
Recently Chartered Banks' Vulnerability to Real Estate Crisis

by *Chiwon Yom**

Even while the U.S. banking industry continues to consolidate and the number of banks continues to shrink, de novo banking activity remains vigorous. De novo banks play important roles in preserving competition in the market, providing credit to small businesses (DeYoung, Goldberg, and White [2000]), and promoting an entrepreneurial spirit (Brislin and Santomero [1991]).¹ At the same time, however, these fledgling institutions are financially fragile and more susceptible to failure. Although they are sound in their early years, with large capital cushions and low levels of nonperforming loans, their financial condition typically deteriorates as capital reserves and the quality of their loans move toward industry levels but earnings remain low. Furthermore—and this may not be widely known—new banks are vulnerable to real estate crises because they concentrate heavily in real estate loans. The extent of new banks' exposure to the real estate market is reflected in their poor ratings on the Real Estate Stress Test (REST). This model measures the severity of a bank's exposure to real estate lending, projecting what would happen to a bank if the real estate market experienced a downturn similar to the New England real estate crisis in the 1990s.²

The FDIC closely monitors recently chartered banks and thrifts. For purposes of offsite monitoring, the FDIC defines young banks as commercial banks and thrifts that are eight years old or younger based on studies showing that new banks need more than three years to fully mature (DeYoung [2000], DeYoung and Hasan [1998]). Newly chartered banks tend to be small, and roughly 80 percent of all young banks are located in metropolitan statistical areas (MSAs). This study examines these young banks. Specifically, it examines the vulnerability of these young banks to real estate problems: how their financial condition evolves over time, the degree of risk they bear because of their real estate lending, how they

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¹ In this article, the terms banks and institutions refer to all insured institutions—commercial banks, savings banks and thrifts.

² See Collier, Forbush, and Nuxoll (2003). The stress test was developed on the basis of the New England real estate crisis in the 1990s, and information from a bank's balance sheet and income statement are used to rate the institution. The REST ratings are directly comparable to CAMELS ratings; a REST rating of 1 indicates least vulnerable to a real estate crisis, and a rating of 5 indicates most vulnerable. The REST model is part of the FDIC's offsite monitoring system and is used to help identify and monitor the institutions that are most vulnerable to a real estate crisis.

compare with established banks in this respect, and what explains the heightened vulnerability of young banks to real estate crises.

For our benchmark group we choose small established banks, defined for this study as institutions that are more than eight years old, have assets of less than \$300 million, and are located in MSAs. In addition, our benchmark group excludes special-purpose institutions, such as credit card banks and banks with extensive trust operations.

This study is preceded by a review of the literature and followed by a summary and conclusion.

The Purpose of This Study in Relation to the Literature

Recent studies have furthered our understanding of newly established banks by examining the determinants of bank start-ups and identifying the factors that determine the performance of de novo banks. De novo banking activity is more likely during periods of favorable economic conditions (Dunham [1989]) and in areas that have undergone merger activity (Dunham [1989], Berger, Bonime, Goldberg, and White [1999], Seelig and Critchfield [2003]). Moreover, new banks tend to locate in urban areas (DeYoung [2000]) and in markets where economic growth is high (Moore and Skelton [1998]).

Among researchers who identify the factors that determine the performance of de novo banks, DeYoung (2003) finds that the relationship between external conditions (for example, intense competitive rivalry or slow economic growth) and higher failure rates is more systematic for the de novo banks than for established banks. Hunter, Verbrugge, and Whidbee (1996) find that adverse economic conditions have contributed to the failure of recently chartered thrifts.

Endogenous factors have also been found to play a significant role in the performance and survival of newly chartered banks. Hunter, Verbrugge, and Whidbee (1996) find that credit risk, low capital stocks, and cost inefficiencies have con-

tributed to the failure of de novo banks. Hunter and Srinivasan (1990) find that differences in operating costs, credit policy, and leverage account for most of the performance variations among the sample banks relative to the established target group during the early years of operation. Arshadi and Lawrence (1987) find that operating costs, deposit growth, composition of loan portfolios, and deposit pricing are important in determining the performance of newly chartered banks; they conclude that the performance of new banks is a function of endogenous factors.

Other studies relate the performance of de novo banks to the banks' business strategies and risk management. Brislin and Santomero (1991) find that de novo banks in the third Federal Reserve district (Pennsylvania, New Jersey, and Delaware) tend to concentrate in single types of loans—for example, real estate loans—and they caution that because of the lack of diversification, such strategies increase portfolio risks. Gunther (1990) attributes the large number of failures of new Texas banks in the 1980s to the banks' aggressive strategies, such as concentrating in commercial and industrial (C&I) loans, maintaining low liquidity, and relying heavily on purchased funds. Hunter and Srinivasan (1990) find that real estate lending has consistent and significant effects on the performance of new banks in the later years of operation.

The present study adds to the literature by exploring the role of real estate lending in relation to the performance and lending strategies of banks established between 1995 and 2003. In the latter half of the 1990s, after severe problems in the banking industry during the 1980s and early 1990s, de novo banking activity picked up. Table 1 reports the number of banks and savings institutions chartered in the United States between 1995 and 2003 that were not affiliates of a holding company.³ The table disaggregates de novo institutions by state and type of charter (national bank charter, state bank charter, and savings institution charter). During this period, the five

³ I thank Tim Critchfield at the FDIC's Division of Insurance and Research for providing these data.

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Table 1

De Novo Institutions by State^a				
(1) State	(2) National Bank Charters	(3) State Bank Charters	(4) Savings Institutions	(5) Total
AL	2	14	—	16
AR	2	15	2	19
AZ	2	17	—	19
CA	28	54	3	85
CO	3	22	1	26
CT	2	11	6	19
DC	1	—	—	1
DE	2	3	2	7
FL	18	86	17	121
GA	32	61	3	96
IA	3	9	1	13
ID	—	6	1	7
IL	4	69	8	81
IN	3	10	3	16
KS	8	9	2	19
KY	12	27	3	42
LA	2	16	—	18
MA	2	2	1	5
MD	3	6	5	14
ME	—	2	—	2
MI	—	26	1	27
MN	6	29	3	38
MO	7	25	4	36
MS	2	8	—	10
MT	1	1	1	3
NC	2	38	3	43
NE	2	—	—	2
NH	—	2	1	3
NJ	5	30	6	41
NM	1	8	—	9
NV	3	18	1	22
NY	4	14	4	22
OH	7	12	7	26
OK	5	4	2	11
OR	—	16	1	17
PA	1	27	7	35
RI	1	1	1	3
SC	12	8	4	24
SD	4	—	—	4
TN	5	38	3	46
TX	36	20	8	64
UT	—	26	1	27
VA	14	19	1	34
VI	—	2	—	2
WA	7	31	3	41
WI	2	21	5	28
WV	—	11	—	11
WY	1	3	—	4
Total	257	877	125	1259
Percent	20.4	69.7	9.9	100.0

^a De Novo institutions chartered between 1995 and 2003.

states with the highest number of new start-ups were Florida, Georgia, Illinois, California, and Texas at 121, 96, 81, 85, and 64, respectively. State charters, at 877, constituted the largest share of new institutions (69.7 percent); there were 257 national charters (20.4 percent) and 125 new savings institutions (9.9 percent).

For a number of reasons, this new batch of de novo institutions may differ in performance and viability from the de novo banks in the 1980s. First, economic conditions are more favorable now than they were in the 1980s, when many banking institutions operated under severe regional recessions. Second, regulation and supervision are more stringent now. The Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA) requires all institutions, including those with national charters, to apply formally to the FDIC for federal deposit insurance. Before FDICIA, the FDIC granted deposit insurance to national banks as a matter of law once the Office of the Comptroller of the Currency had approved a bank's charter. In contrast, the chartering of state banks depended heavily on whether the FDIC approved the bank's application for insurance: without the FDIC's approval of the application, a state was unlikely to grant a bank charter.

Third, once chartered, a new bank is now supervised more closely by its regulatory agency. The FDIC conducts a limited-scope examination at each newly chartered state nonmember bank within the first six months of operation, followed by a full-scope examination within the first twelve months. Subsequently, each state nonmember bank is examined each year until the end of the third year, although the FDIC may alternate with the state supervisors in conducting the examination.⁴ Similarly, the Federal Reserve Banks examine newly chartered state member banks at a higher frequency compared to established banks, conducting full-scope examinations for safety and soundness at newly chartered state

⁴ I thank Don Hamm at the FDIC's Division of Supervision and Consumer Protection for referring me to the Manual of Examination Policies, Section 1.1 Basic Examination Concepts and Guidelines.

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member banks at 6-month intervals (whereas established banks are examined every 12 to 18 months) and continuing to schedule exams at this frequency until the bank receives a strong composite CAMELS ratings (a rating of 1 or 2) in two consecutive exams (DeYoung [2000]).⁵

Fourth, new banks are required to maintain a higher capital ratio than their established counterparts. Normally the FDIC requires all proposed depository institutions to start with enough capital to provide “a Tier 1 capital to assets leverage ratio (as defined in the appropriate capital regulation of the institution’s primary federal regulator) of not less than 8.0% throughout the first three years of operation.”⁶ These temporary capital requirements are meant to ensure that new banks have enough capital cushion to absorb the negative earnings and rapid asset growth of the first few years.

Finally, bank supervisors typically place restrictions on dividend payouts by new banks, limit the amount of debt that new bank holding companies can issue, and require new banks to maintain minimum levels of loan-loss reserves (DeYoung [2000]).

The Life Cycle of the Performance of Young Banks

We begin our examination of young banks’ exposure to the real estate market by describing the evolution of the performance of young banks. To document this evolution, we group young banks chartered between 1995 and 2003 into classes according to the year they are chartered. For example, new banks chartered in 1997 and 1998 are grouped into Class 1997 and Class 1998. Grouping young banks this way is motivated by recent studies that have found that newly chartered banks follow a distinct life-cycle pattern (DeYoung [1999, 2000]).

Figures 1 through 5 graph the median values of financial ratios for each of our classes of young banks, starting when the banks are four quarters

old (the flow variables are four-quarter sums). For each ratio, the financial performance of all the classes of young banks is compared with the median 2—the median financial ratio of all institutions with a CAMELS composite rating of 2—serving as an industry benchmark.

The figures show that in the early years of young banks, the banks’ financial ratios follow similar time paths regardless of the year of chartering. Figure 1 shows that the median bank of each class earned negative profits in the first few years. But although the median banks start to earn profits after about two years, they continue to underperform established banks (the median 2). In the early years, however, young banks’ negative or low earnings are offset by a large initial capital and low nonperforming assets: as figures 2 and 3 show, in the first few years young banks have very high capital and very few nonperforming loans. For instance, in their fourth quarter since establishment, the median equity-to-assets ratios for Class 1995, Class 1998, and Class 2000 are 17.40 percent, 18.46 percent, and 18.77 percent, respectively. This is substantially higher than the median 2 equity-to-assets ratio of 8.96 percent. Similarly, the median nonaccruing-loans-to-total-assets ratio is zero for all classes of young banks in their fourth quarter, compared with 0.24 percent for the median 2. A number of years after having been chartered, however, young banks experience financial deterioration, as their capital cushions are depleted by low earnings and fast growth. Figure 4 shows that the median asset growth (annualized) of young banks is very high in the first few years.

But as the rapid rise in nonaccrual loans indicates, assets begin to show signs of trouble. Notably, young banks’ performance begins to deteriorate for the most part after the third year (12th quarter), the age when supervisors stop paying close attention to these institutions. The

⁵ CAMELS is an acronym for *Capital, Asset quality, Management, Earnings, Liquidity, and market Sensitivity*.

⁶ The FDIC Statement of Policy on Applications for Deposit Insurance.

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Figure 1

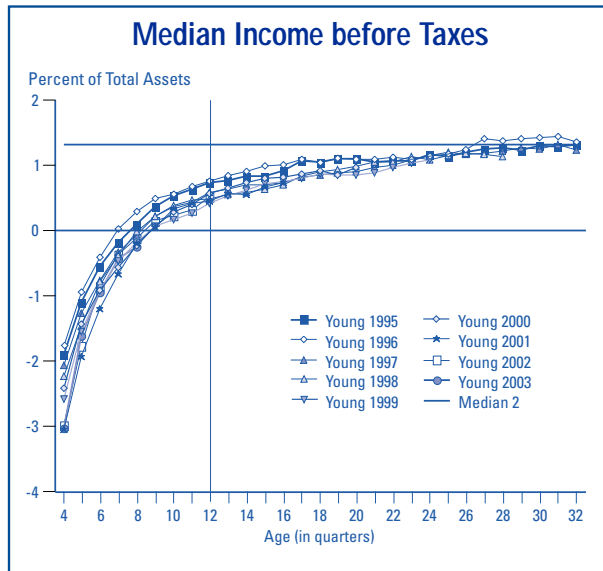


Figure 3

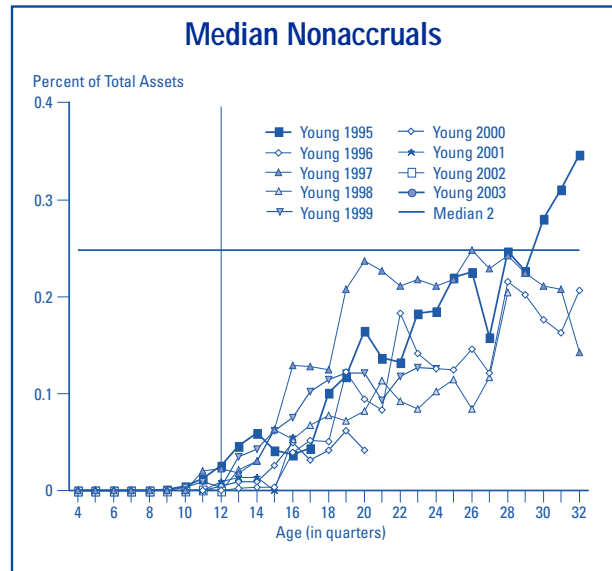


Figure 2

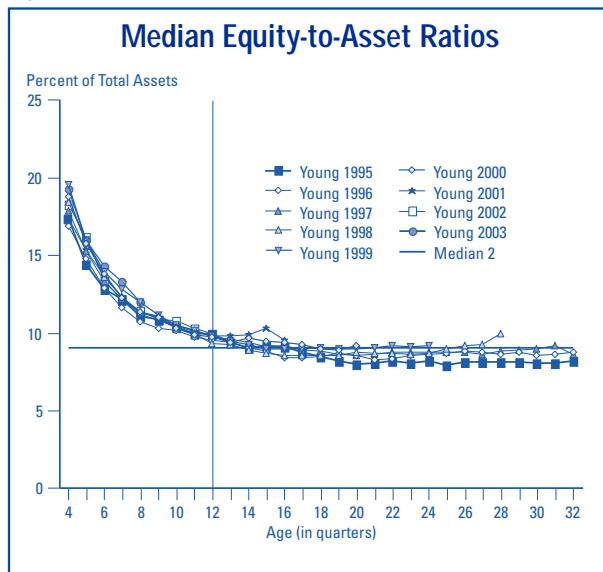
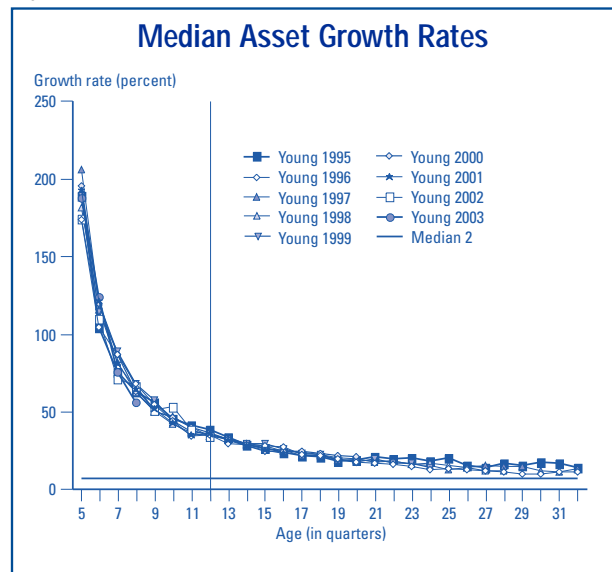


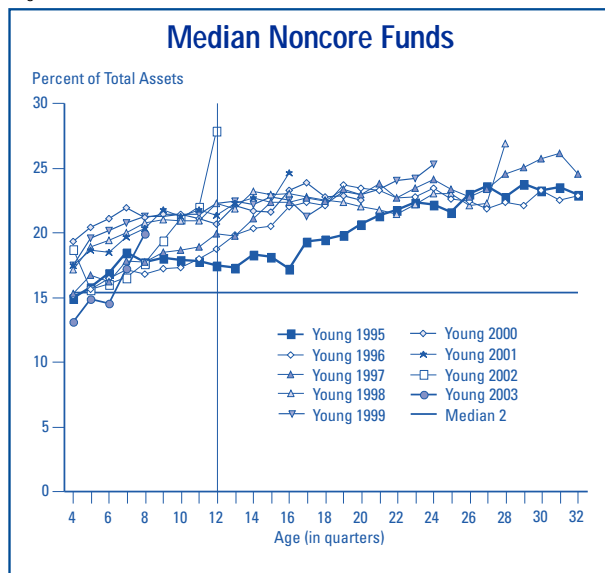
Figure 4



poor performance continues for a number of years until these banks reach full maturity and perform much like established banks. Young banks' reliance on noncore funds, too, remains high up to the eighth year. Figure 5 shows that throughout the sample period, young banks have a higher median ratio of noncore-funds-to-total-assets than the median 2.

