CHAPTER 1 - INTRODUCTION

The United States of America provides protection to depositors in its banks, savings and loan associations, and credit unions. One of the key players in this process is the Federal Deposit Insurance Corporation (FDIC), which oversees the insurance funds for banks and for savings and loan (S&L) associations (also known as thrifts).

The FDIC's primary mission is to maintain stability and public confidence in the United States financial system by insuring deposits up to the legal limit[1] and promoting sound banking practices. In its unique role as deposit insurer, and in cooperation with other federal and state regulatory agencies, the FDIC promotes the safety and soundness of insured depository institutions and the U.S. financial system by identifying, monitoring, and addressing risks to the deposit insurance funds through its bank examination practices.

The FDIC promotes public understanding of banking and sound public policies by providing financial and economic information and analysis. It minimizes disruptive effects from the failures of banks and savings and loan associations, and it assures fairness in the sale of financial products and the provision of financial services. The FDIC is responsible for effectively managing receivership operations and for making sure that failing institutions are resolved in the manner that will result in the least cost to the deposit insurance funds.

To fulfill its mission, the FDIC performs three functions.

- In its capacity as insurer, the FDIC maintains, manages, and controls risks to two deposit insurance funds.[2] Whenever a federally insured depository institution fails, the FDIC pays off insured deposits or, more frequently, it arranges for the transfer of accounts from the failed institution to a healthy one.

- The FDIC shares responsibility for the supervision and regulation of banks and thrifts in the United States with other federal regulators and with state banking authorities. Of the federal banking agencies, the Office of the Comptroller of the Currency is responsible for supervising national banks; the Federal Reserve System is responsible for supervising both state member banks and holding companies; and the FDIC is responsible for supervising state nonmember banks and FDIC insured savings bank.[3]

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[1] The limit for deposit insurance was initially set at $2,500; this limit was raised to $5,000 on June 30, 1934; $10,000 in 1950; $15,000 in 1966; $20,000 in 1969; $40,000 in 1974; and $100,000 in 1980, where it remains to this day.

[2] The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 established two separate deposit insurance funds, the Bank Insurance Fund (BIF) and the Savings Association Insurance Fund (SAIF).

[3] FDIC, *History of the Eighties—Lessons for the Future: An Examination of the Banking Crises of the 1980s and Early 1990s* (Washington, D.C.: Federal Deposit Insurance Corporation, 1997), 463.

- The FDIC acts as the receiver or liquidating agent for failed federally insured depository institutions. In its role as receiver for a failed depository institution, the FDIC has a statutory obligation generally to maximize the return on the sale or disposition of the receivership estate's assets. The receiver distributes any funds realized from its liquidation efforts to the failed institution's creditors[4] and shareholders in accordance with the FDIC's priority scheme.

The FDIC has learned a great deal about the regulation of bank and thrift institutions since it was created in 1933. An important part of that experience has been learning how best to resolve failed financial institutions. By "resolving" a failed bank or thrift, the FDIC meets its obligations to the failed institution's customers who had insured deposits and helps maintain the stability of the banking system.

> The **resolution process** involves valuing a failing federally insured depository institution, marketing it, soliciting and accepting bids for the sale of the institution, determining which bid is least costly to the insurance fund, and working with the acquiring institution(s) through the closing process (or ensuring the payment of insured deposits in the event there is no acquirer).
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> The **receivership process** involves performing the closing function at the failed bank or thrift; liquidating any remaining failed institution assets; and distributing any proceeds of the liquidation to the FDIC, to the failed institution's customers who had uninsured deposit amounts, to general creditors, and to those with approved claims.

The United States has confronted massive bank failures more than once in its history. One notable time was in the midst of the Great Depression, when 9,096 banks failed from 1930 through the first three months of 1933. The FDIC was created in response to this crisis, and the foundation was laid for our current system of deposit insurance.

The success of the U.S. deposit insurance system through the 1950s and 1960s may be partly attributed to the generally stable and prosperous economic climate that prevailed, as well as to the regulated environment in which banks operated. During that 20-year period, 75 banks failed, an average of fewer than four banks per year. While this number of failures may seem large in comparison to bank failures in most other countries, it is important to note that the United States banking system consists of a large number of small, independent banks that serve their communities. For example, in 1979, there were 14,364 insured commercial and mutual savings banks in the United States and 4,363 S&Ls.

The banking economy began to change in the 1970s, leading up to the banking and thrift industry crisis of 1980 through 1994 during which time 1,617 banks and 1,295 savings and loan institutions

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[4] A failed institution's creditors include the FDIC (in its corporate capacity), which essentially stands in the place of the failed institution's customers with insured deposits.

failed or required financial assistance. By 1995, the number of financial institutions ha decreased, leaving 9,040 insured commercial and mutual savings banks in the United States and 2,030 S&Ls.

Until 1989, the Federal Savings and Loan Insurance Corporation (FSLIC), which was created in 1934 under the National Housing Act, insured savings and loan associations. The FSLIC insurance fund was declared insolvent in 1987, and the U.S. Congress dissolved that agency in 1989, transferring its failure resolution and receivership responsibilities to the newly created Resolution Trust Corporation (RTC). At that time, the U.S. Congress also gave responsibility for insuring the deposits in S&Ls to the FDIC.

