The Resolution Trust Corporation and Congress, 1989–1993

PART I: 1989–90

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Policymaking is forever a work in progress, balancing the concerns of the regulated with the interests of society, and making adjustments as new imbalances inevitably arise. Good policy begins with good supporting legislation, and the process of making these laws leaves behind a rich trail of lessons for the future. This article looks back at an important episode involving the FDIC—the creation and operation of the Resolution Trust Corporation (RTC)—and highlights the political give-and-take that is often necessary to craft important legislation. The legislative history of the RTC, reflected both in the consequences of the statute that created it and in debates over subsequent legislation concerning the agency, was affected by the unique use of taxpayer dollars to protect insured depositors at failed thrifts. Readers should note, however, that this article only tangentially examines everyday RTC operations, which often (though not always) proceeded largely unaffected by the debates over the RTC's management structure and funding that were central to the legislative debate. When the RTC started its work, hundreds of insolvent thrifts needed to be closed, their insured depositors protected, and their assets returned to the private sector. Hundreds more would fail after the RTC opened, and in all, the RTC would resolve 747 failed thrifts and dispose of more than $450 billion in failed thrift assets before closing, a year earlier than originally planned, in 1995. The RTC successfully accomplished the broad public policy goals set out for it in 1989. The legislative story does, however, provide a window into understanding the environment in which the RTC operated. Readers interested in more details on the RTC's operations may want to consult the FDIC's study, Managing the Crisis: The FDIC and RTC Experience 1980–1994 *(1998). The legislative history of the establishment of the RTC, "Politics and Policy: The Creation of the Resolution Trust Corporation," appeared in* Banking Review *17, No. 2 (2005). The continuation of that legislative history, covering the years 1989–1993, is presented in two parts: Part I appears here; Part II will follow in an upcoming issue.* —Editor's note.

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The statute that created the Resolution Trust Corporation (RTC) in 1989—the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, or FIRREA—spelled out the agency's mandate with a good deal of specificity, even providing a date for the agency's shutdown just six years from its opening.[1] Such specificity, as well as the size of the initial funding ($50 billion), indicated that the agency would get a good deal of congressional attention. Nevertheless, given FIRREA's detailed content and the short time horizon it set for the RTC, one might think that a history of RTC-related legislation in the years after FIRREA would be relatively brief. One would be wrong. In each of the four congressional sessions from 1990 through 1993, significant RTC legislation was proposed or enacted: in 1991 two RTC laws were passed, and in 1993 another one was;[2] in 1990 and 1992 Congress considered but failed to pass RTC legislation.

Broadly speaking, during the life of the RTC Congress repeatedly sought to address two main issues. The first, and one that Congress found particularly hard to confront, was that of additional RTC funding. It quickly became apparent that the $50 billion provided by FIRREA in 1989 would prove inadequate. And when Congress did muster the political will to appropriate more funds (twice in 1991), those funds, too, proved insufficient (according to estimates at the time). Legislation providing still more funding did not pass until 1993. The second main issue that Congress repeatedly sought to address was that of the management and operation of the RTC. This broad issue encompassed a whole range of smaller ones, including management structure, methods and speed of disposing of assets and resolving failed institutions, contract oversight, provision of affordable housing, and the hiring of minority firms to do RTC work. These issues of management and operations were debated in the context of each major bill.

The debates leading to the passage of FIRREA had not been marked by overt partisanship (except for the arguments over budgetary treatment of RTC funding). Once the RTC was in existence, however, it was a highly visible part of the George H. W. Bush administration and a target for congressional critics, most often from the opposing party. A year after the RTC had been created, one observer noted that "the RTC can't make a move without somebody in Congress taking a shot at them . . . it's like being in a giant fishbowl where people not only look at you, but they line up along the sides, take harpoons, and start throwing them at you."[3] By 1992, the unpopularity of voting funds for the RTC meant that it had become hard to get even Republican support for the RTC's funding needs, a situation exacerbated by the election of a Democratic president in 1992. But although the debates on proposed RTC legislation were often highly politicized, they were also substantive and demonstrate that Congress was attempting to make major and minor adjustments in an agency with vast responsibilities that had been started from scratch in 1989 and was expected to operate effectively under intense scrutiny.

Post-FIRREA Issues (1989–1990)

The RTC's early operations (1989–90) were of great interest to many in Congress and generated much activity both in the legislature and within the administration. Although none of the legislation proposed during this period succeeded, the debates as well as the failed bills they accompanied contributed to the substance of the legislative

[1] As enacted, FIRREA made the RTC a limited-life (the corporation was to terminate by year-end 1996) entity that would manage and resolve all formerly FSLIC-insured institutions placed under conservatorship or receivership from January 1, 1989, through August 9, 1992. As of the date of enactment, the RTC was to succeed the Federal Savings and Loan Insurance Corporation (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. (FIRREA expanded the FDIC's Board from three to five members, adding the head of the Office of Thrift Supervision (OTS) and a member to be nominated by the president). The FDIC would be the RTC's "exclusive manager." For a detailed discussion of the creation of the RTC, see Lee Davison, "Politics and Policy," *FDIC Banking Review* 17, no. 2 (2005).

[2] In 1991, Congress passed the Resolution Trust Corporation Funding Act of 1991 (Public Law 102-18) and the Resolution Trust Corporation Refinancing, Restructuring and Improvement Act of 1991 (Public Law 102-233). In 1993, it passed the Resolution Trust Corporation Completion Act of 1993 (Public Law 103-304).