These findings are consistent with those of studies that examined the performance trend of new banks chartered in the 1980s. Using the sample of new banks chartered between 1980 and 1985, DeYoung and Hasan (1998), and DeYoung (2000), conclude that it takes many years for de novo banks to reach full maturity and perform as well as established banks. In fact, DeYoung and Hasan (1998) find that it takes nine years for new

Figure 5

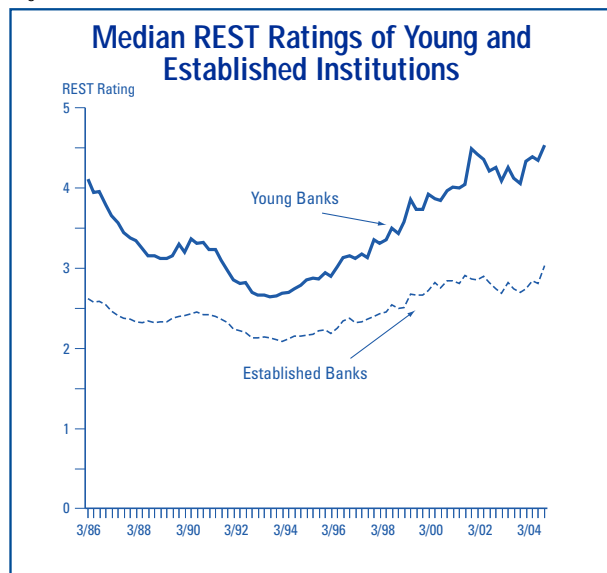


banks to become as efficient, in terms of profitability, as established banks.

The Real Estate Exposure of Young Banks Compared with That of Established Banks

We have seen that young banks are financially fragile. This is well known. What is less well known is that they concentrate heavily in risky assets—more heavily than established banks do. Table 2 reports the median REST ratings of young and established banks across time and the number of banks in each of the two groups, and figure 6 represents the two “median” columns graphically. As figure 6 shows, the median REST ratings of young banks are consistently worse than those of established banks. A formal test using Kendall’s rank correlation confirms that the REST ratings of young banks are worse (with statistical significance) than those of established banks. Like Pearson’s correlation coefficient, Kendall’s rank correlation takes values between -1 (perfect negative correlation) and $+1$ (perfect positive correlation). Moreover, figure 6 shows that the REST ratings of both young and established banks steadily worsened in the latter half of the sample period—yet the gap between the median ratings widened. It can be inferred, therefore, that the

Figure 6



REST ratings of young banks deteriorated more rapidly than those of established banks.

Figures 7 and 8, whose solid lines trace the percentage of young and established banks with poor REST ratings over time, show the percentages of both young and established banks with REST ratings of 4 or 5 rose between 1993 and 2004, but at the same time, the percentage of young banks with poor ratings became higher. It rose from 21 percent in 1993 to 77 percent in 2004, whereas the percentage for established banks with poor ratings rose from 8 percent in 1993 to 40 percent in 2004. These figures show the extent to which young banks are more vulnerable to the stress of a real estate crisis than their established counterparts are.

(Parenthetically, figures 7 and 8 also trace the percentage of young and established banks with poor CAMELS composite ratings. The broken lines in these figures show the percentage of banks with a CAMELS rating of 4 or 5. During the period 1993–2004, when the percentage of institutions with poor REST was rising, the percentage of institutions with poor exam ratings was falling. The contrast between the trend in the health of the banking industry and the trend in the industry’s risk exposures to real estate lending

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Table 2

Comparison of Median REST Ratings for Young and Established Institutions									
Date (1)	Young Banks		Established Banks		Date (1)	Young Banks		Established Banks	
	Number (2)	Median (3)	Number (4)	Median (5)		Number (2)	Median (3)	Number (4)	Median (5)
Mar-86	84	4.11*** ^a	5465	2.62	Mar-96	496	2.90***	3792	2.19
Jun-86	169	3.95***	5386	2.58	Jun-96	461	3.02***	3748	2.26
Sep-86	267	3.96***	5369	2.59	Sep-96	435	3.14***	3688	2.34
Dec-86	346	3.79***	5219	2.54	Dec-96	414	3.16***	3623	2.38
Mar-87	410	3.66***	5137	2.47	Mar-97	402	3.12***	3566	2.32
Jun-87	473	3.57***	5037	2.41	Jun-97	384	3.18***	3521	2.33
Sep-87	527	3.45***	4978	2.38	Sep-97	378	3.14***	3466	2.37
Dec-87	569	3.38***	4898	2.37	Dec-97	383	3.36***	3401	2.40
Mar-88	607	3.35***	4833	2.33	Mar-98	378	3.31***	3332	2.43
Jun-88	638	3.25***	4732	2.32	Jun-98	386	3.36***	3263	2.45
Sep-88	676	3.16***	4636	2.34	Sep-98	400	3.50***	3214	2.54
Dec-88	708	3.16***	4503	2.32	Dec-98	409	3.44***	3134	2.50
Mar-89	732	3.12***	4431	2.33	Mar-99	429	3.58***	3085	2.51
Jun-89	766	3.12***	4389	2.33	Jun-99	447	3.86***	3025	2.68
Sep-89	798	3.16***	4302	2.38	Sep-99	472	3.74***	2971	2.67
Dec-89	837	3.30***	4235	2.40	Dec-99	514	3.74***	2904	2.67
Mar-90	860	3.20***	4163	2.41	Mar-00	533	3.93***	2849	2.72
Jun-90	894	3.37***	4079	2.43	Jun-00	575	3.87***	2801	2.82
Sep-90	922	3.31***	4009	2.45	Sep-00	625	3.85***	2739	2.76
Dec-90	960	3.32***	3953	2.42	Dec-00	679	3.97***	2664	2.84
Mar-91	990	3.23***	3899	2.42	Mar-01	727	4.02***	2591	2.85
Jun-91	1019	3.24***	3829	2.40	Jun-01	773	4.00***	2548	2.81
Sep-91	1041	3.10***	3759	2.37	Sep-01	824	4.05***	2508	2.91
Dec-91	1048	2.97***	4781	2.32	Dec-01	860	4.49***	2434	2.87
Mar-92	1008	2.86***	4702	2.24	Mar-02	897	4.43***	2388	2.86
Jun-92	977	2.81***	4676	2.22	Jun-02	882	4.36***	2325	2.90
Sep-92	938	2.82***	4652	2.20	Sep-02	902	4.21***	2265	2.82
Dec-92	916	2.70***	4567	2.13	Dec-02	937	4.26***	2222	2.75
Mar-93	879	2.67***	4541	2.13	Mar-03	943	4.09***	2184	2.69
Jun-93	841	2.67***	4497	2.14	Jun-03	942	4.26***	2144	2.82
Sep-93	815	2.65***	4431	2.13	Sep-03	947	4.13***	2125	2.75
Dec-93	770	2.66***	4348	2.11	Dec-03	939	4.06***	2100	2.70
Mar-94	737	2.69***	4286	2.09	Mar-04	931	4.34***	2066	2.75
Jun-94	699	2.70***	4234	2.12	Jun-04	930	4.39***	2032	2.85
Sep-94	662	2.74***	4172	2.15	Sep-04	915	4.35***	2018	2.81
Dec-94	635	2.79***	4123	2.15	Dec-04	905	4.54***	2002	3.03
Mar-95	608	2.86***	4034	2.17					
Jun-95	586	2.88***	3965	2.18					
Sep-95	553	2.87***	3899	2.22					
Dec-95	517	2.94***	3852	2.23					

^a Based on Kendall's rank correlation test.
 *** Indicates statistical significance at the 1 percent level.

is consistent with the high cyclicity of the real estate market. During periods of favorable economic conditions, the real estate market expands, and meeting the increasing demand for real estate loans leads banks to large exposures.)

The reason the REST ratings of young banks are worse than the ratings of established banks is that the kinds of real estate lending done by young banks are riskier than the kinds done by estab-

lished banks. Table 3 shows that as of December 2004, young banks tended to have more commercial and industrial (C&I), construction and development (C&D), and nonresidential real estate loans—the three types generally considered risky. Specifically, the new institutions' median ratio of C&I loans to total assets was roughly twice that of the established peer: young banks' 11.85 percent versus established banks' 6.59 percent. Similarly, nonresidential real estate lending made up a

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Figure 7

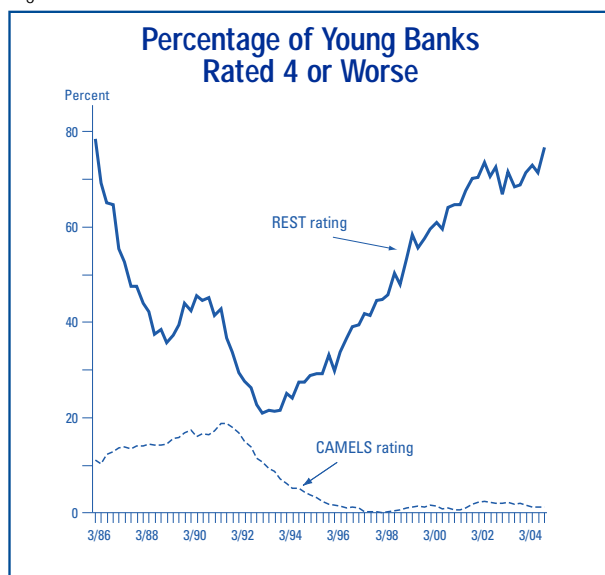
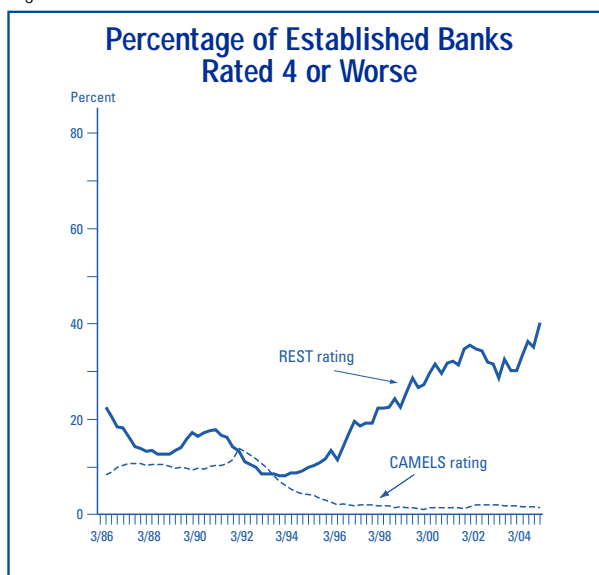


Figure 8



higher percentage of total assets for new institutions than for established banks. And most importantly, a typical new bank had 8.58 percent of total assets in construction loans—more than twice the percentage for the established peer. Previous studies have found construction and development lending to be the primary risk factor of real estate crises because the success of construction loans is highly dependent on the future of the real estate market (Collier, Forbush, and Nuxoll [2003]) and because commercial real estate projects are highly leveraged and more sensitive to changes in market conditions (Freund, Curry, Hirsch, and Kelley [1997]).

In contrast, the relatively safer real estate 1–4 family loans make up a smaller share of assets for young banks than for established banks.

As table 3 also shows, the comparison between young and established banks holds for rate of growth and reliance on noncore funds. Young banks grow more rapidly than established banks: a typical young bank grows at the rate of 22.32 percent annually—roughly four times the median growth rate of established banks. And to fuel such rapid growth, young banks rely more heavily on noncore funds, which are expensive sources of funds and the first to be demanded in times of

Table 3

Comparison of Median Ratios between Young and Established Institutions
(as of December 31, 2004)

Variable ^a	Young	Established
C&I	11.85*** ^b	6.59
RE Agricultural	0.00***	0.14
RE C&D	8.58***	3.93
RE Multifamily	1.04***	0.75
RE Nonfarm nonresidential	21.14***	13.12
RE 1-4 family	15.77***	20.47
Noncore liabilities	24.72***	17.33
Asset Growth	22.32***	4.90
Equity Growth	-3.50***	0.68
No. of observations	905	2002

^a Loan ratios are expressed as a percentage of assets. The growth measures are one-year change (in percent) in assets and equity.
^b Based on Kendall's rank correlation test.
 *** Indicates statistical significance at the 1 percent level.

stress. Noncore liabilities make up 24.72 percent of total assets for a typical young institution, compared with 17.33 percent for established banks.

In sum, the statistics presented in table 3 suggest that the poor REST ratings of new banks are likely to be attributable to higher concentrations in construction, C&I, and nonresidential real estate loans; to rapid growth; and to heavy reliance on noncore funds.

Possible Explanations for Young Institutions' More Risky Lending

How does one explain young institutions' heavier engagement in riskier real estate lending activities? One might attribute it to the geographic location of these institutions. Young banks tend to start up in areas of rapid economic and population growth (Moore and Skelton [1998]) and therefore young banks may simply be meeting the local market's growing demand for real estate loans. Alternatively, perhaps young banks simply engage in more aggressive risk management.

To evaluate these two possible explanations, we first determined whether young banks in fact are concentrated in rapidly growing states; we then compared the average REST rating of each state with the percentage of new banks in the state. On the one hand, if states with large percentages of new banks have high average REST ratings, that finding will support the first explanation. For if the geographic location of young institutions is important in explaining the institutions' poor REST ratings, other established institutions in the same states will also have poor ratings, and the REST rating of a typical bank in these states will be high. On the other hand, if states with large percentages of new banks do not show high average REST ratings, the second explanation—more aggressive risk management—is the more likely. For if young institutions' poor REST ratings are unrelated to their geographic locations, typical banks in the same states will not necessarily have a poor REST rating. And if aggressive risk management is the answer, what factors might explain it?

Geographic Location

Table 4 reports, by state, the number of young institutions, the total number of institutions, the ratio of young institutions to total institutions, and the median REST rating for the state, based on December 2004 data. In the aggregate, young banks make up 13.3 percent (1,197 out of 8,975) of all banks. But rather than being evenly distributed, young banks are concentrated in a few

Table 4

Median REST Ratings by State (as of December 31, 2004)				
State	Young (Number)	All (Number)	Young/All (Percent)	Med. REST Rating (All)
AZ	32	50	64.00	4.98
NV	21	38	55.26	4.88
UT	31	67	46.27	4.43
FL	121	298	40.60	4.25
OR	15	40	37.50	4.49
NC	38	110	34.55	4.50
DC	2	6	33.33	2.50
ID	6	18	33.33	4.41
RI	5	15	33.33	2.65
DE	11	35	31.43	3.71
CA	93	302	30.79	4.51
GA	100	351	28.49	4.36
NJ	40	141	28.37	2.91
WA	28	99	28.28	4.58
VA	38	140	27.14	3.79
SC	23	97	23.71	3.80
TN	46	212	21.70	3.75
CT	12	58	20.69	2.90
MI	33	174	18.97	3.53
NM	11	58	18.97	3.24
CO	27	177	15.25	3.78
KY	32	238	13.45	2.64
NY	26	203	12.81	2.62
MS	13	102	12.75	2.88
MD	14	116	12.07	3.42
PA	31	266	11.65	2.40
AL	19	164	11.59	2.91
WV	8	74	10.81	2.38
LA	15	168	8.93	2.85
MO	33	375	8.80	2.71
IN	17	198	8.59	2.65
TX	58	689	8.42	2.64
MN	40	482	8.30	2.58
AR	13	168	7.74	2.97
IL	58	756	7.67	2.44
IA	30	416	7.21	2.12
OH	21	296	7.09	2.51
WY	3	44	6.82	2.72
WI	20	309	6.47	3.10
MT	5	80	6.25	2.83
KS	16	372	4.30	2.15
ND	4	104	3.85	1.96
OK	10	274	3.65	2.39
NH	1	30	3.33	2.71
NE	7	265	2.64	1.99
ME	1	39	2.56	3.10
SD	2	93	2.15	2.12
MA	3	200	1.50	2.85
AK	0	7	0.00	4.25
HI	0	8	0.00	3.44
VT	0	19	0.00	2.54

states. For instance, in Nevada and Arizona young banks make up more than 50 percent of all banks, but Alaska, Hawaii, and Vermont have no young banks.