The FDIC was responsible for developing a plan to address the savings and loan crisis of the 1980s and for helping the fledgling RTC begin to manage hundreds of thrift failures. The RTC was an independent temporary government agency created by the U.S. Congress specifically to handle the savings and loan crisis. At its inception on August 9, 1989, RTC's sunset date was established as December 31, 1996. Because of the efficiency with which it handled its task, the RTC was closed one year early. When the RTC was dissolved as of December 31, 1995, its duties with regard to failure resolution and receivership management for S&Ls were transferred to the FDIC.

Overall, from 1980 through 1994 the United States financial institution crisis resulted in 2,912 failed or assisted financial institutions. By 1995, the number of combined annual failures and assistance transactions had dropped to eight, and to six by 1996. In 1997, there was only one bank failure, and no failures of savings and loan associations. Chart 1-1 shows all the failures and assistance transactions per year, per agency during the crisis years.

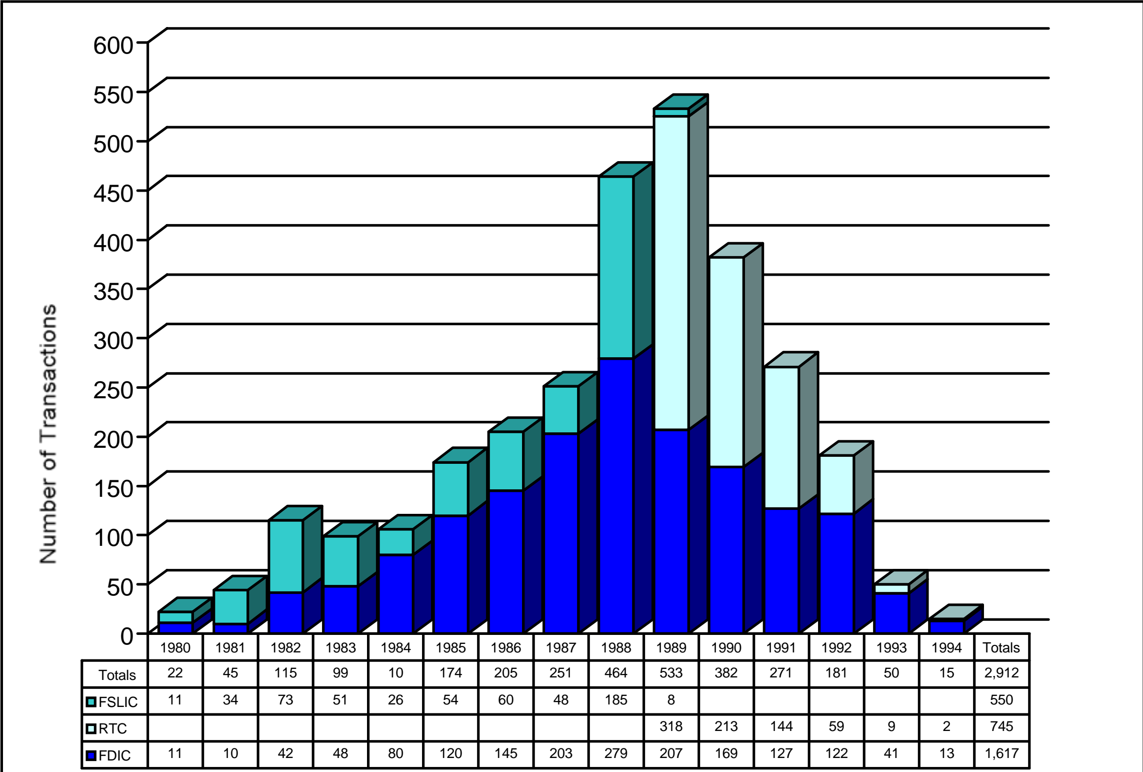
Many countries face difficulties with their financial industries not unlike the ones that the FDIC faced first at its inception and again in the 1980s and the early 1990s. Each year the FDIC provides information and resources to a wide range of foreign and domestic parties interested in the FDIC's resolution experiences. The purpose of this publication is to describe the FDIC's resolution process, to outline the different resolution methods, to provide information on other resolution alternatives, to describe the duties of the FDIC as receiver, and to highlight some important lessons learned through the FDIC's more than 60 years of experience in resolving failing and failed institutions.

The intended audiences for this publication are regulators and chartering authorities of foreign financial institutions, foreign central bankers, and others interested in the bank and thrift industries and their regulation. By sharing this information, the FDIC hopes to contribute to the international dialogue needed to promote stable banking systems and productive economies throughout the world.

A glossary is included in the back of this handbook for easy reference to the terms and abbreviations used herein.

Chart 1-1

Total Failures and Assistance Transactions (Banks and Savings & Loans) 1980-1994



	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	Totals
Totals	22	45	115	99	10	174	205	251	464	533	382	271	181	50	15	2,912
FSLIC	11	34	73	51	26	54	60	48	185	8						550
RTC										318	213	144	59	9	2	745
FDIC	11	10	42	48	80	120	145	203	279	207	169	127	122	41	13	1,617

Figures include open bank assistance transactions.

Source: FDIC Division of Research and Statistics.