[3] Steve Klinkerman, "The High Road Is Costing the RTC Time and Money," *American Banker* (August 16, 1990).

changes that would be enacted in 1991 and illustrate the terms of the debates about the RTC overall.

During 1989–1990 three areas were most important: the first was general and multifaceted, combining concerns about the perceived slowness of the RTC's startup with concerns as to whether the bureaucratic structure outlined by FIRREA would be able to handle its appointed task. In a sense, this first area could be taken to include almost any of the agency's activities, but generally the concerns focused on the speed and manner of resolution and asset disposition. The other two areas were quite specific and dealt mainly with money—the bottom line of most of the debates over the RTC. The first of these was the need to provide the agency with working capital, and the second was the need to provide the agency with additional loss funds as it became clear that the money allocated under FIRREA would prove insufficient. (Both of these issues became embroiled in the partisan debate over the federal budget at a time when the deficit was a political lightning rod.)[4] Because the inadequacy of loss funding was not of immediate concern in the early months of the RTC's existence, this section will examine only the early criticisms of RTC operations and the debates over the provision of working capital.

Speed

Questions about whether the RTC was moving fast enough both to resolve institutions and to sell assets began almost immediately. Expectations for the RTC were high—unrealistically so. The decision to confront the thrift crisis had been announced in February 1989; the concept of the RTC had therefore been present for six months before its August creation. Somehow, despite the obvious challenges facing it, many observers felt that results should have been expeditious.[5] The RTC's management knew this. During deliberations in August about some of the first resolutions of failed institutions, RTC Chairman L. William Seidman noted, "I think the worst thing we can do now is not move forward quickly. . . . Mr. Brady [Nicholas Brady, secretary of the treasury] has said . . . that we're going to do them tomorrow, and if we don't, that's big news, . . . the kind of news the White House doesn't like to hear."[6] But although the FDIC, in consultation with other agencies, had been readying itself for the task of taking on the RTC, not until July was its precise role clear.[7] In any case, expecting the RTC to simply start work as if it had been in existence for years was unrealistic. As former FDIC Chairman William Isaac would note before Congress in the spring of 1990, "The scale of the RTC's undertaking is breathtaking. The RTC is in the process of creating, from scratch, virtually overnight, the world's largest financial institution, all of whose assets are troubled." Isaac believed it would take the better part of a decade for the RTC to accomplish its goals.[8]

In terms of resolutions, between August 9 and September 30 the agency resolved 24 institutions, but during the final quarter of the year it resolved only another 13, and during the first quarter of 1990 only another 15. To put this in perspective, by August 8, 1989, the day before the RTC came into existence, there were 262 failed thrifts in conservatorship that the agency would inherit and an additional 140 institutions would fail by the end of the

[4] It is, of course, impossible to divorce the issues of working capital and loss funding from the question of management: in mid- to late 1990, the expectation and then the reality of imminent shortfalls placed considerable constraints on the agency's ability to carry out its work. In short, there was no way the RTC could make continued significant progress without the necessary underpinning of adequate working capital and loss funds. Nevertheless, the lack of funds and the RTC's response to it contributed to criticism, even if the funding problem was beyond the agency's control. And criticism of the RTC in general could mean a multitude of things. The criticism might be directed at the agency itself, by the public or Congress, or the criticism might be aimed not specifically at the RTC but at the administration's conduct (whether exemplified by the Oversight Board or by the Treasury) or at "the bailout," with varying degrees of specificity or breadth. Although some detractors aimed their criticism precisely, many others did not.

[5] John Murphy, former FDIC general counsel noted, "Let's face it, the legislation has been percolating for six months . . . [and] now that it has bubbled to the surface, people will be expecting prompt action" (Steve Klinkerman, "All Eyes Are on Seidman to Move Fast and Smart on Thrift Cleanup," *American Banker* [August 10, 1989]).

[6] RTC Board of Directors Meeting, August 9, 1989.

[7] See Davison, "Politics and Policy."

[8] Robert Trigaux, "RTC Must Rely on Sales Mentality for Its Role in Bailout to Succeed," *American Banker* (May 9, 1990). Many observers were more impatient than Isaac, but pessimists were far less sanguine than he about the RTC's prospects: in October 1989, John Oros, a partner at investment banking company Goldman Sachs, declared it likely that "our grandchildren will be buying assets from the RTC" ("5-Year RTC Cleanup Called the "Big Lie," *National Mortgage News* [October 2, 1989]).

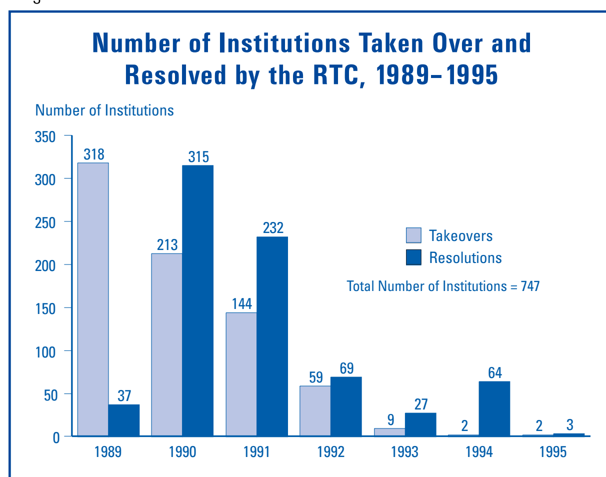
first quarter of 1990.[9] (See Figure 1 for the number of conservatorships and resolutions during the agency's existence.) By early 1990, the volume of criticism, particularly from House Democrats, had begun to rise significantly. Rep. Bruce Vento said he thought the RTC had failed to hit the ground running and it was "not too early to suggest that they should be doing more." He noted that the 37 resolutions carried out in 1989 had been "deposit sales, not really the sale of institutions, and they were not very complicated deals."[10] Rep. Frank Annunzio stated that the RTC "has spent more time posturing for more money than in using what they have."[11]