Table 4 also shows that states with large percentages of young banks tend to have poor median REST ratings. Arizona, where young banks constitute 64 percent of all banks, has the worst median REST rating—4.98. Seven of the ten states with the largest percentages of young banks have ratings worse than 4.

A formal statistical test—again, Kendall's rank correlation—confirms the positive correlation noted above between the ratio of new to all banks in a state and the median REST rating for the state. There is strong evidence that states with larger percentages of young banks tend to have worse median REST ratings. The rank correlation between these two variables is 0.47 and is highly significant.

This result is consistent with the first explanation for young banks' relatively heavier engagement in real estate lending—that the geographic location of these banks is an important contributor to their poor REST ratings. As earlier studies have showed, young banks are concentrated in urban and rapidly growing markets (Moore and Skelton [1998], DeYoung [2000]), and it is plausible that in such markets there are growing amounts of deposits and increasing demands for loans, including commercial and real estate loans. By supplying the loan demands of the local market, both young and established banks lend more heavily to the real estate sector. Consequently, banks in rapidly growing states have poor REST ratings.

Risk Management: Young Banks vs. Established Banks

Although geographic location—a heavy concentration in rapidly growing markets—can be considered an explanation for young banks' poor REST ratings, it may not necessarily offer a full

explanation. To explore whether young and established institutions engage in similar lending activities in high-growth states, we compared the loan portfolio composition of young banks in three high-growth states with that of established banks in the same states. As noted above, young banks are predominantly small and urban, so the established institutions with which we compared them are small and located in metropolitan statistical areas.

Three states with relatively large percentages of young banks are Florida, Georgia, and New Jersey. In Florida, the percentage is 40.6; in Georgia, 28.5; and in New Jersey, 28.4. Moreover, in these states the number of institutions, too, is relatively large, so statistical tests can be performed. Florida and Georgia have median REST ratings worse than 4, but a typical bank in New Jersey has a REST rating of 2.9.

To test whether, in these three states, young banks' loan ratios are ranked worse than the ratios of established banks, we used Kendall's rank correlation statistic. (Rank correlation is estimated for each bank's loan ratio and a dummy variable, valued 1 if a young bank and 0 if an established bank.) The results of the rank correlation test are reported in table 5.

In our three states, young banks generally use riskier lending strategies. They tend to devote greater shares of their assets to loans, and they concentrate in riskier loans, such as C&I and construction loans. Moreover, they grow more rapidly than established banks.

In New Jersey, young banks had a statistically significantly higher concentration of riskier loans (C&I loans, C&D loans, and nonresidential real estate loans). And asset- and loan-growth rates were significantly higher for young banks. In contrast, young banks had lower concentrations of safer loans (for example, loans to municipalities and 1-4 family real estate loans), which help shield banks from downturns (Collier, Forbush, and Nuxoll [2003]).

Table 5

Comparison of Median Ratios between Young and Established Institutions (December 2004)						
Loan Type ^a	Florida		Georgia		New Jersey	
	Young	Established	Young	Established	Young	Established
Agriculture	0.00	0.00	0.00	0.00	0.00	0.00
C&I	9.66	7.37	10.86***	7.19	8.77***	1.05
Other Consumer	1.39	1.48	2.16**	3.41	0.39	0.47
Credit Card	0.00	0.00	0.00	0.00	0.00	0.00
Depository	0.00** ^b	0.00	0.00	0.00	0.00	0.00
Municipality	0.00**	0.00	0.00*	0.00	0.00*	0.00
Agriculture-Real Estate	0.00	0.00	0.02	0.22	0.00	0.00
Construction	10.43*	6.46	20.97	17.31	5.18***	0.77
Multifamily	1.42	1.53	0.41*	0.35	1.23**	0.58
Non-residential Real Estate	24.11	24.35	22.97	19.28	25.70***	8.19
1-4 Family	15.32	14.02	13.08	15.58	15.99***	37.50
Leases	0.00	0.00	0.00	0.00	0.00	0.00
Assets (\$000s)	143,405	175,778	141,793	128,030	132,710	182,949
Asset Growth	56.77***	23.25	46.01***	15.24	45.65***	12.31
Loans to assets	75.68	73.10	79.11**	73.45	68.03***	56.51
Noncore Funds	22.41**	18.86	26.90***	21.00	16.71	17.00
REST Score	4.76***	3.95	5.00**	4.98	3.95***	1.92
No. of Observations	90	79	67	40	34	35

^a Loan and liability ratios are expressed as a percentage of assets. The asset growth is one-year change (in percent) in assets.
^b Based on Kendall's rank correlation test.
*** Indicates statistical significance at the 1 percent level.
** Indicates statistical significance at the 5 percent level.
* Indicates statistical significance at the 10 percent level.

In Florida the picture was similar. Young banks had a greater percentage of their assets in a riskier loan type (C&D loans). They grew more rapidly (higher asset growth) and relied more on noncore liabilities. And they had fewer loans to depository institutions and municipalities.

In Georgia, young banks concentrated more heavily than established banks in C&I and multi-family loans and grew more rapidly, but their ratio of construction loans did not differ significantly from the ratio for established banks. Nevertheless, young banks in Georgia had a higher percentage of assets devoted to construction loans than did the young banks of New Jersey and Florida. In Georgia young banks devoted more than 20 percent of their assets to construction loans, whereas the comparable percentages in Florida and New Jersey were 10.43 percent and 5.18 percent, respectively.

Explanations for Aggressive Risk Management

These findings suggest that geographic location alone does not fully explain young banks' concentration in riskier loans and greater vulnerability to real estate crises. Even within rapidly growing states, young banks pursue more aggressive lending strategies than established banks. We now explore other factors that may explain young banks' pursuit of riskier activities.

One such factor may be young banks' desire for rapid growth. Arshadi and Lawrence observe that growth in the first few years is vitally important for new banks' survival and sound performance (Arshadi and Lawrence [1987]). With low business volume, new banks are likely to spend proportionately more on salaries and overhead expenses,⁷ and to become profitable, they need to

⁷ For instance, Brislin and Santomero (1991) note that overhead expenses account for 92 percent of total expenses in the first quarter of operation at a typical de novo bank in the third Federal Reserve district (Pennsylvania, New Jersey, and Delaware).

Recently Chartered Banks' Vulnerability to Real Estate Crisis

grow and use their facilities and staff more efficiently. This need may drive young banks to grow rapidly using noncore liabilities and relaxed underwriting standards.

Another reason that young banks may be attracted to the riskier assets is that these assets tend to generate immediate income. For instance, commercial real estate loans have large up-front fees. A third possible reason is that specialized business strategies require expertise in fewer areas and may help young institutions find their market niche (Brislin and Santomero [1991]).

Fourth, young banks' concentration in risky activities may result from the growth constraints they encounter. Unlike their established counterparts, young banks lack established customer relationships and market recognition. As a result, their growth is constrained by limitations on deposits and on good investment opportunities. Young banks may be left to lend to the pool of borrowers with poor credit and to finance highly risky ventures. Economists refer to this phenomenon as adverse selection.

Whatever the rationale for the aggressive lending strategies undertaken by young banks, they are particularly vulnerable to downturns in the real estate market, as the experience of the new Texas banks in the 1980s demonstrates.⁸ New Texas banks in the early 1980s were heavily concentrated in growing markets; according to Gunther, new banks made up 54 percent of the banks in the five largest and most rapidly growing markets in Texas (Austin, Dallas, Fort Worth–Arlington, Houston, and San Antonio). Gunther's analysis suggests that new banks pursued riskier strategies, such as concentrating on riskier loans and relying more heavily on wholesale funds.

After oil prices plummeted in 1986, Texas entered a recession and experienced a real estate crisis. Although many banks suffered, it was evident that the recession had an especially great effect on *de novo* banks. In the subsequent four years 39 percent of *de novo* banks failed, but only 21 percent of established banks. Finding that new banks with capital levels similar to the levels of

established banks and risk did not fail at significantly higher rates than mature banks, Gunther concludes that new banks' relatively higher risk postures led to the high incidence of failure.

The experience of the new Texas banks offers a scenario of what could happen to the current vintage of young banks if the markets now experiencing rapid growth—and where there are many young banks—were to experience busts. Young banks in these states would be likely to experience greater failures and losses. Of course, one must be cautious when extrapolating from a banking experience in the 1980s to a banking experience today, for even if economic conditions were to become comparable to those in the 1980s, the regulatory environment, as noted above, differs greatly from what it was in the 1980s.

Summary and Conclusion

It is well known that new banks are financially fragile and more susceptible to failure than established banks. What is less well known is that new banks have a substantial exposure to the real estate market. The extent of this exposure is reflected in the poor REST ratings of new banks. For example, in December 2004 the median REST rating of young banks was 4.54, whereas the median for established banks was 3.03. This difference is statistically significant.

Part of the explanation for young banks' vulnerability to a real estate crisis is geographic location. Young banks tend to locate in rapidly growing markets, where economic activity is greater and the demand for riskier real estate loans (such as C&D loans and C&I loans) is also greater.

But if geographic location fully explained young banks' vulnerability to a real estate crisis, the established banks in the same market would use strategies roughly similar to those used by the

⁸ Gunther (1990) tracks the failure rates during the period 1986 to 1989 of banks that had been established between 1980 and 1985. Accordingly, new banks in his study were ten years old and younger.

young banks. Our research shows that they do not. A closer examination of young banks in three rapidly growing states—Florida, Georgia, and New Jersey—suggests that the young banks in those states use riskier lending strategies than their established counterparts.

The disproportionate use by young banks of the risky strategies may have a number of explanations. Young banks may undertake aggressive business strategies in order to grow rapidly, bolster low earnings, and become profitable. More importantly, their heavy concentration in risky loans may reflect the severe problem of adverse selection that they encounter: lacking a well-

established customer base, new banks may find that a disproportionately large share of the loan applications they receive are from borrowers with risky ventures who have been turned down by other banks. In other words, the financial vulnerabilities of young banks may in fact be augmented by these institutions' asset composition.

Past experiences hint at the extent to which adverse episodes in the real estate market could affect these fledgling institutions. Thus, regulators are further motivated to closely monitor not only the banks' performance but also their risk management.

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Politics and Policy: The Creation of the Resolution Trust Corporation

by Lee Davison*

As the U.S. government sought solutions to the S&L crisis in 1989 and set about revamping the thrift industry's activities, regulation, and supervision and restoring the industry's insurance fund, it faced a multitude of challenges. One of the most significant was to create a mechanism that would resolve all then-insolvent thrifts as well as the large number of thrifts expected to become insolvent in the near future. The mechanism not only had to be created but it also (optimally) had to be able to accomplish its mission—closing, selling, or merging institutions and disposing of vast amounts of assets—as quickly as possible. Furthermore, it had to do so in a way that would minimize taxpayer costs and avoid serious dislocation in markets. Quite obviously some of these goals were at cross-purposes. One circumstance that aided policymakers was the existence of the Federal Deposit Insurance Corporation (FDIC)—that agency could provide expertise, an initial set of policies, and so allow for a relatively swift start to the task. Even with this advantage, the task of creating the necessary mechanism was not going to be easy.

Given the extensive use of tax dollars that would be required, inevitably the mechanism would be a governmental entity. But because of recent history, the creation of such an entity was fraught with

problems. In 1988 the handling of troubled and failed thrifts by the Federal Home Loan Bank Board (FHLBB) had been roundly criticized; and the record of the Federal Asset Disposition Association (FADA), which the FHLBB had created in 1985, also failed to inspire confidence. (Both the 1988 deals and the FADA's record are described in the appendix.) Awareness of these past failures—whether real or perceived—helped shape the policy decisions relevant to the creation of the Resolution Trust Corporation (RTC) and where governmental responsibility for the its work would lie.

President George H.W. Bush announced his plan for what would become the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA) on February 9, 1989. This bill promised to become the most significant legislation affecting depository institutions in a decade and the most important legislation affecting the S&L industry since the Great Depression. The adminis-

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tration began with the ambitious objective of achieving passage of the legislation within 45 days, and at least initially, Congress was receptive to the idea of a speedy process. Rep. Frank Annunzio told the president that normally such a “timetable to rewrite major portions of the financial laws of our country would not be adequate, but these are unusual times, and swift action must be taken.”¹ The breadth of the legislation and the variety of interested parties, however, combined to make this timetable unworkable, and FIRREA was not signed into law until August 9, six months after the president’s plan was announced.

FIRREA abolished the Federal Savings and Loan Insurance Corporation (FSLIC), the insurance arm of the FHLBB, and created the Savings Association Insurance Fund (SAIF), a new deposit insurance system for thrifts to be administered by the FDIC. FIRREA also dismantled the FHLBB and, in its stead, created the Office of Thrift Supervision (OTS), an agency within the Treasury Department, both to charter federal thrifts and to serve as the primary federal regulator of all thrifts. The law laid down much stricter minimum capital and accounting requirements for thrifts (including phasing out the inclusion of supervisory goodwill by January 1995),² tightened the “qualified-thrift-lender” test, and altered the rules on thrift acquisitions by bank holding companies. The law gave financial institution regulators significant new enforcement powers, made substantial changes to existing FDIC authorities and granted new powers to the FDIC, and reformed the Federal Home Loan Bank System. Finally, FIRREA also created the RTC—a government agency charged with tasks never before undertaken in the history of the United States.³

As enacted, FIRREA made the RTC a limited-life (for five years) entity that would manage and resolve all formerly FSLIC-insured institutions placed under conservatorship or receivership from January 1, 1989, through August 9, 1992.⁴ As of the date of enactment, the RTC was to succeed the FSLIC in its role as conservator or receiver of any institution. General oversight of the RTC was vested in an Oversight Board, which was to direct

the RTC’s overall policy, but operational control would rest with the RTC itself. The Board of Directors of the FDIC was to serve as the RTC’s Board of Directors (and FIRREA expanded the FDIC’s Board from three to five members, adding the head of the OTS and a member to be nominated by the president); and the FDIC would be the RTC’s “exclusive manager.” The RTC was to have no employees of its own but was to use the employees of other federal departments or agencies, most notably the FDIC. In addition, the RTC was to manage and dissolve the FADA within 180 days and was to review the transactions made by the FSLIC during 1988 to determine if cost savings could be found. The law also dealt with issues such as contracting, audits and reporting, asset disposition, and the mechanism for funding the RTC.

The RTC created by FIRREA’s enactment was recognizably the product of the administration’s approach, but the new agency also reflected changes made during the legislative process. The RTC emerged both more defined by statutory requirements and more accountable to the public, but also more cumbersome by virtue of an intragovernmental battle for authority and the potentially contradictory goals that Congress grafted onto the structure. All the changes would sig-

¹ Annunzio was the chairman of the House Subcommittee on Financial Institutions Supervision, Regulation and Insurance. George Bush Presidential Library (GBPL) F1002/14513: Annunzio to Bush (March 6, 1989).

² Earlier in the 1980s, faced with growing numbers of insolvent thrifts but without any means of paying for their closure, the government encouraged mergers as a way to deal with this intractable problem. To make such transactions viable for acquiring institutions, the government allowed the acquirers (for the purposes of meeting capital requirements) to offset the liabilities they were assuming with a counterbalancing paper asset called supervisory goodwill. Acquirers were allowed as much as 40 years to write off supervisory goodwill. In addition, other variances from generally accepted accounting principles (GAAP) were allowed for all thrifts. FIRREA’s provision therefore had serious negative implications for many acquirers’ net worth, even their solvency, and led to litigation that eventually reached the Supreme Court; in 1996 the Court ruled (in *United States v. Winstar*) that the government had had no right to repudiate accounting variances that had been included in resolution contracts. As a result of this decision, a number of institutions successfully sued the government for damages.

³ This brief summary of FIRREA is by no means exhaustive. For a detailed examination of the elements of the statute, see Bloch and Williams (1989).

⁴ Despite the statute’s date of January 1, 1989, the FSLIC did resolve a small number of small institutions early in 1989. These S&Ls therefore “belonged” to the FSLIC Resolution Fund, and so did not pass to the RTC. Starting in February 1989, the FDIC took responsibility for S&L conservatorships that would have been run by the FSLIC—these institutions did pass to the RTC.

nificantly affect the way in which the RTC would carry out its work.

The next section presents an overview of the administration's initial plan and the changes it underwent. The process by which those changes were achieved is spelled out in detail in subsequent sections. The appendix briefly recapitulates the history of the FADA and the 1988 FSLIC deals and the ways in which FIRREA proposed to dispose of both of them.

