determine whether the institution meets the act's eligibility requirements as well as additional program eligibility requirements established by each agency". In the case of the Bank Board, the final determination as to whether an institution has met all statutory and regulatory eligibility requirements is made by the Supervisory Agent in consultation with the District Director.

Finally, footnote number 6 on page 7 states that Mr. Donald Hovde is a member of the Board of Directors of the Federal Home Loan Bank Board. However, Mr. Hovde's proper title is "Board Member"; the Bank Board does not have a "Board of Directors" as such.

We appreciate this opportunity to provide our comments, and, if you have any questions or need additional information, please let us know.

Sincerely,

Edwin J. Gray
Chairman

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