No matter where one stood with regard to the RTC's performance, it was clear that the agency was not resolving failed thrifts at a rate that kept pace with the growing number of thrifts in conservatorship (institutions in conservatorship still operated, but were under RTC control). The RTC's most obvious response to the criticism was the so-called Operation Clean Sweep announced by Seidman in March 1990. Designed to assuage critics, restore the RTC's credibility in the eyes of potential acquirers, and demonstrate progress, this ambitious plan called for 141 resolutions by the end of June. The agency exceeded this goal, resolving 155 institutions with total assets of $44.4 billion in just three months.[12]

Although Operation Clean Sweep might have mollified critics of the resolution process, it made the asset-disposition part of the agency's task more difficult by adding substantially to the RTC's inventory of assets, particularly problem assets. And in fact, the agency's strategy for disposing of its inventory at first (and also later) provided fertile ground for disapproval. During the debate on passage of FIRREA, most concerns had centered on the idea that the RTC would move too quickly to sell off assets (particularly real estate), swamping an already severely depressed market, especially in the Southwest. These fears persisted during the agency's early days. Sen. Phil Gramm of Texas stated that if distressed thrifts' assets were disposed of too quickly, the effect might be to "bankrupt every healthy bank and thrift left [in the Southwest]."[13] The RTC was certainly aware of these fears. RTC Board member Robert Clarke, during a discussion in October 1989, noted that "there has been so much sensitivity to this issue of dumping. And people are going to be, as you know all too well . . . really be looking . . . closely."[14]

Once the RTC was operating, however, the fear of dumping was gradually replaced by the fear that the RTC was not moving quickly enough to divest itself of the assets of resolved institutions.[15] By mid-1990, with the inventory of assets rising and the prospect of more to come, many people realized that if the agency did not move assets quickly, it would never finish the job. In addition, people had come to believe that the only way to return real estate markets to normal was to get RTC properties back into the private sector. Ken Guenther of the Independent Bankers Association noted, "The attention has shifted from dumping to speeding up the disposition process . . . in some markets,

Figure 1



[9] Resolution Trust Corporation, *1989 Annual Report* (1991), 51-55 and *Annual Report 1990* (1991), 87-88.
[10] It should be noted that the RTC's management was inclined to do more complicated deals, but the Oversight Board's cautious attitude inhibited such activity.
[11] Robert M. Garsson, "Vento Urges Abolition of RTC Oversight Board," "Tough Scrutiny Ahead for RTC," and "Banking Panel Faults Bush on Pace of S&L Resolutions," *American Banker* (January 8, 22, and 24, 1990). For the debate over working capital, see the relevant section of this article.
[12] FDIC, *Managing the Crisis* (1998), 127.
[13] Steve Klinkerman, "Southwest Fears Impact of Real Estate Liquidation," *American Banker* (August 16, 1989).
[14] RTC Board of Directors Meeting, October 24, 1989.
[15] Seidman noted in January 1990 that "on one side are the anti-dumpers, on the other side are the fast sellers" (Robert D. Hershey, Jr., "Savings Rescue Cost Seen Rising," *New York Times* [January 25, 1990]).

nothing will stabilize until we get rid of the overhang of RTC properties."[16] Texas congressmen were complaining that the RTC was moving too slowly—at a "snail's pace."[17]

As the need for swift action began to outweigh fears of dumping, constraints that FIRREA had put on the RTC (and especially the agency's interpretation of the requirements for selling assets in "distressed areas")[18] came under fire. In June 1990, with the expected costs of the thrift rescue escalating and the argument becoming more partisan, House Democrats' condemnations of the agency's methods became more pointed. Rep. Vento told Treasury Secretary Brady, "There is an appearance to many of us that the RTC is floundering and the oversight board isn't doing what it can. It's simply not moving the assets."[19]

To facilitate speedier sales of assets, the RTC began to alter its asset-disposition policies. For example, in early May 1990, it decided to adopt a more flexible approach to real estate sales in distressed areas.[20] By June it began to move toward a policy of using bulk sales to rid itself of at least some of its asset inventory. Though there was opposition to this strategy as creating a lack of competition among bidders (and as handing "sweetheart deals" to large investors), possibly lowering asset sale prices because of attendant discounts, and possibly hurting some real estate markets, such concerns were largely trumped by the desire to get assets moved out of the RTC quickly.[21] Undoubtedly the changes were to some extent a response to clamor in Congress, but they were much more a function of the newly created agency's finally getting some experience under its belt and responding to the marketplace. In the area of asset-disposition policy and practice as in the area of resolutions, demonstrable change was a response both to public debate and to experience.