Overview: The Initial Plan and the Ways It Changed

The creation of the RTC was affected by the magnitude of the changes contemplated in the bill the administration sent to Congress, the need for the bill's speedy enactment,⁵ and the lack of detail in the administration's initial pronouncements on the RTC. Because 1) the bill embraced the wholesale modification not only of thrift regulatory structure but also of many aspects of thrift regulation and 2) speed was critical, the RTC was considerably less visible than it might have been. And the lack of detail (among other causes) meant that despite the interest and involvement of people both inside and outside the government, many aspects of the RTC's structure remained undecided until very late in the legislative process, while other aspects were left entirely (not always unintentionally) undressed.

Although the RTC was at the heart of the administration's plan for restoring the thrift industry,⁶ as first announced the plan did not spell out the RTC's structure and operating procedures. Rather, it provided only a few basics. It simply established the RTC (which was not to be deemed an agency of the U.S. government) for a limited life of five years to manage and resolve all FSLIC-insured institutions placed either in receivership or conservatorship for the three years following enactment. It would also take over from the FSLIC as conservator or receiver for institutions where the FHLBB had appointed a conservator or receiver after January 1, 1989. In addition, the RTC was to manage the assets of the FADA and wind that organization

down within 180 days. The real work of resolution and asset disposition would be contracted out, much of it through a management contract to the FDIC, which was considered the most experienced agency available to perform such tasks. To carry out its mission, the RTC was to receive powers identical to those of the FDIC—basic corporate powers—as well as several special powers. Included among the latter would be the power to enter into contracts with the FDIC or other entities, so long as the FDIC would be the RTC's "primary manager" and that all contracts other than those with the FDIC be subject to competitive bid. The RTC also would be given the power to set credit standards for institutions for which it was responsible, to require mergers or acquisitions, to organize federal mutual savings associations, and to review the 1988 FSLIC cases. Institutions managed by the RTC were to be restricted in certain ways—for example, with respect to asset growth, lending, use of brokered deposits, and interest rates. As for funding, the RTC would be given the power to issue capital certificates to the funding mechanism espoused by the administration (the Resolution Funding Corporation) and would be permitted to borrow \$5 billion from the Treasury.⁷ The RTC would be overseen by an Oversight Board, which would serve as the RTC's Board of Directors and would consist of the Treasury Secretary, the Chairman of the Board of Governors of the Federal Reserve System, and the Attorney General. The Oversight Board would appoint a CEO to head the new agency.

With respect to size, the administration initially conceived of the RTC as a relatively small entity. Although a Republican administration was forced to swallow the bitter pill of paying for a good part of the rescue with taxpayer dollars, it disdained to

⁵ Senate Committee on Banking, Housing, and Urban Affairs (1989b), 29. "The emergency nature of this legislation requires that Congress give the Executive Branch latitude to fashion a system in which the Administration has confidence. If time had permitted, however, the Committee would have expanded its hearings to include discussion of alternative means to accomplish the Administration's goals."

⁶ See the testimony by Treasury Secretary Nicholas Brady before the Senate (U.S. Senate Committee on Banking, Housing, and Urban Affairs [1989a], 23).

⁷ U.S. Senate (1989a), §501.

establish a large new federal bureaucracy.⁸ Certainly few in Congress or in the country at large would have applauded the establishment of such a bureaucracy, and if President Bush was going to persuade Republicans to support the plan, creating a large new agency would best be avoided. Treasury Secretary Nicholas Brady stated that the RTC was not envisioned as having a “large staff component.” Robert Glauber amplified on this vision during his confirmation hearings for the position of Undersecretary of Treasury for Finance in May, when he stated that the administration intended the RTC to be an “administrator of contracts” and that it was to be “a lean organization . . . that does not exceed 100 employees.”⁹

In retrospect, the part of the administration’s plan that called for the RTC to be a small organization was wholly unrealistic. Even if the RTC had been solely a contract administrator, the sheer volume of business in managing and disposing of assets would clearly have required many more people for adequate oversight. As it turned out, however, before FIRREA was passed the administration substantially altered its somewhat abstract notion of RTC management and structure.

Other aspects of the administration’s original plan for the RTC’s structure and function also underwent change, largely as a result of a debate that was mostly carried on within the government—unsurprisingly, given that the establishment of the RTC involved allocating and reallocating governmental responsibilities.¹⁰ Varying opinions from the administration, the FDIC, and Congress set the parameters of discussion. This fundamental dynamic did not prevent specific interest groups outside the government from playing a role in the RTC’s creation, nor did it mean that the RTC occasioned little comment. Two interest groups that sought to influence the shape of the RTC should be mentioned specifically. One was the real estate industry, which was concerned both with the effects of RTC operations on local real estate markets and with the role of private contractors in the management and disposition of assets. The second group consisted of affordable-housing advocates—groups pressing for an increased availability

of affordable housing for lower-income families. As for other interest groups, congressional perspectives inherently brought the viewpoints of various constituencies to the legislative process. This relationship was reflected especially in the opinions of legislators from areas such as the Southwest, where the S&L crisis and its attendant problems were particularly severe.

One group that played little or no role in the establishment of the RTC was the thrift industry itself. Insolvent thrifts, the group with which the RTC was to deal, could exert little influence on Capitol Hill. And as FIRREA progressed through Congress, it became clear that even on behalf of the industry’s surviving members, the once-powerful thrift industry lobby held much less sway with legislators than it had during the previous decade. The U.S. League of Savings Institutions, the industry’s trade group, had had tremendous influence in both Congress and with the FHLBB, and its agenda had shaped thrift deregulation in the early 1980s. The League successfully fought the Reagan administration in the mid-1980s as it sought ways to recapitalize the FSLIC, not only because such plans meant that the government would be able to close insolvent S&Ls (which, of course, made up a large and growing part of the League’s membership), but also because they normally involved some types of industry contributions. When recapitalization was finally enacted in the 1987 Competitive Equality Banking Act, the League still managed to decrease the amount from \$15 billion to \$10.8 billion. Just two years later, however, the industry’s power had waned and what little influence it had left was focused on areas far more important to the industry in the long run than was the RTC—areas such as

⁸ Secretary Brady did admit that the FDIC would probably have to increase its staff resources to manage the liquidation of RTC assets. He was uncertain just how many new staff members would be required but thought that added efficiencies would allow the increase to be rapidly scaled back (Senate Committee on Banking, Housing, and Urban Affairs [1989a], 619).

⁹ House Committee on Banking, Finance and Urban Affairs (1989a), 23. See also U.S. Congress (1989) (April 17), S3995; Senate Committee on Finance (1989), 7–49.

¹⁰ Of course, many parties outside government were very interested in the nascent RTC, particularly in the profits that could flow from being involved in the RTC’s work or from astutely adapting to its policies.

FIRREA's new regulatory regime and capital requirements. Certainly the industry was extremely interested in the amount of money it would be required to contribute to the RTC's funding, but here again, it had little effective voice in trying to increase taxpayer contributions while decreasing its own.¹¹ Although the thrift lobby did not completely ignore the RTC, apart from its role in funding the new entity, the industry paid comparatively little attention until the legislative process was well along.

Input from the FDIC

As noted above, the management structure initially envisaged by the administration was that a very small entity would be directed by a small group of senior officials and would contract its activities out primarily to the one existing government agency with experience in this area—the FDIC—but also to private sector firms. Some aspects of this initial plan were undoubtedly unworkable, but in any case the FDIC's leadership was unhappy with the agency's place in the division of responsibility and sought a more active role. Accordingly, a compromise was reached: the FDIC would become the RTC's exclusive manager, but an administration-controlled Oversight Board would determine overall strategy. Congress tinkered around the edges of this accommodation between the FDIC and Treasury but, because time was short, left it essentially intact. The compromise meant that the RTC's management structure would be unique—and complicated.

Pressure from Congress

In other areas, it was Congress that made significant changes and additions to the administration's plan—without much resistance from the administration. For one thing, the creation of a new government agency was guaranteed to provoke disagreement. For another, since the RTC was certain to spend vast amounts of taxpayer money and would control and dispose of a truly immense quantity of assets with the potential to affect markets across the nation, the administration's initial

undefined outline for the RTC was not likely to remain unaltered.

Congress viewed the administration's plan as imprecise and moved to refine it. The process was, of course, not one-sided, and the administration responded with clarifications of its own (as in the case of the Oversight Board).¹² In general, the administration sought to preserve what it viewed as necessary flexibility in the RTC's mission and operations.

Congressional critics, broadly speaking, focused their modifications on three areas (which were not necessarily mutually exclusive). First, because many observers both inside and outside Congress believed that the RTC had the potential to generate scandal and corruption on a grand scale, Congress looked to increase accountability within the RTC and among its ancillary functions.¹³ Second, because the experiences of both the FADA and the 1988 FSLIC deals were fresh in the minds of legislators, Congress tried to influence—in some respects very specifically—the way the RTC would do its job, something the administration tended to see as legislative micromanagement. Finally, Congress wanted to address public and social policy goals that were not necessarily immediately germane to the RTC's task. The administration opposed many of the proposed changes in this area, believing not only that they were a distraction but also that they might impair the RTC's

¹¹ The same might be said of the industry's ability to influence the administration. For example, the U.S. League of Savings Institutions sought a personal meeting with President Bush about a week before he was to announce his S&L cleanup plan, but since the League had already met with Bush's senior advisor on the matter (Richard Breeden), it was not granted a meeting with the president (GBPL F1002/003274: B. R. Beekma and Frederick L. Webber to Bush [January 30, 1989], and accompanying White House tracking worksheet).

¹² The conference report noted that the RTC provisions in the final bill consisted of "the Administration's proposal as modified by additional comments made by the Administration during the course of the conference" (U.S. House [1989c], 412).

¹³ For example, see Sen. David Pryor's statement that the RTC's activities would be a "fertile breeding ground" for scandal (U.S. Congress [July 17, 1989], S8058). Pryor introduced a separate "Ethics in Thrift Resolutions Act," which he hoped would be incorporated into FIRREA (S.1329): for purposes of conflict-of-interest and disclosure regulations, all contractors would have been treated as if they were agency employees. Even after the conference agreement, Rep. Toby Roth stated that the RTC contained the "seeds of a major scandal." (U.S. Congress [July 31, 1989], E2750).

ability to accomplish its mission at the lowest cost to the taxpayer, but it did not think any of these issues important enough to take a stand on, and virtually all of Congress's changes in these three areas were enacted with relatively little apparent discussion.

Such was not the case when it came to deciding just how to raise the money the RTC would receive to resolve insolvent thrifts. This question engendered the most partisan and prolonged debate associated with the RTC's creation. The estimates of how much money would be needed ranged widely, but once the administration adopted its \$50 billion estimate, most of the debate was driven by the politics of the budget deficit. The Republican administration wanted a funding structure that would put the expense "off-budget." The Democrats controlled Congress, and many of them wanted to fund the RTC with direct borrowing from the Treasury (a plan that would be less costly), which would move the expense "on-budget." The budget deficit, after decreasing in 1987 from all-time high levels in the two previous years, had risen substantially in 1988, and neither the administration nor Republicans in Congress were eager to fuel further increases in the deficit. Congressional Democrats' arguments about the costs of the "off-budget" plan were accurate, but a rising deficit also proved too useful a political cudgel to leave unused. This battle had the very real potential to disrupt and delay FIRREA's passage, but other than the (very salient) fact that the initial funding would quickly prove inadequate, the debate was mostly a political one and meant relatively little to the genesis of the RTC.

Management Structure: The Oversight Board, the FDIC, and the RTC

The Bush administration's initial plan for the Oversight Board was clearly designed to ensure the administration's control over the use of substantial amounts of taxpayer dollars. Because the administration would be held accountable for the RTC's use of the money, this approach was understandable. The Oversight Board, to be chaired by the

Secretary of the Treasury and also composed of the Chairman of the Federal Reserve Board and the Attorney General, was to serve as the RTC's Board of Directors and was to "review and have overall responsibility over the work, progress, management and activities" of the RTC. It was also to approve or disapprove of any RTC action, including those dealing with the disposition of individual institutions.¹⁴ The need for this kind of control was at least partly a byproduct of the perception that the deals put together by the FSLIC in 1988 had committed taxpayer dollars without authorization.

Congress essentially went along with the basic idea of Oversight Board control of the RTC. However, both the Senate and House suggested changes to the Board's composition, with each house's banking committee placing additional members on the Oversight Board. The Senate Banking Committee decided that two private sector individuals with experience equivalent to that of the CEO of a major corporation should be on the Board: many legislators thought that the named government officials would probably not have enough time to devote to the work of the RTC, and noted that these additions would add essential expertise in real estate and management.¹⁵ The whole Senate, spurred by concern about the local nature of real estate assets, added further private sector input by providing that 12 regional advisory boards be established.¹⁶ Treasury officials opposed the addi-

¹⁴ This power was reflected in early versions of the bills in both the House and Senate. See U.S. Senate (1989c), §501(\$21A(d)), and U.S. House (1989a), §501 (\$21A(c)(5)).

¹⁵ Senate Committee on Banking, Housing, and Urban Affairs (1989b), 29. Senator Robert Kerrey later introduced an amendment that would have created a seven-member Oversight Board. He wanted to add four private sector members having experience in banking, finance, real estate, and business management; reduce the government members to ex officio status; and have one of the private sector members appointed chairman by the president. He also argued that the government members, having their own substantial responsibilities, would be unable to devote adequate time to overseeing the RTC. His stated goal was to insulate the RTC from both political and financial pressure, and he predicted that Congress would regret its failure to create the position of a strong appointed chairman independent of direct ties to any interest group. His amendment was opposed by the administration as forcing it to relinquish too much authority. Many other senators felt that other safeguards, including regional advisory boards and stringent ethics requirements, would address Kerrey's concerns, and the amendment was defeated, 66-32. (U.S. Congress [April 17 and 18, 1989], S4012; S4074ff).

¹⁶ U.S. Congress ([April, 18, 1989], S4093).

tions to the Oversight Board, which they believed was properly made up only of public sector representatives. They argued that the RTC could draw from private sector expertise by establishing advisory groups and contracting with private sector firms.¹⁷

The House Banking Committee added three members: the Secretary of Housing and Urban Development (HUD), an individual from the private sector, and the Chairman of the FDIC as a nonvoting member.¹⁸ Banking Committee member Marge Roukema argued that adding the three new members would mean that “all relevant parties” were on the Board; the inclusion of the HUD secretary was logical because the department “already has experience in residential property disposition.” In response, Assistant Treasury Secretary David Mullins stated that although having the FDIC on the Board would not necessarily create a conflict of interest, the administration preferred that that agency not be represented.¹⁹ Another administration official labeled the inclusion of the FDIC a grab for power by the agency.²⁰ The emphasis on placing private sector experience on the Board, an emphasis that private real estate interests supported and lobbied for, stemmed from the notion that asset disposition was an activity with which government officials were unfamiliar—as had been attested to, many thought, by the experience of the FADA.²¹ For the most part the concern about asset disposition reflected fears that the new entity would engage in asset dumping.²² The whole House made other changes affecting the Oversight Board; perhaps most significantly, it required the Oversight Board to establish and oversee a minority outreach program to ensure that minority- and women-owned entities were included in contracts with the RTC.²³

The composition of the Oversight Board, however, was a relatively minor point of contention compared with the Board’s function. Indeed, the House Banking Committee’s inclusion of the FDIC Chairman as a nonvoting member of the Board foreshadowed the larger debate, which centered on the role of the FDIC vis-à-vis the role of the Oversight Board in the RTC. The crux of the question

had been identified in April by the U.S. General Accounting Office (GAO), which expressed concern about the administration’s conception of the Oversight Board as “operationally involved in decisions about case resolution.” Comptroller General Charles Bowsher argued that the RTC should make such decisions, with the Oversight Board “limited to evaluating the appropriate use of funds, and providing a check on the process.”²⁴

Although the GAO report was directed to Congress, the debate occurred not in that body but between the administration and the FDIC. As noted above, the administration plan placed the Oversight Board in charge of every aspect of RTC activity—but it also named the FDIC as the RTC’s “primary manager.” This nomenclature was puzzling to many. If the Oversight Board was charged with directing the RTC, just what was the FDIC’s role? The Senate Banking Committee, although it did not change the administration’s plan, noted that it was “not entirely clear how the relationship

¹⁷ GBPL OA/ID 02054: Memorandum from Gregory P. Wilson (Deputy Assistant Treasury Secretary for Financial Institutions Policy) to Robert R. Glauber (Undersecretary of Treasury for Finance Designate), April 20, 1989.

