

Banking by John Hoefle

Washington changes the rules

The government arrogantly breaks its contracts with buyers of failed savings and loan institutions.

In an amazing display of arrogance and contempt, the Office of Thrift Supervision has double-crossed the buyers of certain failed thrifts by retroactively declaring that certain funds the new owners were counting as part of their regulatory capital could no longer be counted. They are unilaterally changing the terms of the deals.

The ruling, announced Jan. 12, affects the buyers of 205 failed thrifts, which were sold in 1988 in 86 separate transactions. These sales occurred under the jurisdiction of the Federal Home Loan Bank Board (FHLBB), which has since been replaced by the Office of Thrift Supervision and the Resolution Trust Corp.

In its haste to sell the failed thrifts—during an election year when the Reagan-Bush administration was doing all it could to hide the depth of the crisis—the FHLBB made concessions to attract buyers, offering relaxed capital standards, tax breaks, and even guaranteed returns on some assets. Now that these deals have served their purpose, the administration has broken its word.

“We know we struck a deal based on their understanding of the rules,” sniffed OTS deputy director of supervision John Robinson to the *Wall Street Journal*. “We have people that are hopping mad.”

The OTS claims that the new interpretation of the rules was mandated by the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA) of 1989, but lawyers representing the 1988 buyers disagree. What the government is really doing,

they say, is reneging on the deals, in effect illegally seizing private property.

The impact of the government’s action upon some of the thrifts is enormous. For example, American Savings of California, the former Financial Corp. of America, bought by Robert Bass in December 1988, says that the ruling wipes about \$300 million in capital off its books. First Gibraltar, the new name for a group of Texas thrifts acquired by Ronald Perelman, will lose some \$40 million in capital. Both of these thrifts say that they will still be able to meet the regulatory capital standards, but it does make life more difficult for them.

The new ruling is actually the second time the rules have been rewritten, the first being with the passage of FIRREA itself. Northeast Savings of Hartford, Connecticut lost \$200 million in capital thanks to FIRREA, and now has lost another \$60 million, for a total of \$260 million. Northeast has filed suit against the federal government for its capricious actions. In all, five thrifts have filed suits over the changes the government has made in their contracts.

The problem that the thrifts will have in pressing their cases is that the government will claim it is acting in the public interest by requiring them to have higher levels of tangible capital. But the government is talking out of both sides of its mouth. Were the welfare of the public truly of concern, the government would have admitted the depth of the S&L crisis up front, before the 1988 elections, instead of

trying to manipulate the crisis behind the scenes. Had it done so, then these sweetheart thrift deals would not have occurred. What the government is attempting to do now is have it both ways: It used the buyers in 1988 to mask the crisis, and now it is piously claiming that it was had.

Besides being hypocritical and corrupt, the action is also quite stupid, coming at a time when the government is desperately trying to unload failed thrifts and their assets.

“If this is upheld, nobody will ever feel secure doing business with the government,” Washington lawyer and thrift lobbyist Douglas P. Faucette told the Associated Press on Jan. 15.

“I don’t know how you can enter into a contract with the government if you don’t know if it’s honorable,” Lewis Ranieri told the *Journal*. “But I wish we were dealing less with a moving target.” Ranieri also acquired a failed thrift, United Savings of Texas, at the end of 1988.

Despite the claims of some thrift operators that the OTS decision will not harm them, it clearly will hurt many of the 1988 buyers, who are operating in an increasingly hostile environment in which capital requirements are rising while real estate values and profitability plummet. Some of the affected thrifts are not going to make it.

“I suspect this means that the number of troubled institutions goes up,” was the understated analysis of James Barth, the former chief economist at the OTS and now at Auburn University. “If some of these deals come unraveled, it will be more costly to put them back together again, if you can,” he told Associated Press.

If you can, indeed. Buying a failed thrift is risky enough these days, without being stabbed in the back by the federal government.