Management Structure

Both resolutions and asset disposition were embroiled in debates about the RTC's management structure, which for Congress became one of the more contentious elements of the thrift cleanup. The most visible issue was the relationship (as created by FIRREA) between the Oversight Board and the RTC. Though ostensibly the two bodies worked together, they had different purposes. The RTC was an operational entity, run by its own board of directors, with a mission primarily of resolving institutions and selling assets. The Oversight Board was a policy and watchdog entity with a mission of setting the general policies under which the RTC would accomplish its goals, controlling the purse strings, and keeping watch on the use of taxpayer funds; it was not to intrude too deeply into RTC operations.[22] Seidman at one point described the RTC as the body and the Oversight Board as the mind. On the surface this division of function might seem fairly straightforward: the Oversight Board would set policy, and the RTC, working within those policies and therefore in accordance with the Oversight Board's directives, would do its job. The operational reality, however, was much more complex.

A complicating factor was the existence of two sets of personnel with different viewpoints and experience. (It should be noted that this discussion is based primarily on certain RTC materials and the public debate; unfortunately, equivalent internal

[16] Steve Klinkerman, "RTC's Aggressive Policy Garners Favorable Reviews," *American Banker* (April 3, 1990).
[17] "RTC Too Slow in Disposing of Real Estate Assets," *National Mortgage News* (April 16, 1990).
[18] See U.S. House Committee on Banking, Housing, and Urban Affairs, Subcommittee on Financial Institutions Supervision, Regulation and Insurance, Resolution Trust Corporation Task Force, *Disposition of Assets* (May 4, 1990), 30. Fears of asset dumping and potential damage to local real estate markets had prompted legislators to add a provision in FIRREA requiring that the RTC not sell property in those areas for less than 95 percent of the market value established by the RTC.
[19] Stephen Labaton, "Savings Debate Gets Partisan Tone," *New York Times* (June 15, 1990).
[20] By then the RTC had its own market experience to go on and could lower an asset's market value by taking this experience into account: if it had not been able to sell a property after six months (four months for residential properties), the market value could be lowered by up to 15 percent; if the property continued unsold for another three months, the market value could be lowered by another 5 percent. If the property still remained unsold, it would be reappraised, but the market value would not be raised if the reappraisal was higher than the most recent market value set by the RTC (Paulette Thomas, "Resolution Trust Corporation to Slash Prices of Hard-to-Sell Realty from Sick S&Ls," *Wall Street Journal* [May 9, 1990]).
[21] Paul Duke, Jr., "Bailout Officials Set Plan to Sell S&L Real Estate–Stockpile Would Be Sold in $500 Million Chunks over the Next Few Years," *Wall Street Journal* (June 11, 1990).
[22] For example, individual transactions were not part of the Oversight Board's purview.

Oversight Board materials were unavailable. Oversight Board members and staff doubtless held their own views on the Board's relationship with the RTC.) The RTC was essentially run by FDIC staff and executives while the Oversight Board had a strong Treasury Department component and so represented the administration's point of view. The FDIC was an independent agency with experience in financial institution failures and resolutions, and its board was accustomed to being able to adjust policies to suit its needs. Moreover, the FDIC's insurance fund came not from the taxpayer but from premiums paid by banks. The Oversight Board members, who had other time-consuming posts, would be able to spend relatively little time on RTC business, and both they and their staff, though experienced in banking, housing, or real estate development, had to come to grips with a new organization.[23] However, with substantial taxpayer money involved, it was appropriate for the administration to be involved in how the RTC accomplished its goals.

This bifurcated structure was a recipe for conflict. Each entity might genuinely believe it was pursuing the best course available, but the two did not necessarily share a single vision. What the Oversight Board perceived as a "general policy," the RTC might see as an operational matter.[24] There was constant tension over who had the power to make decisions and concern about perceptions of who was responsible for results.

Although FIRREA demanded that the Oversight Board create general policies, RTC executives thought the Oversight Board was attempting to write a set of rules for a process that was ill-suited to being governed by rules.[25] In these executives' experience, judgment had to be applied in the making of decisions, but the politics of the S&L cleanup had led to statutory mandates as well as Oversight Board authority constraining the ability to make such judgments. Moreover, the RTC's executives believed that the need for the Oversight Board to overcome the difficulties of starting from scratch further complicated matters. The RTC would, of course, have to follow Oversight Board policy (although the agency could and did seek to change that policy); Seidman warned RTC staff specifically not to exercise judgment but to follow the rules. Although FDIC staff had previously had more flexibility, Seidman noted, "we didn't [previously] have a statutory standard and we didn't have anybody upstairs to raise the issue about how we were operating."[26]

As the RTC began its work, the officials involved sounded conciliatory notes about this somewhat cumbersome relationship. Treasury Secretary Brady said it would be a "cooperative effort." Seidman publicly predicted a good working relationship with the Oversight Board.[27] Tension, however, was present from the outset. The RTC wanted to move immediately to sell five institutions but the Oversight Board prevented it from doing so, believing that the transactions were too complicated inasmuch as many key policies had not yet been formulated.[28] RTC Executive Director David Cooke stated that the Oversight Board had asked the RTC to "stay with fairly simple, small transactions" until policies could be determined; he said, diplomatically, that he did not mind this since the organization was just getting on its feet.[29]

[23] As structured by FIRREA, the Oversight Board had five members. Three of these were government officials: the Secretary of the Treasury (Nicholas Brady, who served as the board's chairman), the Chairman of the Federal Reserve Board (Alan Greenspan), and the Secretary of Housing and Urban Development (Jack Kemp). The other members were individuals to be nominated by the president and confirmed by the Senate. The first such members were Philip Jackson (a former Fed governor) and Robert Larson (the CEO of a real estate development firm). The Senate confirmed Jackson and Larson in April 1990.