¹⁸ It was reported that L. William Seidman (Chairman of the FDIC) was encouraging Congress to replace the Federal Reserve member of the Oversight Board with HUD Secretary Jack Kemp (Rehm [1989a], 1). It was also reported that Kemp had been “angling” to play a role in the S&L rescue (*National Mortgage News* [1989a]). Shortly after the administration’s plan was announced, Kemp stated that the S&L industry’s rescue should be accompanied by a commitment to providing housing for the poor (Tolchin [1989]). Since the FDIC was to serve as primary manager for the RTC but the idea was that the Oversight Board might contract with other entities, the House made the FDIC’s position nonvoting so as to remove possible conflicts of interest.

¹⁹ For Roukema and Mullins, see Garsson (1989b).

²⁰ FDIC spokesman Alan Whitney said the FDIC had taken the position that it did not want voting membership and so was not seeking to increase its power (*National Mortgage News* [1989b]). However, when the FDIC presented its position on priority issues in FIRREA to congressional staff in late June, the agency recommended that the FDIC Chairman should be a voting member of the Oversight Board (Climo [June 23, 1989], 26).

²¹ See U.S. Congress (April 18, 1989), S4093.

²² The National Association of Realtors and the National Association of Homebuilders were prominent lobbyists on behalf of the inclusion of private sector members. See *National Mortgage News* (1989a). For the views of these groups, see also Senate Committee on Banking, Housing, and Urban Affairs (1989a), 469ff.

²³ House Committee on Banking, Finance and Urban Affairs (1989c), 356. The House bill was also more specific than the Senate’s about the nature of the Oversight Board, declaring that it was a body corporate and enumerating its powers as such.

²⁴ Letter from Comptroller General Charles Bowsher to Sen. Donald Riegle, April 7, 1989, printed in U.S. Congress (April 19, 1989), S4274.

between the RTC and its primary manager, the FDIC, will evolve.”²⁵ The FDIC and its chairman clearly did not approve of a system in which the agency was asked to shoulder the burden of conducting the S&L cleanup without having any say in how the cleanup would be run.²⁶

By June, negotiations between the FDIC and Treasury were under way to clarify the operating structure of the RTC and the Oversight Board’s powers. The administration proposed replacing the original and somewhat nebulous notion of the FDIC as “primary manager” with a structure in which the FDIC would be the “exclusive manager” of the RTC. In other words, instead of simply being the RTC’s primary (but not necessarily only) contractor, the FDIC would now run the RTC, and any contracts with private sector firms would be arranged and overseen by the FDIC. However, the FDIC believed that the draft management agreement presented by Treasury still gave the Oversight Board powers that would allow it to have too great an influence on RTC operations. The FDIC also believed that if the agency was to serve as the RTC’s exclusive manager, it ought to have a seat on the Oversight Board. Treasury rejected this position and insisted that the FDIC have no presence on the Oversight Board. In this impasse, Treasury sought to preempt further negotiation by setting out the FDIC’s role legislatively—that is, going through Congress to settle the argument. The FDIC Board responded by suggesting both to Treasury and to Congress that the FDIC’s Board of Directors serve as the RTC’s Board; that any funds appropriated for the S&L cleanup be appropriated directly for the FDIC’s use; and that supervision be provided by the president and congressional committees rather than by the Oversight Board.²⁷ Such a structure would, of course, have removed much of the administration’s control over the RTC and was therefore unacceptable to Treasury.

By mid-July the FDIC had become somewhat more conciliatory and proposed that the Oversight Board’s role in the formulation of policy be eliminated and, instead, that that body have the power to review RTC strategies and policies as well as to remove the FDIC from management of the RTC if

the agency’s performance was unsatisfactory. The FDIC proposals were provided to Sen. Donald Riegle.²⁸ The administration, too, sent proposals to the Hill; David Mullins (Assistant Secretary for Domestic Finance) stated that the administration had now removed all ambiguity from its proposal.²⁹ After several days of continuing negotiation, Treasury and the FDIC finally concurred on a draft management agreement that was formally sent to Congress on July 20. By this time the administration might have realized that the RTC was likely to be a potential magnet for problems, and although sharing responsibility with the FDIC meant having less control, it also provided cover. One financial services industry official noted at the time that the administration had become “skittish” in reaction to the problems associated with creating a new entity out of whole cloth to deal with such a large problem and had decided that delegating RTC activities to the FDIC was preferable to having sole responsibility.³⁰ In addition, the FDIC and its chairman were viewed very favorably, and the administration probably did not want to fight an even more public battle with the FDIC over the latter’s RTC role.

The Treasury–FDIC agreement retained the administration’s three-person Oversight Board, chaired by the Treasury Secretary. The Board’s authority, however, was fundamentally changed: it was now to develop and establish overall strategies and policies in consultation with the RTC. These overall strategies and policies included general policies for case resolutions, disposition of assets, the use of private contractors, the use of notes, overall financial plans and budgets, and restructuring the 1988 FSLIC deals. In addition, the Oversight Board would review and approve any financing requests and would review regulations and procedures, but with an important exception: it would have no authority over case-specific mat-

²⁵ Senate Committee on Banking, Housing, and Urban Affairs (1989b), 32.

²⁶ L. William Seidman (1993), 199–200.

²⁷ FDIC Board of Directors’ Minutes, June 27, 1989.

²⁸ *Ibid.*, July 12, 1989.

²⁹ Thomas (1989c).

³⁰ *BNA’s Banking Report* (1989d).

ters involving individual case resolutions, asset liquidations, or the day-to-day operations of the RTC. The FDIC was to serve as the exclusive manager of the RTC but could be removed by the Oversight Board if its performance was unsatisfactory. The FDIC Board of Directors would double as the Board of Directors for the RTC. Until the Oversight Board could establish policies, FDIC policies would govern the RTC.³¹

Treasury had succeeded in keeping the FDIC Chairman off the Oversight Board, but the FDIC had limited the ability of the Oversight Board to intervene in RTC operations.³² Deputy Treasury Secretary John Robson predicted that the FDIC and the Oversight Board would work in concert but acknowledged that he was also expecting “the FDIC [to] initiate a number of policies.”³³ The compromise created a bifurcation in authority, with the Oversight Board setting overall policies but the RTC making its own operational decisions. Potentially, such an arrangement could make management of the RTC unwieldy.

The FDIC and Treasury arrived at this agreement a little more than two weeks before a final statute had to be crafted (if it was to be completed before the August recess—a deadline that no-one wanted to miss), so Congress had little time to intervene. One congressional staff member complained that first the administration was admonishing Congress to speed up and pass the bill, “then they throw a whole new draft at us.”³⁴ Congress did not tamper with the agreement’s basic structure, but many legislators still felt that the nature of the RTC remained unclear. One attempt to clarify it was to require that the Oversight Board establish a strategic plan for conducting the RTC’s operations and submit it to Congress no later than December 31, 1989.³⁵ This requirement answered to the concern of some in Congress that the Oversight Board was an unaccountable entity.

Originally the Oversight Board had simply been a group of high-ranking government officials with broad responsibilities, and the administration’s bill stated that the Board would not be considered an agency of the United States government, a status that left it free of all sorts of statutory requirements

affecting the way in which it could act. But despite the administration’s general resistance to having constraints placed on this agency it was creating, by mid-July, in both the House version of the bill and in the Treasury–FDIC agreement, the Oversight Board had become an instrumentality of the U.S. government.³⁶

With regard to the membership of the Oversight Board, Congress insisted on nongovernmental representation and settled on a five-person scheme: the Secretary of the Treasury and the Chairman of the Federal Reserve remained; the Attorney General was removed in favor of the Secretary of HUD; and two independent persons to be chosen by the president and confirmed by the Senate completed the group. As had been the case from the beginning, the Secretary of the Treasury would serve as the Board’s Chairman. Although the administration did not favor independent members, both the House and Senate (at least partly at the urging of the real estate industry) had supported the idea, and since President Bush would nomi-

³¹ The agreement was in the form of statutory language and was provided to the House and Senate conferees to be considered for inclusion in Title V of FIRREA. The document dealt with many specifics, such as the exact corporate powers of both the Oversight Board and the RTC, compensation issues, the creation of the national and regional advisory boards, the development of policies and strategies for asset disposition, reporting requirements (both from the RTC to the Oversight Board and from the Oversight Board to Congress), legal issues such as the ability to sue and be sued, removal of actions from state courts, and so forth. See John E. Robson (Deputy Secretary of Treasury) and L. William Seidman (Chairman, FDIC) to Donald Riegler, Henry Gonzalez, Jake Garn, and Chalmers Wylie, with attached “Revised Version of Statutory Language Establishing the RTC” (July 20, 1989).

³² It should be noted that the Treasury–FDIC agreement also included some elements from the House and Senate bills, namely, specifying that the Oversight Board would be a body corporate with specific powers, establishing both national and regional advisory boards, and including at least some language about strategies for asset disposition. The agreement also included the House’s minority outreach program but, since the Oversight Board was no longer directly responsible for contracting, placed it within the RTC instead.

³³ Rehm (1989b), 1.

³⁴ *BNA’s Banking Report* (1989d).

³⁵ The plan would address 17 specific issues, including resolution practices, asset disposition, organization of the RTC, and minority outreach.

³⁶ In the Treasury–FDIC agreement, the Oversight Board had been specifically designated as not being an agency of the government. In FIRREA, the Board was an agency for the purposes of subchapter II of Chapter 5 and Chapter 7 of Title 5 of the United States Code. Chapter 5 deals with the Federal Administrative Procedure Act and concerns issues such as public information, records, proceedings, and rulemaking. Chapter 7 provides for judicial review of agency actions. In FIRREA the Oversight Board was also an agency for purposes of the conflict-of-interest rules of Title 18 of the United States Code (see Chapter 11, on bribery, grafts, and conflict of interest).

nate the two individuals, the administration probably did not perceive this as an issue on which it needed to take a hard and fast position.

In addition to its responsibility for setting overall policy for the RTC, the Oversight Board would approve RTC financing requests; establish the national and regional advisory boards; authorize the use of Resolution Funding Corporation (as noted above, a funding mechanism to be created by FIRREA) and Treasury funding; and could require the RTC to modify its rules, regulations, and guidelines. On the one hand, the administration retained a measure of control through the Oversight Board; on the other hand, by statute the RTC was given a much freer hand than the administration had originally intended. The real nature of the working relationship between the Oversight Board and the RTC (with the FDIC as its manager) was, however, an open question as the new entity began operations in August 1989. Later legislation would be required to clarify that relationship.

Accountability

The debate over the role and makeup of the Oversight Board was paralleled by discussion about the entity it was to oversee. As noted, some in Congress (and elsewhere) believed that, given the sheer volume and dollar value of assets involved, the RTC was destined to become a scandal of gargantuan proportions. Corruption, bribery, and favoritism, according to these observers, were likely to mar the RTC's work and add to taxpayer costs. After all, just when FIRREA was wending its way through the legislative process, Washington was preoccupied by scandals involving the misuse of funds, the overpayment of consultants, and charges of political favoritism at the Department of Housing and Urban Development in the Reagan administration.³⁷ Members of Congress, cognizant of the problems at HUD, were anxious to find ways to increase the RTC's accountability.³⁸ Significant mechanisms to ensure oversight and controls were therefore attached to the administration's plan, although some legislators

thought that even these changes did not go far enough (Rep. Toby Roth remarked that "two years from now . . . the RTC . . . will be a scandal so large that HUD will seem like a lemonade stand gone sour").³⁹

Perhaps the most basic way in which Congress sought to impose additional oversight was by altering the legal definition of the RTC. This impetus came mostly from the House and has been mentioned above in connection with the Oversight Board. The president's bill had stated that the RTC, like the Oversight Board, would not be considered an agency of the United States government. One House member suggested that the administration "wanted a body that was essentially undefinable, an entity that lives in the twilight zone between the public and private sectors."⁴⁰ Such a declaration was undoubtedly somewhat overwrought, but those sentiments were reflected in the House's decision to make the RTC—except when acting as conservator and receiver—subject to the Administrative Procedures Act and other laws.⁴¹ In opposing this change, one Treasury official argued that the more extensive the restrictions on the RTC, the more difficult it would be for that agency to "resolve institutions and dispose of assets in a cost-effective and non-controversial manner." A further Treasury argument was that because the RTC had a very specific task and a limited life, subjecting it to the Administrative Procedures Act

³⁷ See, for example, House Committee on Banking, Finance and Urban Affairs, Subcommittee on Housing and Community Development (1989). For a detailed synopsis of congressional action on the problems at HUD, see *Congressional Quarterly Almanac* (1990), 639ff.

³⁸ HUD was explicitly mentioned in the conference report. See U.S. House (1989c), 417.

³⁹ U.S. Congress (August 3, 1989), H4966.

⁴⁰ See Rep. William Gradison's remarks, U.S. Congress (May 2, 1989), E1469.

⁴¹ House Committee on Banking, Finance and Urban Affairs (1989c), 352. The Administrative Procedure Act, among other things, requires an agency to publish rulemaking procedures and hold hearings or provide other means of public comment on proposed rules, prescribes standards and procedures for agency adjudications, and provides for judicial review for any persons suffering legal wrong because of an agency action. Amendments to the law include the Sunshine Act and the Freedom of Information Act.

was inappropriate.⁴² The Senate, whose bill had followed the administration's plan, accepted the House position in conference, and the position was included in FIRREA as enacted.⁴³

Some of the most significant elements of these laws addressed conflicts of interest, but Congress did not stop at simply making the RTC subject to the laws governing U.S. agencies—it also demanded specific actions beyond what those statutes required. Within 180 days, the Oversight Board and RTC had to set down rules at least as stringent as those applicable to the FDIC governing conflict of interest, ethical responsibilities, and post-employment restrictions. Any RTC CEO was subject to a one-year revolving-door provision preventing him or her from immediately turning RTC service into profit in the private sector. All RTC and Oversight Board employees from other agencies were to file with the RTC whatever financial disclosure forms those other agencies required.

Because the RTC was to rely on the private sector, Congress was particularly concerned about potential abuses in contracting. The Oversight Board and the RTC were therefore required to create regulations on conflicts of interest and ethics for independent contractors, as well as on contractors' use of confidential information. The Oversight Board would prescribe regulations establishing procedures to ensure that contractors met certain minimum standards. Contractors had to provide a description of any instance within the preceding five years in which the person, or the company under that person's control, had defaulted on a material obligation to an insured depository institution. No one who had been convicted of a felony, or had been removed from or prohibited from participating in the affairs of an insured depository institution, or had demonstrated a pattern of defalcation regarding obligations to insured depository institutions, or had caused a substantial loss to federal deposit insurance funds, was to serve the RTC in any capacity. In addition, the Oversight Board was permitted to rescind contracts with individuals who fell into these categories, or who failed to dis-

close material facts, or who had been subject to a final enforcement action by any federal banking agency. Congress clearly sought to limit one perceived problem: the possibility that those who had helped create the S&L debacle through fraud or mismanagement would be able to profit from the cleanup.

The House Financial Institutions Supervision, Regulation and Insurance Subcommittee also adopted an amendment that designated the RTC as a "wholly-owned government corporation."⁴⁴ The House proponents of the amendment viewed this as an added precaution to ensure proper oversight of the RTC,⁴⁵ but the administration successfully lobbied against this proposal, and the RTC was designated a "mixed-ownership" government corporation, a move denounced by Rep. Paul Kanjorski as "a fiction designed to exempt it from a host of . . . laws and safeguards."⁴⁶ Although the administration generally sought to keep the RTC free of encumbrances, "mixed ownership" was the designation of the FDIC, and the administration thought it made sense to have the RTC given the same designation as the FDIC, which would, after all, be operating the new entity. In addition, the GAO had specifically recommended that the RTC be created as a mixed-ownership corporation.⁴⁷

The precise ramifications of the mixed-ownership status (as opposed to wholly owned status) are unclear, for in fact no definition for these terms

⁴² GBPL OA/ID 02054: Memorandum from Gregory P. Wilson through David W. Mullins, Jr., for Robert R. Glauber, April 20, 1989, 4.

⁴³ "Senate Offer on Selected Core Issues" (July 13, 1989), 19; U.S. House (1989c), 193.

⁴⁴ Rep. Paul Kanjorski put forward this amendment (*BNA's Banking Report* [1989a]).

⁴⁵ U.S. House Committee on Banking, Finance and Urban Affairs (1989b), 442.

⁴⁶ See U.S. Congress (April 3, 1989), H4993. See also Rep. Kanjorski's exchange with Treasury Secretary Brady in U.S. House Committee on Banking, Finance and Urban Affairs (1989a), 39–40.