[24] For example, in December 1989 there was some suggestion that the Oversight Board might be interested in setting RTC employment ceilings. When RTC Executive Director David Cooke, remarking that this seemed to be outside of the Oversight Board's territory, asked the RTC Board if it wanted to provide guidance to the Oversight Board, the RTC Board's members declined, with Seidman noting, "If this is oversight, they might as well handle everything" (RTC Board of Directors Meeting, December 12, 1989).

[25] RTC Board of Directors Meeting, January 9, 1990.

[26] RTC Board of Directors Meeting, October 24, 1989.

[27] Barbara A. Rehm, "21-Year Veteran of FDIC Climbs to Top RTC Post," *American Banker* (August 10, 1989).

[28] Jim McTague, "RTC Told to Delay Major Deals; Key Policy Issues Must Be Resolved First," *American Banker* (August 14, 1989).

[29] Barbara Rehm, "Helmsman Cooke Plots RTC Course," *American Banker* (August 14, 1989). Seidman later recalled that even small transactions created problems. The RTC had decided that as a means to show the world that it would hit the ground running, the agency would liquidate three small S&Ls and pay off their depositors. In the absence of defined policies, the Oversight Board initially chose not to make funds available. Seidman informed Deputy Treasury Secretary John Robson that if asked to explain why the thrifts had not been liquidated (he was scheduled to appear on the news), he would state that lack of funds was responsible. The Oversight Board reversed its decision and made the funds available (L. William Seidman, *Full Faith and Credit: The Great S&L Debacle and Other Washington Sagas* [1993], 204).

When Clarke asked in August 1989 about the relationship with the Oversight Board, Seidman stated that it was taking a lot of work and that

> We've time and time again gotten to the brink with them where they say they don't have this or they need that in order to give us money. And I have instructed the staff at that point to tell them that we are closing shop and going home. And when they have money, we'll go back in business. And so far they've given us the money. One of these times they probably won't.

Seidman did say that he and William Taylor, the Oversight Board's acting vice president for finance and administration, were attempting to create practical solutions to their problems.[30] Nevertheless, in the matter of funds disbursement, the Oversight Board wanted to keep the shortest possible rein on the RTC, a policy that Seidman criticized openly just weeks after the RTC began operations, complaining that John Robson, deputy treasury secretary and the acting president of the Oversight Board, essentially had veto power over RTC management decisions because of his control over funding. In turn, Treasury was reported to be angered by public discussion of disagreement, and one commentator noted that the Oversight Board felt exposed, since it had ultimate responsibility for handing money over to the RTC.[31]

Although Nicholas Brady called the troubles mere "healthy friction" that would occur in any startup operation, others thought the system was too complex; in their eyes, the "zeal to have prudent supervision . . . meant that the buck stops everywhere." Daniel Brumbaugh, who had been an economist at the Bank Board, said the structure led to "artificial, arbitrary outcomes."[32] Rep. Vento described the RTC and the Oversight Board as "operating for the past two months by the collective seat of their collective pants"—a management style that, he claimed, had not worked.[33] Congressmen such as Vento and Annunzio criticized initial drafts of the Oversight Board's strategic plan as vague.[34] The General Accounting Office (GAO) also found the early version of the plan too amorphous.[35] The unfavorable perceptions were reinforced by the inability of the RTC and Oversight Board to decide on the method for raising the RTC's working capital (discussed in detail below).[36]

Daniel Kearney's appointment as Oversight Board president in October was meant to bring to the Oversight Board someone who had experience in both private sector real estate and government and who would be able to repair the frayed relationship between the RTC and Treasury.[37] However, Kearney resigned after only four months, citing a misunderstanding on both his and the Treasury's part about the scope of the powers vested in the position. This was generally taken to mean that Treasury had never given Kearney any real authority and that he found the situation unacceptable.[38] Seidman noted that Kearney was replaced on an interim basis by William Taylor, who was able to get much more done not only because he was an experienced government official but also because, after Kearney's resignation, Treasury had to be far more accommodating to avoid the repercussions from a second departure.[39]

[30] RTC Board of Directors Meeting, August 15, 1989.

[31] Nathaniel C. Nash, "Federal Savings Industry Rescue Is Entangled in Agency Disputes," *New York Times* (August 28, 1989).

[32] Paulette Thomas, "Thrift Bailout, Lacking a Chief and Floundering as Officials Feud, Slows and Grows More Costly," *Wall Street Journal* (October 11, 1989).

[33] Jim McTague, "RTC Sales Unfair to Small Banks," *American Banker* (October 20, 1989).

[34] Barbara A. Rehm, "Lawmakers Say Guidelines from RTC Oversight Board Are Vague," *American Banker* (November 7, 1989).

[35] Gregory Wright, "RTC May Run Dry by 1991," *National Mortgage News* (November 13, 1989).

[36] John L. Douglas, the FDIC's outgoing general counsel, stated in December that if the working capital debate was not resolved, it would put the RTC out of business, noting that the bickering with Treasury had to stop: "The RTC is a beggar at Treasury's door constantly" (Barbara A. Rehm, "No Money, Too Many Rules, and No Friends," *American Banker* [December 11, 1989]).

[37] Kearney was a principal at a Boston real estate advisory firm and had previously held posts at the Department of Housing and Urban Development, the Government National Mortgage Association, and the Office of Management and Budget (OMB) as well as Salomon Brothers (Barbara A. Rehm, "Top RTC Overseer Plays Conciliator for Rival Factions," *American Banker* [November 7, 1989]).

[38] Barbara A. Rehm, "Confidence in RTC Seen Waning; Kearney Exit Spells Deeper Trouble for S&L Agency," *American Banker* (February 12, 1990); Brian Collins, "News Analysis: RTC Resignation Shows Tensions," *National Mortgage News* (February 19, 1990); and "The Thrift Bomb," *Wall Street Journal* (February 13, 1990). Kearney's difficulties can be illustrated by a discussion at an RTC board meeting, where it was noted that Kearney had made clear to the Oversight Board that the RTC needed more flexibility to make deals. The RTC board believed that Kearney was supportive and understood the issues but that, despite significant effort, he had been unable to make real progress. During the discussion, it was mentioned that the Oversight Board's lack of action was not the real problem because funding was controlled by Treasury and the OMB (RTC Board of Directors Meeting, January 12, 1990).

[39] Seidman, *Full Faith and Credit*, 205-6.

Toward the end of 1989, largely as a result of the bifurcated management structure, the RTC's operations were described as paralyzed. Noting that only 37 thrifts had been resolved since the agency had opened for business and that only 3 small thrifts had been resolved in the previous 10 weeks, one observer blamed much of the agency's inaction on the Oversight Board, which, "in its zeal to avoid even the appearance of impropriety in cutting deals, . . . has thrown out all the bargaining tools developed over the years [by the FDIC]." An attorney dealing with financial institutions predicted that it would take several months at least before the Oversight Board might liberalize the terms of deals, several more months before the terms under which assets could be sold would be determined, and then a couple of more months before the RTC would be able to react to those rules and put significant numbers of deals into the pipeline.[40]

By January, public criticisms of the management structure became more and more numerous. Auburn University economist James Barth, who had been the chief economist at the OTS, said the S&L cleanup was quickly unraveling. Rep. Henry Gonzalez noted that key positions remained unfilled and important policies unannounced. Vento called for the Oversight Board to be abolished because it was too cumbersome. Another commentator called the structure "an absolute absurdity" and argued that split responsibility meant no responsibility.[41] Inside the RTC, there was clearly a certain amount of frustration with the situation. Seidman remarked that he thought it was the RTC's job to run the cleanup and the Oversight Board's to finance it, and that the Board should tell the RTC what they wanted, and the RTC would do it. "We can't both have the responsibility and not have the responsibility and so we're sitting here thinking up ways to get around the fact that they don't know how to provide financing."[42]

The split between the RTC and the Oversight Board was evident in congressional oversight hearings in January 1990. When Rep. Chalmers Wylie asked Seidman and RTC Executive Director Cooke if the Oversight Board was necessary, Seidman replied that when originally consulted about the structure, he had suggested either setting up a new and separate RTC with its own board answerable to the administration or allowing the FDIC to take over the cleanup, with the inclusion in FIRREA of whatever constraints were considered necessary. Seidman's implication was that the present structure was lacking. Cooke answered: "What we need at the operational arm is a fully operational board. We need a board that is available, accessible, and that we can exchange views and get decisions made." Seidman noted that people at the Oversight Board had tried hard to cooperate and that Kearney's performance was excellent, but asked, "Where did the buck stop in this whole process? If you can tell me, then we will know how to get it done, but at the present time it is almost impossible for David [Cooke] to know where to go and how to get operational decisions." After this exchange, Wylie noted that he had asked the question "somewhat facetiously, but apparently it was a better question than I first thought."[43] During the following week, Robson told the Senate Banking Committee that he knew of "no instance in which the working relationship between the Oversight Board and the RTC has thwarted progress toward the common goal of carrying out the mandates of FIRREA."[44]

Just two weeks later, Kearney resigned. According to Rep. Charles Schumer, his departure suggested that initial startup frictions had not diminished. According to Vento, his leaving confirmed Vento's belief the Oversight Board should be abolished. Former FDIC Chairman Isaac argued that the policies set by the Oversight Board had made deals uneconomical for bankers and that much of the problem had to do with the multiplicity of man-

[40] Steve Klinkerman, "RTC Hogtied by Its Overseers," *American Banker* (December 26, 1989).

[41] For these three observations, see Glenn Brenner, "Pace Slows in Bailout of Thrifts; Shortage of Funds Threatens Effort to Sell Failed S&Ls," *Washington Post* (January 8, 1990); see also Robert M. Garsson, "Vento Urges Abolition of RTC Oversight Board," *American Banker* (January 8, 1990).

[42] RTC Board of Directors Meeting, January 9, 1990.

[43] U.S. House Committee on Banking, Finance and Urban Affairs, *Oversight Hearings* (January 23-25, 1990), 98–100.

[44] U.S. Senate Committee on Banking, Housing, and Urban Affairs, *Second Oversight Hearing* (January 31, 1990), 19.

agement layers.[45] Gonzalez added his voice to those calling for change, noting that disarray and indecision were now publicly evident.[46] The *Wall Street Journal* ran an editorial suggesting that "at the end of the day, Treasury has to get out of the way and let someone make decisions."[47] David Cooke reiterated that he had had a good relationship with Kearney and that [he and Kearney] had worked with Oversight Board staff to produce recommendations, "but where it goes from there is a mystery."[48]