⁴⁷ Letter from Comptroller General Charles Bowsher to Sen. Donald W. Riegle (April 7, 1989), printed in U.S. Congress (April 19, 1989), S4274.

exists.⁴⁸ In general, mixed-government corporation status was believed to provide greater financial and accounting flexibility.⁴⁹

Congress also chose a more direct route to increase the RTC's accountability: the imposition of very extensive reporting and auditing requirements.⁵⁰ Both the House and the Senate added these requirements, and for the most part the final statute reflected them. In debate on the Senate floor, Sen. Riegle noted that the Senate Banking Committee would be "very aggressive" in its oversight of the RTC and, through careful monitoring, would guard against the RTC's not "follow[ing] through on the original legislative intent."⁵¹ The GAO recommended reporting requirements to be certain the RTC "is accountable to the public and to Congress."⁵² Since many of those in Congress who were skeptical of the how well the RTC would function believed that the administration had not sufficiently defined the way the RTC would work, Congress chose to carve out a substantial role for itself in the oversight of the RTC's affairs, a role it did not later shrink from performing. Very soon after FIRREA was passed, the House Subcommittee on Financial Institutions Supervision created a separate RTC Task Force, something not mandated by FIRREA, to monitor the RTC, with Rep. Bruce Vento as its chairman.⁵³

The statute itself provided for an annual audit either by the Comptroller General or (in the event the Comptroller General declined to perform it) by an independent certified public accountant. The RTC and the Oversight Board were required to make all books and records available for this audit. The provision for the annual audit essentially mirrored the Senate version of the bill (the House bill would have required an annual GAO audit). The statute also called for the submission to Congress and the president of a full annual report of operations, activities, budget, receipts, and expenditures. In addition, there were to be specific semiannual reports to Congress, followed by appearances of the Oversight Board before the banking committees of both houses.⁵⁴ The law also mandated that the Oversight Board and the RTC send representatives to appear before Congress to report on the RTC's startup. On the

House's initiative, the statute established the position of Inspector General for the RTC and provided for the appropriating of funds for the office.⁵⁵ The administration does not appear to have opposed these kinds of requirements, at least some of which it may well have anticipated.⁵⁶

FIRREA also included various other mechanisms to ensure RTC accountability. The RTC was required to document decisions made concerning the solicitation and acceptance of offers⁵⁷ that involved both the acquisition of troubled institutions or assets. Legislators wanted to ensure that RTC procedures provided for fair competition and

⁴⁸ Wholly owned and mixed-ownership corporations are simply enumerated as such in the Government Corporation Control Act (U.S. General Accounting Office [1995], 3, n.6). Basically, each government corporation's enabling legislation may or may not enumerate that corporation's relationship to existing laws; after reviewing the statute, each corporation decides just how it will operate. It is telling that in 1995, when the GAO sought to determine which laws government corporations adhered to, it surveyed them to find out what they did in practice. The RTC reported that it was wholly subject only to 3 of 15 statutes listed by the GAO, partly subject to 5 others, and not subject at all to the remainder, although it followed some of the other laws nevertheless (*ibid.*, 123-29). (The RTC claimed it was wholly subject to the Government Corporation Control Act, the Inspector General Act of 1978, and the Ethics in Government Act of 1978; partly subject to the Privacy Act of 1974, the Freedom of Information Act of 1966, the Federal Tort Claims Act, the Anti-Deficiency Act, and the Chief Financial Officers Act of 1990; and not subject at all to the Government in the Sunshine Act, Title 5: Employee Classification, Title 5: Pay Rates and Rate Systems, the Federal Property and Administrative Services Act of 1949, the Federal Managers Financial Integrity Act of 1982, the Government Performance and Results Act of 1993, and the Federal Credit Reform Act of 1978. However, some wholly owned government corporations were also not subject to these same laws (*ibid.*, 34-35). A 1981 study by the National Academy of Public Administration defined mixed-ownership corporations as those having a "combination of governmental and private equity" (National Academy of Public Administration [1981], 1:20). However, this definition does not apply to all mixed-ownership corporations. The FDIC, for example, repaid the government's stake in its fund long ago.

⁴⁹ Moe (1995), 6, n.21.

⁵⁰ The administration bill eventually came to include reporting requirements for the RTC. These reports and audits were, however, designed to provide information for the scaled-down version of the Oversight Board ("Revised Version of Statutory Language Establishing the RTC," 34).

⁵¹ U.S. Congress (April 18, 1989), S4079.

⁵² Comptroller General Bowsher to Sen. Riegle, U.S. Congress (April 19, 1989), S4274.

⁵³ McTague (1989).

⁵⁴ The semiannual reports were to include statements of book value of assets, total book value of RTC assets under private management, total book value and sale value of assets during period, data on discounts from book value on assets sold, list of areas designated as distressed and evaluation of markets in those areas, staffing numbers, information on any change adopted by the Oversight Board in a minimum disposition price, and the methods adopted by the RTC to value assets and the reasons these methods were chosen.

⁵⁵ House Committee on Banking, Finance and Urban Affairs (1989b), 443.

⁵⁶ For example, the joint Treasury-FDIC version of the RTC portion of Title V included the House provision for an IG ("Revised Version of Statutory Language Establishing the RTC," 38).

⁵⁷ U.S. House (1989d), 413.

the consistent treatment of qualified bidders while minimizing costs to the government. With regard to acquisitions, clearly the 1988 FSLIC deals were uppermost in the minds of legislators.⁵⁸ One congressman who worked on this provision noted that “we need this type of information if we’re going to avoid the RTC repeating the December 1988 deals.”⁵⁹ The RTC was also required to publicly disclose any assistance transaction agreements and all agreements relating to 1988 FSLIC cases that it reviewed, unless the Oversight Board unanimously determined that disclosure would be against the public interest; all such transactions were, however, to be made available to Congress.

The 1988 deals were responsible for a House provision designed to impose accountability on the RTC: the imposition of a cap on the issuance of RTC obligations. Banking Committee Chairman Henry Gonzalez argued that, without such a provision, “the [1988 FSLIC deals] could be repeated on a grander scale,” and stated that the RTC “should not hold a blank check on the U.S. Treasury.”⁶⁰ His solution was to limit the RTC’s total debt by creating a formula: the sum of contributions from the Resolution Funding Corporation (the RefCorp—the funding mechanism created by FIRREA) and the RTC’s outstanding obligations minus the sum of the RTC’s cash and the total fair market value of its assets could not exceed \$50 billion. With the RefCorp originally envisioned to raise \$50 billion, this would place a cap on RTC outstanding obligations equal to the sum of its cash, the fair market value of its other assets, and the balance of RefCorp bonds remaining to be issued. In addition, Rep. Gonzalez proposed other limitations on the RTC’s ability to obligate the government, including—with yet another glance at the 1988 deals—a prohibition against entering into any agreement that did not specify the maximum dollar amount for which the RTC would be liable.⁶¹ The amendment passed the House on a voice vote.

The Senate had not included an obligations limit but accepted the House provision in conference and proposed that it be modified to conform to the Senate language limiting FDIC borrowing (this

language prevented the FDIC from issuing notes in excess of 85 percent of the fair market value of assets and required the FDIC to include the estimated costs of any guarantees as a liability). The Senate applied the same rules to RTC borrowing but maintained the House language allowing RefCorp funding authority not to be treated as an asset subject to the 15 percent discount. The 15 percent haircut was intended to provide a cushion against inaccurate or changing asset valuations. The Senate also extended the full faith and credit of the United States to RTC obligations.⁶² The administration had argued that Congress needed to give the RTC the flexibility to issue notes and guarantees for working capital, especially before it received RefCorp funds. If such a limit were adopted, it preferred that obligations be measured against the full amount of resources authorized to be available to the RTC (RefCorp contributions and assets acquired from insolvent thrifts) rather than that a 15 percent haircut be imposed on the fair market value of noncash assets.⁶³ The Senate version of the limitation on obligations was included in FIRREA.⁶⁴

The note cap did end up placing potential constraints on RTC operations, but these went well beyond the constraints the administration had envisioned in criticizing the note cap. Within just a few months it became evident that the RTC’s need for working capital would push far higher

⁵⁸ Senate Committee on Banking, Housing, and Urban Affairs (1989b), 30–31.

⁵⁹ Rep. David E. Price, U.S. Congress (June 14, 1989), H2568.

⁶⁰ *BNA’s Banking Report* (1989b); U.S. Congress (June 15, 1989), H2749.

⁶¹ U.S. Congress (June 15, 1989), H.2752.

⁶² “Senate Offer on Selected Core Issues,” 19. The FDIC supported the idea of limiting the RTC’s ability to incur debt but opposed the House version, saying that it was “so strict as to effectively prohibit the efficient functioning of the RTC” (Climo [1989], 28).

⁶³ *BNA’s Banking Report* (1989c). See also Rep. Chalmers Wylie’s statement in U.S. Congress (June 15, 1989), H2751.

⁶⁴ The note cap formula in FIRREA was as follows: (RefCorp contributions + total outstanding RTC obligations) – (RTC cash held + 85 percent of fair market value of RTC assets) could not exceed \$50 billion. Full faith and credit was extended only if the principal amount and the term of the obligation were stated in the obligation. (This provision was therefore similar to the House maximum dollar amount noted above.) The law also required the RTC to estimate contingent liabilities quarterly and to include such liabilities in financial statements.

than the limit set by FIRREA. The law had provided the RTC with the ability to borrow \$5 billion from the Treasury, but the RTC estimated it would need between \$40 billion and \$100 billion for working capital. Significant discussions during late 1989 and early 1990 were required to arrive at a solution: the RTC was allowed to borrow from the Federal Financing Bank to fund its working capital needs.⁶⁵

Legislative Management

Imposing adequate accountability was only one way in which Congress tried to change how the RTC would work. Legislators also sought to intervene directly in the new agency's operations. As was mentioned above in connection with the Oversight Board, Congress tried to impose direction on the RTC's management by requiring a strategic plan. This idea originated in the Senate, where it was mostly tied specifically to asset disposition methods. Sen. Riegle noted that the strategic plan was included to address concerns about the effects of such massive asset sales, particularly in areas of the country where markets were already depressed.⁶⁶ The Senate bill required the RTC to develop the plan, but when the role of the Oversight Board was redefined to focus on overall strategy and policy, the House-Senate conference placed responsibility for the plan with the Oversight Board instead. At the same time, the content of the plan was broadened significantly to cover almost every aspect of RTC operations. Although the strategic plan does fit under the rubric of legislative management, the actual implementation of the plan was still up to the RTC, under the supervision of the Oversight Board; and the statute did not spell out the role of the plan in the RTC's operations. As things turned out, after the strategic plan was drafted it was rarely mentioned, but at the same time the RTC generally operated in accordance with it.

Congress was more specific in insisting that the RTC use the private sector in carrying out its mission. Both the House and the Senate bill incorporated language to that effect, and there appears to

have been little resistance to such provisions. Certainly use of the private sector dovetailed with the notion that the RTC would have only a short life and that a large new government bureaucracy would not be created. In addition, many believed the government had neither the manpower, nor the experience or expertise to handle asset disposition effectively. The author of the House provision, Thomas McMillen, stated that Congress needed to "set up a system designed to utilize the forces of free enterprise and market competition" as a way to get both high-quality service and cost competition; disposing of these assets would require entrepreneurial individuals with experience in business, finance, real estate, and accounting, and this was "not the substance of government" but was, instead, "the substance of [the] . . . highly competitive commercial marketplace."⁶⁷ Connie Mack, one of the authors of the Senate provision, stated that "private enterprise needs to be used to the fullest possible extent" and that the bill made clear Congress's preference for the private sector to be used in management of the disposal of thrift assets.⁶⁸

Emphases did differ. For example, the House approach was more zealous, stating that the private sector should be used unless such services were unavailable, impracticable, or inefficient.⁶⁹ The Senate, on the other hand, included a provision that the private sector should be used if such serv-

⁶⁵ The debate over working capital lasted well into 1990 and was bound up with the partisan politics of the budget; this issue is discussed fully in Davison (forthcoming).

⁶⁶ U.S. Senate (1989b), 334. This Senate version of the strategic plan requirement called for the RTC to develop a plan and implement procedures to maximize net present value return from assets, minimize disruption to local real estate markets, and provide for an adequate level of capital for itself. The plan was to provide for efficient disposition of assets, taking into consideration market conditions, financing standards, asset values, expenses and risks of holding assets, and so forth. Policies were also to provide for adequate competition and fair and consistent treatment of third parties seeking to do business with the RTC. See also U.S. Congress (April 18, 1989), S4075. The House also had a plan related to asset disposition but called it a "business plan" rather than a strategic plan; it dealt with the orderly disposition of assets in areas that might be adversely affected by those transactions (U.S. House [1989b], 224).

⁶⁷ U.S. Congress (June 6, 1989), H2341. He noted that his amendment was "overwhelmingly adopted" in committee.

⁶⁸ U.S. Congress (April 19, 1989), S4284.

⁶⁹ U.S. House (1989b), 219. Rep. Thomas McMillen was responsible for the language used in the House approach.

ices were available, practicable, and efficient.⁷⁰ In the Treasury–FDIC agreement of July 20, written with knowledge of the provisions already adopted on the Hill, the RTC was permitted to use the private sector if the services were available and were determined to be practicable and efficient.⁷¹ In other words, the administration, as always, sought to preserve flexibility. Ultimately the middle road of the Senate language was adopted, making it clear that the law intended the RTC to use such services but providing the new agency with discretion in choosing how to use them.

Although use of the private sector to dispose of failed-institution assets was incorporated into the law, details about the asset disposition process received much more emphasis, with particular attention paid to the disposition of real estate assets. For example, the sole provision—it was originated in the House—that actually sought to define the internal organizational structure of the RTC required that the RTC establish a real estate asset division. The division’s purpose would be to ensure the “orderly disposition of real property assets by exercising primary responsibility over actions of conservators, receivers or managers of institutions with respect to the management, sale or disposal of real property assets.”⁷² The division was specifically required to publish an inventory of real property assets of institutions under the RTC’s jurisdiction.⁷³ Treasury apparently opposed the House’s provision in the belief that “the RTC should not be encumbered by legislative mandates as to operating structure.”⁷⁴ The provision was, however, agreed to by the Senate in conference,⁷⁵ and it remained in the legislation as enacted. But the RTC’s organizational structure would undergo so many metamorphoses that this initial mandate was not particularly meaningful.

Congress also believed that the RTC should consult with experts from outside the government on real estate assets and provided for the creation of advisory groups. To some extent this was a response to the urging of the real estate lobby, whose members were concerned about asset dumping and its effects on local markets. The Senate bill called for regional advisory groups and the

House bill for both a national advisory board and regional boards. One observer noted that the advisory boards might be useful but that, if they were merely political entities protecting local interests, they would be ignored.⁷⁶ And indeed Treasury initially opposed such groups not only because it saw them as reducing the RTC’s flexibility but also because it questioned their ability to be “sufficiently objective to support the best long-term solution to the overhang of properties in those local markets” (that is, in distressed areas).⁷⁷ However, the advisory boards were included in the Treasury–FDIC language sent to Congress in July, and the statute provided for both the national and regional advisory boards.⁷⁸ The statute, however, placed no precise requirements on either the RTC or the Oversight Board for following the recommendations of these groups.

Both the House and Senate did add prescribed goals for RTC asset disposition. First and foremost, the Senate bill, trying to dictate the rules under which RTC decisions would be made, required that the RTC obtain maximum net present value from assets under its control. Seeking to accom-

⁷⁰ U.S. Senate (1989c), §501(v).

⁷¹ “Revised Version of Statutory Language Establishing the RTC,” 22.

⁷² House Committee on Banking, Finance and Urban Affairs (1989b), 440.

⁷³ This inventory was to be published by January 1, 1990, and was to be updated semiannually. This inventory was also to list properties with natural, cultural, recreational, or scientific value of special significance. This was an adaptation of a provision written by Sen. Tim Wirth and included in the Senate-passed bill; Wirth’s approach would also have required that the list be provided to appropriate federal and state agencies so they could act to acquire the properties (U.S. Congress [April 19, 1989], S4252; Senate Committee on Banking, Housing, and Urban Affairs [1989b], 204).

⁷⁴ GBPL OA/ID 02054, 3.

⁷⁵ “Senate Offer on Selected Core Issues,” 17.

⁷⁶ *National Mortgage News* (1989a). It was noted that both the realtors and the home builders supported the creation of advisory groups.

⁷⁷ GBPL OA/ID 02054, 1–2.

⁷⁸ Both types of advisory board were to be established by the Oversight Board. The national board was to advise the Oversight Board on policies for the disposition of real assets and was to consist of a chairman appointed by the Oversight Board and the chairmen of any regional advisory boards. FIRREA required the Oversight Board to establish at least six regional boards (wherever it was determined that a significant real estate asset portfolio existed) to advise the RTC on the disposition of assets. Each regional board was to have five members, serving two-year terms but at the pleasure of the Oversight Board, and the members were to be selected from among local residents “who [would] represent the views of low- and moderate-income consumers and small businesses” or who were knowledgeable about business, finance, and real estate. All the boards were to meet at least four times a year.

moderate real estate interests, the Senate qualified this by adding that the RTC should also minimize disruption to local economies. The House followed with similar language but added affordable housing provisions (see below). Again, the legislative proposal was colored by fears of asset dumping. The Senate Banking Committee mentioned its belief that HUD's real estate auctions in Denver had depressed that city's residential real estate market, and stated that it "expected the RTC to maximize net present value without damaging local markets."⁷⁹ Moreover, the committee added a separate provision that would prevent the RTC from selling real property assets in "distressed areas" (designated as Arkansas, Colorado, Louisiana, New Mexico, Oklahoma, and Texas, although the law also empowered the RTC Board of Directors to change these designations) for less than 95 percent of the market value established by the RTC.⁸⁰ Congressional alterations to the bill submitted by the administration thus began to include potentially contradictory goals and therefore began to blur the mission of the RTC.

Treasury officials opposed such proposals as a "prescription for gridlock," stating that "the overriding purpose of the RTC is to resolve failed thrifts and manage the disposition of assets in the most cost-efficient manner possible for the taxpayer. To do this the RTC requires flexibility, not a 'straitjacket' of conflicting objectives."⁸¹ The administration took congressional opinion into account in the Treasury-FDIC agreement sent to Congress in July, which included a requirement for "the development of a business plan for the disposition of assets in geographic areas that might suffer significant adverse effects as a result of conditions in local real estate or financial markets."⁸² All of the relevant House and Senate provisions, however, were retained in the legislation eventually enacted.

Social and Public Policy Objectives

Congressional concerns about asset disposition did not stop with questions of asset dumping and local markets but extended to the accomplishment of wider policy goals. In the case of asset disposition, the House added provisions to "provide homeown-

ership and rental housing opportunities for lower income families."⁸³ (Affordable housing issues were also dealt with elsewhere in FIRREA.)⁸⁴ Reps. Barney Frank and Henry Gonzalez championed this idea, arguing that although the RTC needed to make maximum use of assets from failed institutions, such property ought not to be turned over to speculators at fire sale prices, further depressing local markets. Instead, true maximum value would be obtained by the use of residential property whenever possible to fulfill local housing needs.⁸⁵ In the Senate, John Kerry, citing the same goals as Reps. Frank and Gonzalez, put forward a similar plan that was narrowly defeated in committee.⁸⁶

In the House bill, the chief mechanism for using the RTC to provide affordable housing was to grant qualified nonprofit organizations, public agencies, or lower-income families a 90-day right of first refusal to purchase residential properties. Originally this right was intended to apply to all RTC property (whether the RTC was acting as conservator or as receiver) with certain appraised values, and a proportion of all RTC property sold was to be reserved and maintained for this purpose (20 percent for "very low-income families" and an additional 5 percent for "lower-income fami-

⁷⁹ Senate Committee on Banking, Housing, and Urban Affairs (1989b), 30.

⁸⁰ *Ibid.* The committee noted that it did not intend its market valuation requirement as a mandate to obtain an appraisal in all cases, countenancing other valuation techniques when appropriate (and this flexibility was reflected in the statute, which stated that the RTC was to "establish an appraisal or other valuation method for determining the market value of real property"). Treasury opposed this provision, noting that the RTC was being established "precisely because of these distressed areas and the intractability of dealing with their problems. To now burden the RTC with restrictions on its activities in these areas is to severely compromise its operations and to render superfluous its establishment" (GBPL OA/ID 02054, 2).

⁸¹ GBPL OA/ID 02054, 3.

⁸² "Revised Version of Statutory Language Establishing the RTC," 27.

⁸³ There were no comparable provisions in the Senate bill, although the Senate Banking Committee noted that in certain cases sales to public housing agencies might obtain true maximum value (Senate Committee on Banking, Housing, and Urban Affairs [1989b], 30).

⁸⁴ Title VII included a community investment program and an affordable housing program through the Federal Home Loan Banks; Rep. Henry Gonzalez sponsored these plans.

⁸⁵ U.S. Congress (April 4, 1989), H914.

⁸⁶ U.S. Congress (April 19, 1989), S4303.

lies”).⁸⁷ If residential units were sold to a single organization, 20 percent of those units were to be reserved and maintained for very low-income families, and an additional 15 percent for lower-income families. Purchasers setting aside a higher percentage of units for such families were to receive preference among substantially similar offers. In addition, the RTC was to sell such properties under net realizable market value and was allowed to provide loans to purchasers at reduced interest rates to the extent necessary to allow a purchaser to comply with the lower-income occupancy requirements. The House also provided for assistance by HUD and the Farmers Home Administration (FmHA) by increasing the budgets for certain programs administered by the appropriate agencies.

In subcommittee, Rep. Chalmers Wylie—a Republican acting on behalf of the administration—succeeded in changing the affordable housing program from a mandatory to a discretionary one, but Rep. Frank, partly by dropping the notion that a proportion of all RTC property would be reserved for lower- and very low-income families, succeeded in restoring it in full committee by a vote of 33–18.⁸⁸ In June the administration “urged the deletion of housing subsidies” to be provided by the RTC and the Federal Home Loan Banks under the bill. Congress, it was argued, should not “grant preferential rights to purchase assets of failed thrifts to any group” but, instead, should deal with affordable housing in separate legislation.⁸⁹ Rep. Wylie stated that the RTC’s business was the disposition of real estate and that Congress could not “afford to tie the hands of the RTC with unwieldy, mandatory procedures.”⁹⁰ Treasury officials had previously opposed the provision for RTC loans to purchasers of residential property, noting that making such loans was well outside the RTC’s primary mission and that there was no need for the RTC to compete with other credit providers in order to dispose of assets. Moreover, the officials believed that long-term lending was incompatible with the short-term life of the RTC.⁹¹

The Senate, having voted down affordable housing provisions in committee, reversed course in conference. Although senators accepted the basic ideas

put forward by the House, they wanted these refined in such a way as to ensure that the program did not “interfere with efficient asset disposition by the RTC, require the RTC to sell properties at below market prices, or provide below-market-rate financing.”⁹² Such a stance was much more in line with the administration’s position. The House–Senate conference made substantial changes to the residential properties disposition program, creating different rules for single and multifamily properties and clarifying the process for each.

For single-family properties the RTC, “within a reasonable time after acquiring title,”⁹³ was to give written notice to “clearinghouses”⁹⁴ providing basic information about the property. These clearinghouses were to make the information available to other public agencies, nonprofits, and qualifying households, and the RTC was to provide reasonable access to the properties. For the three months after the RTC made an eligible property available for sale, the agency was to offer the property only to qualifying households, nonprofits, or public agencies that would either make the property available for occupancy by, and maintain it for occupancy by, lower-income families, or would make it available for such families to purchase. After the three-month period, the RTC could offer to sell to any purchaser.

For multifamily housing, the RTC was again to provide written notice to the clearinghouses containing basic information about the property, as

⁸⁷ Very low-income families were defined as earning less than 50 percent of median income, and lower-income families were defined as earning less than 80 percent but more than 50 percent.

⁸⁸ See Pulles et al. (1989–98), 800–801. For the final version of the House bill, see House Committee on Banking, Finance and Urban Affairs (1989b), 136ff.

⁸⁹ *BNA’s Banking Report* (1989c).

⁹⁰ Wylie sought to reintroduce his amendment on the floor but was ruled out of order (U.S. Congress [June 14, 1989], H2538).

⁹¹ GBPL OA/ID 02054, 3.

⁹² “Senate Offer on Selected Core Issues,” 7.

⁹³ This was significant because, unlike the House language, it would not apply to assets in RTC operating conservatorships.

⁹⁴ Defined as state housing finance agencies, offices of community investment within the Federal Housing Finance Board, and national nonprofit entities selected by the RTC.

well as reasonable access. Qualifying purchasers were allowed to give written notice of serious interest during the 90-day period after notice was provided to the clearinghouses or until the RTC determined a property was ready for sale, whichever came first. The RTC was then required to give notice to those who had expressed interest, after which those parties had 45 days to make an offer. Multifamily properties were subject to lower-income occupancy requirements (at least 35 percent of units had to be reserved for lower-income families, and at least 20 percent for very low-income families). The RTC could sell to other purchasers after the 90-day period if no qualified purchaser had expressed serious interest. The RTC was to give preference among substantially similar offers to those that reserved the highest percentage of units for lower-income occupancy.

In addition, the conference removed the new funding (just over \$500 million for fiscal year 1990) that the House had included for HUD and FmHA financing, and replaced it with statements directing the relevant cabinet officials to provide expedited assistance to purchasers under laws already on the books. The conference also weakened the House's requirements concerning sale and financing: the RTC, rather than being required to sell properties below the market price, was permitted to do so if that would facilitate the goals of the affordable housing program. Moreover, the RTC was again allowed—not required—to provide loans to purchasers at below-market interest rates in order to facilitate expedited sales to qualified owners. All these changes essentially reflected Senate positions.⁹⁵ The law also provided for rent ceilings on multifamily properties for very low- and lower-income tenant families.

Although some of the more ambitious goals of House Democrats were not achieved in FIRREA, affordable housing provisions certainly made their mark on the statute, and even if the volume and number of assets in these programs would prove to be relatively small, the law nevertheless required a significant effort on the part of the new agency. The administration apparently did not think it

advisable to make a stand on affordable housing, despite its view that the provisions were incompatible with the RTC's mission. In any case, given that House Banking Committee Chairman Gonzalez backed the inclusion of affordable housing measures, compromise on this issue was probably necessary to ensure passage of the legislation.

Congress sought to address another social policy goal through the RTC in another and very different way: by including minorities and women in the S&L cleanup process. The House bill required the Oversight Board to create a minority outreach program to ensure “inclusion, to the maximum extent possible of minorities and women, and entities owned by [them]” in all RTC contracts. The House bill contained another provision that called for the RTC to establish policies that “called for the active solicitation of offers from minorities and women” and specified reporting requirements that would detail the number of women and minority investors participating in the bidding for both acquisitions and assets.⁹⁶ In the Senate, Alan Cranston had successfully put forward an “equal opportunity” amendment requiring that all the banking agencies, including the RTC, were to establish programs for soliciting business from such entities in their procurement programs.⁹⁷ The Senate apparently was willing to accept the House provision for an outreach program led by the Oversight Board, but that provision was not included in the final law.⁹⁸ Instead, policies on outreach programs were included in the required strategic plan; and the reporting requirements were retained, as was the general equal opportunity provision. Congress would, however, return to the subject of minority- and women-owned businesses in future legislation concerning the RTC, and the subject

⁹⁵ “Senate Offer on Selected Core Issues,” 8.

⁹⁶ House Committee on Banking, Finance and Urban Affairs (1989b), 126–27, 132, 143.

⁹⁷ Senate Committee on Banking, Housing, and Urban Affairs (1989b), 289–90.

⁹⁸ “Senate Offer on Selected Core Issues,” 18.

would remain an important aspect of the agency's political environment.

Funding for the RTC

The most contentious RTC-related battle between the Republican administration and the Democrat-controlled Congress was fought over the manner in which funding for the cleanup would be provided to the RTC. The RTC's funding was entangled in the politics of the budget, and specifically in the constraints of the Gramm-Rudman-Hollings deficit reduction law (GRH).⁹⁹ Once the amount of the funding had been decided, the method of providing the funding made no difference to the way in which the RTC would be structured or would operate. Nonetheless, the method generated heated rhetoric and threatened to delay or even scuttle the bill.¹⁰⁰

The administration plan provided \$50 billion for the RTC to use in resolving insolvent institutions. The \$50 billion would be raised through the sale of bonds by the RefCorp. This approach mirrored the one taken in 1987, when the Competitive Equality Banking Act established the Financing Corporation to issue bonds to raise funds to recapitalize the FSLIC. This approach also met the highly desirable (for the administration) goal that the spending on the RTC's caseload would not increase the reported U.S. budget deficit (as Treasury funding would) and therefore would neither invoke sequestration under GRH nor require increased taxation to avoid sequestration.¹⁰¹ However, many Democrats and some Republicans questioned this course, preferring that Treasury provide the funds to close failing thrifts.

The merits of on-budget versus off-budget financing became by far the most politically charged issue accompanying the creation of the RTC. Although Democrats in Congress undoubtedly pushed for on-budget financing as a way to embarrass the Bush administration by increasing the budget deficit in the face of Bush's "no-new-taxes" pledge, the substantive argument put forward for on-budget financing was simple: RefCorp-issued bonds, because they would not be considered Treas-

ury-backed securities, would carry a higher interest rate than Treasury obligations. Financing under the Bush plan would, therefore, be significantly more expensive than direct Treasury borrowing; the figure most often cited was approximately \$4.5 billion over the life of the bonds. In addition, opponents of off-budget financing saw the plan as a dangerous precedent that would encourage future administrations to establish such entities as a way to avoid future budget targets.

The administration argued that although there might be additional costs, they would be outweighed by the benefits of the off-budget approach. Administration officials stated that using \$50 billion in Treasury funding but exempting it from GRH could push up domestic interest rates (possibly defeating the purpose of lowering the borrowing cost) because that action would cause domestic markets and foreign nations to question the U.S. commitment to lowering the budget deficit.¹⁰² The administration also argued that because the \$50 billion principal of the RefCorp's bonds would be financed by contributions from the S&L industry (the interest would be paid by the Treasury), treating the principal on-budget would be unnecessary.

⁹⁹ Its proper title was the Balanced Budget and Emergency Deficit Control Act of 1985; it was amended by the Balanced Budget and Emergency Deficit Control Reaffirmation Act of 1987.

¹⁰⁰ Throughout the RTC's existence, the most acrimonious debates were engendered by funding. The legislative history of the agency—from FIRREA through the RTC Funding Act of 1990, the RTC Refinancing, Restructuring and Improvement Act of 1991, and the RTC Completion Act of 1993—is partly a history of the corporation's funding, for each piece of legislation contained a funding component. The decisions made before passage of FIRREA set the terms of that funding history.

¹⁰¹ GRH created "maximum deficit amounts." If these were exceeded, the law mandated that the president issue an order (a sequester order) to reduce all nonexempt spending by the same percentage.

¹⁰² See Thomas (1989a). See also Nicholas Brady's testimony before the House Committee on Banking, Finance and Urban Affairs (1989a), 26. The Congressional Budget Office (CBO) was among those suggesting direct Treasury borrowing and exemption of the spending from GRH. See House Committee on Ways and Means (1989), 237–40. But the CBO director, James Blum, also noted that this was fundamentally a political question that had to be decided by the president and Congress. Economist Martin Feldstein also supported the CBO's position, arguing that the RefCorp should be scrapped in favor of direct Treasury borrowing but that the \$50 billion could be exempted from GRH because the "rescue plan would neither increase aggregate spending nor crowd out any private borrowing" (Feldstein [1989]).

In the Senate, Banking Committee Chairman Riegle put forward his own financing design in opposition to the administration's plan: he wanted Treasury to sell the bonds and then transfer the proceeds to the RefCorp. This would save money but still use the administration's mechanism. (Of course, this plan ignored the fact that there was little point in creating the RefCorp if it simply funneled Treasury funds to the RTC.) Riegle avoided the GRH-mandated cuts by putting the entire cost into the current fiscal year (1989), where, for the purposes of GRH, it had no effect.¹⁰³ This accounting procedure was fairly transparent, and, some argued, would make it plain that the U.S. government was willing to ignore budget discipline. Sen. Riegle's amendment failed in committee by a single vote. Sen. Alan Dixon stated that although he believed the direct Treasury financing approach would reduce the cost of the cleanup, he voted against it in committee because the support required for passage on the Senate floor could not be obtained, and in his view the need to pass the bill outweighed the merits of Riegle's plan.¹⁰⁴ Republicans noted that the threat of a presidential veto also influenced the committee's vote.¹⁰⁵

Despite this setback, when the bill reached the Senate floor the Democrats renewed their efforts and again generated considerable debate. Republican Jake Garn probably captured the Senate's true feelings when he remarked that neither of the funding mechanisms was particularly desirable and that "all of us would prefer to be someplace else doing something else" but that they needed to get the bill passed quickly.¹⁰⁶ The Democrats' plan fared better than it had in committee, but failed again. The vote was almost completely along party lines: only a single Republican voted for it, and only six Democrats against it.¹⁰⁷ Once it became clear that the Treasury financing approach was doomed, however, senatorial pragmatism took hold, and the Senate overwhelmingly passed the bill with the administration approach intact, 91–8.¹⁰⁸

Democrats in the House also sought to change the financing scheme. In the House Banking Committee Reps. Joseph Kennedy and John LaFalce

both introduced amendments that would have used an on-budget, taxpayer-financed plan, a course that had no chance of succeeding. Because the House Banking Committee was not the appropriate venue for tax bills, these amendments were not even considered. The Ways and Means Committee was, however, the proper place for such bills, and the vote there was 25–11 in favor of Dan Rostenkowski's plan for direct Treasury financing, but with the \$50 billion exempted from GRH calculations.¹⁰⁹ Partisanship over the funding issue was just as dominant in the House as it had been in the Senate, and only two Republicans on the Ways and Means Committee voted for this plan. When the on-budget financing plan came to a vote on the House floor, it was approved fairly easily, 280–146, but 251 of those votes came from Democrats.¹¹⁰

The House–Senate conference eventually voted to use Treasury financing despite the administration's intensive lobbying for the RefCorp plan.¹¹¹ The Senate conferees had for some time supported the administration's position, but Democrat Alan Cranston changed his stance, paving the way for the Senate to agree with the House.¹¹² Although it was clear that the House would have supported

¹⁰³ OMB Director Richard Darman warned that if the Riegle plan passed, he would apportion the \$50 billion over a three-year period, adding significantly to the deficit and possibly invoking across-the-board cuts under GRH (Nash [1989c]). GRH was thought to apply to the upcoming fiscal year, not the current year, and was based on estimates and not actual spending.