Cumulatively the early record eventually resulted in proposed legislation designed to change the management structure put in place by FIRREA. In the immediate aftermath of Kearney's departure, two bills were introduced, one in the Senate and one in the House. Sen. Robert Kerrey, who had attempted to change the makeup of the Oversight Board during the FIRREA debate, had reiterated his concerns in October. He maintained that the Oversight Board's appointed officials were too busy with their governmental duties elsewhere to properly oversee the RTC.[49] His solution to the management problem was to create a new single board of governors to manage the RTC. It would replace both the Oversight Board and the RTC Board of Directors and would have nine members, five of whom would be independent members nominated by the president and confirmed by the Senate; the others would be members of the current Oversight Board and the Chairman of the FDIC. Although in March Kerrey's bill was also introduced in the House (by Rep. Peter Hoagland), nothing came of it.[50] Vento, head of the House RTC task force, also introduced a bill to alter the management structure. His bill would abolish the Oversight Board and transfer its powers to the FDIC Board of Directors.[51] This bill, too, failed to get anywhere, but clearly the RTC's management structure was on its way back to the drawing board.[52]

One reason Congress did not address the issue at this time was that just before Kearney's resignation, Senate Banking Committee Chairman Donald Riegle said he thought FIRREA needed to be given time to work and he had "no intention of opening it back up."[53] Even after Kearney left, it was reported that Congress was unlikely to take up any structural change, and Seidman discounted the possibility of such change, noting that Bush would veto any bill incorporating a change of that nature.[54] In addition, by late March, Treasury officials were reported as having said that relations between the RTC and the Oversight Board had improved markedly. They ascribed the improvement to Seidman's recognition that criticism of the Oversight Board "eventually sticks to him as well."[55] As noted above, the improvement was certainly partly the result of William Taylor's having become acting Oversight Board president in place of Kearney.[56] The RTC, Treasury and the Oversight Board were likely all chastened by the consistent criticism of them in the public debate. The structure of RTC management and its perceived effect on RTC performance would, however, return to the congressional agenda repeatedly as Congress debated RTC operations during the next several years.

[45] Nathaniel C. Nash, "Resignation at Savings Agency," *New York Times* (February 10, 1990).
[46] Barbara A. Rehm, "Confidence in RTC Seen Waning; Kearney Exit Spells Deeper Trouble for S&L Agency, *American Banker* (February 12, 1990).
[47] "The Thrift Bomb," *Wall Street Journal* (February 13, 1990).
[48] Brian Collins, "RTC Resignation Shows Tensions," *National Mortgage News* (February 19, 1990).
[49] U.S. Senate Committee on Banking, Housing, and Urban Affairs, *Oversight Hearing* (October 4, 1989), 66–67.
[50] S. 2155 and H.R. 4386, the Resolution Trust Corporation Reorganization Act.
[51] H.R. 4127, introduced on February 27, 1990.
[52] During 1990, two other bills also sought to change the RTC's management structure. One, H.R. 4851, the Financial Institutions Oversight Reform Act introduced by Rep. William Gradison in May, was a sweeping bill establishing Treasury control over financial institutions. It would have abolished not only the RTC but also several other entities, including the Office of Thrift Supervision (OTS). Given the extreme nature of this bill, it is unsurprising that it received little attention. Another bill, S. 3112, introduced by Senator Tim Wirth in September, would have abolished the Oversight Board and created a new Board of Directors for the RTC, consisting of the FDIC's board and two independent members to be nominated by the president. These bills show that in some quarters the notion of changing the management structure persisted throughout 1990.
[53] Robert M. Garsson, "Riegle Opposes Efforts to Amend S&L Bailout," *American Banker* (February 6, 1990).
[54] Brian Collins, "RTC Resignation Shows Tensions," *National Mortgage News* (February 19, 1990).
[55] Robert M. Garsson, "Seidman Opens 2nd Office at RTC Headquarters," *American Banker* (March 26, 1990).
[56] Seidman predicted that Taylor would be able to be more flexible than his predecessor (RTC Board of Directors Meeting, February 13, 1990). Taylor served as acting president until June, when Peter Monroe, a former deputy assistant secretary at HUD, took the position (Linda Corman, "RTC's New Oversight Chief Has Learned to Get Along," *American Banker* [June 4, 1990]).

The Working Capital Problem

The $50 billion that FIRREA provided to the RTC were "loss funds," funds to make insured depositors whole for losses suffered by insolvent institutions. FIRREA was silent about working capital, but the need for it was obvious: the RTC would incur carrying costs associated with the assets of failed institutions until those assets could be sold. The money borrowed for working capital would eventually be repaid from those asset sales. The requirement for working capital had been communicated to Congress before FIRREA passed.[57] Just several weeks after the RTC began its work, David Cooke noted that the Oversight Board was investigating setting up a financing vehicle.[58] In October, Seidman told the Senate Banking Committee that the RTC would require working capital so that it could continue resolving institutions without resorting to "uneconomic asset disposition policies." He emphasized that the working capital borrowings would in no way add to the $50 billion provided for loss funds and that any working capital program would still fall under the obligation limit imposed by FIRREA (discussed below) and would therefore be determined by the underlying value of the RTC's assets.[59] The subject of working capital was discussed again before the congressional RTC task force in October and November, when Oversight Board members, RTC officers, and the GAO all emphasized the need for it.[60]