¹⁰⁴ U.S. Congress (April 17, 1989), S4000.

¹⁰⁵ See statements of Sen. Jake Garn and Sen. Kit Bond (U.S. Congress [April 17, 1989], S3997, S4001).

¹⁰⁶ U.S. Congress (ibid.), S4009.

¹⁰⁷ The vote was 50–48, but 60 votes were needed for passage because it was a waiver to the 1974 Budget Act that would have increased outlays and the deficit (Thomas [1989b]).

¹⁰⁸ Nash (1989d).

¹⁰⁹ Nash (1989e).

¹¹⁰ Rep. John LaFalce introduced a substitute amendment that, unlike Rep. Rostenkowski's, did not exempt the \$50 billion outlay from GRH. Rep. Rostenkowski and others strongly opposed this because it would almost certainly have resulted in sequestration under GRH. Rep. LaFalce's amendment was defeated 256–171. U.S. Congress (June 15, 1989), H2730-2747.

¹¹¹ For example, on July 13 the president wrote to the leaders of the conference asking them specifically not to use a waiver of GRH (Nash [1989g]).

¹¹² Nash (1989h).

the conference report to use Treasury financing, the path in the Senate was much less certain. Republican Phil Gramm stated that since the financing provision of the bill involved a waiver of GRH, he believed that passage would require 60 votes, and he and 40 other senators had informed Treasury Secretary Brady that they would not support the conference report.¹¹³ The president, several days later, informed Congress that he would veto the bill if it contained the Treasury financing proposal; the Senate, seeking to avoid this confrontation, then rejected the conference report, and the House and Senate conferees met again to reconsider the bill.¹¹⁴

This stalemate over the funding issue prompted Bush aides to draft a presidential proclamation that would have forced Congress to forego its planned recess and convene to consider the bill. Bush's planned statement would have stated that "delays necessary to craft the best possible solution are justifiable. The Congress' plans for a summer recess, however, cannot justify an additional delay."¹¹⁵ The last president to actually invoke this constitutional power had been Harry Truman, when he ordered the "do-nothing" Congress into session in July 1948 to act on housing, civil rights, and price controls.¹¹⁶ As it turned out, Bush did not find it necessary to issue the proclamation, but its drafting underscored the seriousness with which completion of the legislative program was viewed. Informing Congress of the administration's intent might have put enough additional pressure on Congress for that body to arrive at a compromise.

The bargain that was reached essentially split the difference: \$18.8 billion would come from direct Treasury borrowing on-budget, but for the current fiscal year (1989).¹¹⁷ For the purposes of GRH, this borrowing would have no effect (i.e., no potential for sequestration). The other \$31.2 billion would be off-budget. Of this amount, \$30 billion would be raised by the issuing of bonds through the administration's proposed funding mechanism, the RefCorp.¹¹⁸ The other \$1.2 billion would be contributed by the Federal Home Loan Banks to the RefCorp, which in turn would

transfer the funds to the RTC. The last obstacle to FIRREA's passage had been overcome.¹¹⁹

Conclusion

Although FIRREA established the RTC, it served only as the beginning of a structure and purpose that Congress would constantly examine, evaluate

¹¹³ Nash (1989f).

¹¹⁴ Garsson (1989c).

¹¹⁵ GBPL F1002/070114: Memorandum from Nelson Lund, Associate Counsel to the President, to James W. Cicconi, Assistant to the President and Deputy to the Chief of Staff, August 4, 1989.

¹¹⁶ Presidential proclamations convening both houses of Congress under Article II, Section 3 of the Constitution have been made only 27 times. Twenty-three of the proclamations took place before the 1933 ratification of the Twentieth Amendment—thus, during the years when Congress was usually not in session between December and March. Although most presidential proclamations of this nature dealt with serious national crises, Truman's decision in 1948 was essentially political, designed for use in the 1948 election. He actually made the announcement at the Democratic convention. See Hartmann (1971), 192ff.

¹¹⁷ The final version of FIRREA erroneously failed to include this \$18.8 billion in the written formula for calculating the RTC's obligation limitation (discussed above, p. 28). Since the RTC ran out of funds in late 1990 and Congress failed to act, this \$18.8 billion "loophole" was used to allow the RTC to continue operations until Congress appropriated further funding. See Davison (forthcoming).

¹¹⁸ For a discussion of the politics surrounding the compromise, see Knight and Downey (1989) and Nash (1989i).

¹¹⁹ The second part of Title V of FIRREA established the Resolution Funding Corporation (RefCorp)—a one-time funding mechanism (future RTC funding would come directly from the Treasury)—as a mixed-ownership government corporation with the authority to issue \$30 billion in bonds. The proceeds had to be transferred to the RTC through the purchase of capital certificates issued by the RTC. The RefCorp was under the authority of the Oversight Board and was governed by a three-person board of directors drawn from the presidents of the Federal Home Loan Banks (FHLBs). The corporation was to receive its funds from several different sources: the FHLBs, SAIF assessments on savings associations, earnings on its assets, RTC receivership proceeds (under certain conditions), the FSLIC Resolution Fund, and the Treasury. The FHLBs were required to pay the corporation's administrative expenses; RTC receivership proceeds, the Banks, the FSLIC Resolution Fund, and (if these were insufficient) the Treasury paid the corporation's interest expense. (Since the FHLB interest contribution was only \$300 million per year, and the RTC and FSLIC Resolution Fund monies would only be used if a surplus was available, the Treasury would pay most of the interest expense.) The FHLBs were required to capitalize the RefCorp by purchasing RefCorp nonvoting capital stock (and the allocation of the capitalization among the FHLBs was set through a complex formula). The RefCorp was required to place the capitalization payments from the Banks into its principal fund, which would use the money to purchase zero-coupon U.S.-issued bonds, and these in turn would eventually be used to pay in full the principal of the RefCorp bonds upon their maturity. To the extent that the capitalization payments from the FHLBs as required by FIRREA were insufficient to fully repay the principal upon maturity, the RefCorp could make up the difference by using a portion of SAIF assessments on savings associations and receivership proceeds received by the FSLIC Resolution Fund. This description is largely based on Lescher and Mace (1991), 521–28.

and change. That process began even before passage: the final law, while certainly reflecting the administration's basic concept for the RTC, also altered that concept in significant ways. First, at the urging of the FDIC, FIRREA made the RTC far more independent of Treasury control than the original plan had envisaged, with the Oversight Board, at least in theory, taking no part in day-to-day management decisions. Second, Congress to some extent modified the RTC's purpose. In the administration's plan the RTC's mission was purely to resolve institutions and return assets to the private sector at the lowest cost; in the bill as enacted, a number of concerns that might conflict with those essential goals had been legislatively mandated—concerns such as affordable housing and limits on asset disposition in “distressed areas.” These mandates made for a more complex decision-making apparatus and hence a more complicated bureaucracy.

Given the scope and character of the RTC's business as well as the agency's seemingly endless need for taxpayer dollars, it is not surprising that Congress—and the media—would find the RTC's operations and management a convenient target for scrutiny and criticism. FIRREA did, however, set the parameters of the legislative changes that Congress would seek in later years: funding, organizational structure, management reform, accountability, and social policy would all retain their place in congressional debate and action concerning the RTC.

Conclusions drawn about the creation of the RTC without reference to its later actions are necessarily incomplete. Some judgments are possible however. The administration deserves credit for confronting a difficult problem. It remains clear, however, that the use of the RefCorp as a financing vehicle, with its higher interest costs, should have been eschewed in favor of direct Treasury financing. This was purely a political decision, understandable in the context of the politics surrounding the deficit, but with no real benefits, and some very real costs. Another funding issue, though touched on only briefly in this article,

should also be mentioned: a specific plan for providing working capital to the RTC ought to have been included in FIRREA. Leaving this detail for later led to delays and uncertainty. When we turn to the management of the S&L cleanup, it seems clear that management structures and responsibilities could have been better defined in FIRREA, though it should be acknowledged that what emerged at the end of the legislative process was a significant improvement over the highly imprecise nature of the initial proposals. The notion of an impossibly small RTC overseen by an Oversight Board that consisted of high officials whose main responsibilities lay elsewhere was impracticable. Deciding whether the grafting of social policy goals onto the RTC's mission was a good idea or a bad one will likely vary depending on a rather subjective cost-benefit analysis. In the end, it is fair to say that the U.S. government was entering uncharted territory, and so it would be unrealistic to expect that the RTC would have sprung Athena-like, fully and perfectly formed from the legislative process.

In closing, it should be noted again that the creation of the RTC would have been much more difficult without the existence of an organization similar to the FDIC. The latter provided two significant benefits; first, a foundation, notably in the form of a reservoir of relevant expertise, upon which the RTC could be built; second, a receptacle for the RTC's unfinished business, and therefore the means by which the RTC could realistically be conceived of as having a limited lifespan—a characteristic that was politically very helpful for this new experiment in government.

Appendix: The Federal Asset Disposition Association and the 1988 FSLIC Deals

Two other significant duties of the RTC—aside from resolving failed institutions and managing and disposing of assets—were elements of the president's bill and were retained, more or less intact, by Congress. They were designed to tidy up ancillary regulatory detritus. One of these additional

duties involved liquidating the FHLBB's experiment in asset disposition, the Federal Asset Disposition Association (FADA); the other involved dealing with the much-criticized transactions entered into by the FSLIC in 1988.

The FADA

In the mid-1980s, as the problems within the S&L industry grew, the FSLIC had on its hands a growing inventory of troubled assets (more than \$2 billion in late 1985) but lacked both the resources and the expertise to dispose of them. The FHLBB established the FADA as the solution to that problem, chartering it in November 1985 for ten years as a stock savings and loan association (wholly owned by the FSLIC), with the FSLIC providing \$25 million in startup funds.¹²⁰ This private corporation was to manage and dispose of assets more efficiently and effectively than either FSLIC staff or contractors had been able to, and would therefore (it was thought) produce substantial savings for the FSLIC.¹²¹ The FADA, however, did not deliver on its promise of savings (by 1988 it had lost approximately \$15 million), and it was heavily criticized for failing to dispose of assets, growing too large, and overpaying its executives.¹²² Critics charged that the organization was unaccountable even to the FSLIC and that its management insisted it was a private entity even as the entity itself claimed governmental privileges.¹²³ The FADA's president and CEO, Roslyn Payne and her salary of \$250,000 became a lightning rod for criticism.¹²⁴ In addition, private companies that were engaged in the asset disposition business wanted a bigger slice of that pie and were eager to see the FADA go. By late 1988, despite the appointment of a new CEO at a considerably lower salary, congressional detractors had drafted legislation calling for the FADA's abolition.¹²⁵ Few supporters of the organization remained as the new administration was putting together its draft for FIRREA, and since the RTC was to handle asset disposition, the organization was not only friendless but also redundant.

The administration plan called for the RTC to manage the FADA and to sell it, wind it down, or

dissolve it within 180 days. The Senate's only change to this was to remove the 180-day requirement. The House, however, retained the 180 days and required that if the RTC chose to sell the FADA, it should do so through a competitive bidding process; the House also wanted to ensure that no contracts entered into by the FADA survived the organization's dissolution or sale, and required that the FADA name could not be transferred to any purchaser. The House Banking Committee, perhaps in continuing dismay over the FADA's failures and in response to the perception that FADA employees had been overpaid, noted the committee's intention that no FADA employees be automatically transferred to the RTC; rather, all of them should have to go through the normal hiring procedures. However, only the prohibition on selling the FADA name remained in the conference report, and even this dropped out during the final negotiations. As enacted, FIRREA simply stated that the RTC was to liquidate the FADA within 180 days.¹²⁶

The FSLIC Transactions of 1988

The flurry of transactions made by the FSLIC at the close of 1988, with their capital loss coverage, yield maintenance agreements, and tax benefits for acquirers, had become the target of congressional ire even before the president announced his plan

¹²⁰ U.S. General Accounting Office (1988), 16-18.

¹²¹ Payne (1986), 12-14.

¹²² House Committee on Banking, Finance and Urban Affairs, Subcommittee on Financial Institutions Supervision, Regulation and Insurance (1987). Moreover, the GAO issued a legal opinion that the FSLIC's chartering of the FADA was illegal (U.S. General Accounting Office [1988], 2-3).

¹²³ For a discussion of the hybrid nature of the FADA, see H. Seidman (1988), 23-27, and Moe (1995), 22-26.

¹²⁴ Taylor (1988a, 1988b).

¹²⁵ For example, H.R. 4646, introduced in May, and H.R. 5521, introduced in October. Both of these bills called for greater use of the private sector in asset disposition.

¹²⁶ U.S. Senate (1989a); Senate Committee on Banking, Housing, and Urban Affairs (1989b), 200, 352; House Committee on Banking, Finance and Urban Affairs (1989b), 134, 361, 444; U.S. House (1989d), 214. Although the House provision about FADA contracts did not survive, it did not go unnoticed. When the RTC was making its plan for liquidating the FADA, Steven Seelig, head of the FDIC's Division of Liquidation, noted that he had recommended that the entity be sold without its management contracts and stated, "It's our belief that was Congress's intent" (Harlan [1989]).

to clean up the S&L mess.¹²⁷ Members of the House Banking committee complained early in January that the FHLBB had exceeded its statutory authority in making the transactions, which were generally viewed as being far too generous to the acquirers of insolvent thrifts.¹²⁸ FDIC Chairman Seidman, taking as his cue the gifts that banks in the past had bestowed on new depositors, described the transactions as “buy a toaster, get a thrift.”¹²⁹ The administration’s bill responded by authorizing the RTC to review the terms of all FSLIC resolutions (from January 1, 1988, until the enactment of FIRREA) to search for ways of reducing costs under the FSLIC agreements, including by restructuring those agreements. If the Oversight Board agreed, the RTC was to pursue changes that would result in cost savings.¹³⁰

As Congress began to consider FIRREA, a GAO report issued in March claimed that tax benefits given to investors in insolvent institutions had frequently cost the government more than liquidating the thrifts would have cost.¹³¹ With opinion decidedly against the FHLBB’s actions, Congress developed a more definitive requirement about the 1988 FSLIC transactions. The RTC was required to review all the cases, “actively review” all means of reducing costs under the existing agreements, and report to both the Oversight Board and to

Congress. Costs were to be specifically evaluated in relation to capital loss coverage, yield maintenance guarantees, forbearances, and tax consequences; bidding procedures were to be examined to determine whether they had been sufficiently competitive. The RTC was to exercise all legal rights to modify, renegotiate, or restructure agreements if savings could be realized.¹³² Moreover, as an additional check and source of information, a House subcommittee amendment sponsored by Toby Roth added a provision requiring a GAO audit of all FSLIC resolutions from January 1, 1988 through the enactment of FIRREA, and requiring a report to Congress estimating the costs of those resolutions.¹³³ This provision, calling for review from a second source, illustrates the level of congressional distrust of the 1988 deals.

¹²⁷ For a detailed discussion of the 1988 transactions, see White (1991), 157ff.

¹²⁸ See Nash (1989a); Hershey (1989).

¹²⁹ Attributed to Seidman by Rep. David E. Price in U.S. Congress (June 14, 1989), H2568. In February, when the FDIC assumed responsibility for insolvent FSLIC institutions, it effectively cancelled all negotiations for any additional such deals (Nash [1989b]).

¹³⁰ U.S. Senate (1989a), §501(f)(5). See also Garsson (1989a).

¹³¹ Rosenstein (1989).

¹³² U.S. House (1989d), 202–203.

¹³³ The Senate had no such provision, but it was agreed to in the conference (Pulles et al. [1989–98], 873).

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