Although the need for working capital was straightforward, finding the means to provide it became highly politicized. As a result, six months would pass before the issues surrounding this funding would be resolved. To understand the debate, one must place it within the larger picture of the budget. FIRREA's provision of the RTC's loss funds had been marked by a partisan struggle over their budgetary treatment. Democrats had argued for all loss funds to be from Treasury appropriations. The administration preferred an "off-budget" financing method. Spending funded by appropriations would increase the reported budget deficit and make it more difficult to meet the Gramm-Rudman-Hollings (GRH) deficit reduction law's targets; spending funded "off-budget" would not.[61] In the end, FIRREA represented a compromise—with $18.8 billion in on-budget Treasury appropriations and $30 billion from bonds issued by the off-budget Resolution Funding Corporation (RefCorp). Another $1.2 billion was funneled from the Federal Home Loan Bank System through RefCorp to the RTC. Some who were involved in the process believed the Democrats saw RTC working capital as a way to try to force the president to abandon his promise not to raise taxes,[62] although the debate was also about the transparency of the budget. But the delay in finding a solution could also be ascribed to the Bush administration's anxiety at being seen as directing increased monies to the RTC and to its desire to at least moot the idea of using an off-budget vehicle to fund working capital in order to avoid further constraints on the administration's spending choices during this period of high deficits. In the end, it turned out that neither Congress nor the administration preferred having the RTC as a constant companion to budget negotiations.

The Debate about Method

The administration was never publicly forthcoming about the methods it was considering using, but it was rumored that one possible way to provide working capital was to create a "Resolution Bank." Some Democrats in Congress thought the administration wanted to create another RefCorp

[57] See for example, letter from L. William Seidman to Sen. Donald W. Riegle, Jr., June 26, 1989, reprinted in U.S. House Committee on Banking, Finance and Urban Affairs, *Oversight Hearings* (Jan. 23-25, 1990), 560ff. Seidman then noted that "RTC likely will need considerably more than $50 billion to provide working capital to effect resolutions. . . . RTC must have the ability to raise cash or provide cash-equivalent obligations."

[58] Brian Collins, "RTC Chafes under Tight Grip," *National Mortgage News* (August 28, 1989).

[59] U.S. Senate Committee on Banking, Housing, and Urban Affairs, *Oversight Hearing* (October 4, 1989), 118-19.

[60] U.S. House Committee on Banking, Finance and Urban Affairs, Subcommittee on Financial Institutions Supervision, Regulation and Insurance, Resolution Trust Corporation Task Force, *Status and Activities* (October 4 and 19, November 6 and 13, 1989), passim.

[61] GRH created "maximum deficit amounts." The law mandated that if these were exceeded, the president would be required to issue a sequester order to reduce all nonexempt spending by the same percentage.

[62] At least this was the case according to OTS Director M. Danny Wall (RTC Board of Directors Meeting, January 9, 1990).

and this belief led to the introduction of the first post-FIRREA RTC-related piece of legislation: the Federal Agency Debt Management Act (referred to below as the Stark bill).[63] The bill—which was aimed specifically at the RTC even though the agency was never mentioned—would have prohibited federal agencies established after December 31, 1988, from "incurring any financial obligation other than authorized borrowings from the Treasury." The bill was intended to underscore congressional Democrats' opposition to another off-budget funding entity. Treasury Assistant Secretary David Mullins told Congress that although FIRREA had no explicit plan for working capital borrowing, the question had been discussed with Congress during the debate over that law. (FIRREA in fact authorized such borrowing—concern about it had engendered Rep. Gonzalez's insistence on an obligations limit—and the method of borrowing had been left open to provide the RTC with maximum flexibility.)[64] Mullins argued that the Stark bill was unworkable and would interfere with routine RTC transactions in offering guarantees; in addition, since FIRREA provided only for $5 billion in RTC borrowing from the Treasury, the bill would apparently limit working capital to that very insufficient amount.

Mullins also noted that the administration believed the budgetary treatment of working capital should wait until some plan was chosen but that nevertheless it would be improper to "distort" the budget by "ballooning budget expenditures in early years with amounts that will be fully repaid with budget receipts in later years." Moreover, recording RTC working capital spending on-budget could have perverse effects. Working capital borrowing (after fiscal year 1990)[65] would count as budget outlays and potentially force budget cuts elsewhere, while the proceeds of asset sales in the later years would reduce net budget outlays, possibly allowing higher levels of government spending in those years than would otherwise be the case. Although there would be no net difference in spending over time, placing RTC working capital on-budget could arbitrarily affect the timing of government spending. Lastly, he noted that scored on-budget, RTC operations might become the largest single discretionary determinant of budget results, making the RTC even more political. Congress, Mullins said, should "think long and hard before allowing the budget process to drive the case resolution and asset disposition process." The administration obviously opposed the bill.

RTC Chairman Seidman said the agency would require at least $50 billion in working capital, noting that working capital would smooth "out the timing difference between the RTC's cash outlays and its cash inflows" and that it was also needed to replace high-cost funds as a way to lower resolution costs. The alternative was to borrow using insured deposits at a much higher cost.[66] Other alternatives to raising working capital, such as using whole-thrift transactions or slowing the pace of resolutions to correspond to asset sales, would also prove costly. He reiterated that because the bill prohibited any financing other than through the Treasury but provided no additional Treasury financing beyond FIRREA's $5 billion, in practical terms the bill would simply "prevent the RTC from raising adequate working capital."[67]

[63] H.R. 3469 was introduced on October 13, 1989, by Rep. Fortney Stark; several important House members, including Dan Rostenkowski, were co-sponsors.

[64] U.S. House Committee on Ways and Means, Subcommittee on Oversight, *Role of Federal Borrowing and Loan Guarantees* (October 31, 1989), 36ff. For the FIRREA obligations limit, see Davison (2005), 29, and the discussion in the present article.

[65] Because the GRH law applied only to prospective fiscal years, working capital outlays financed by borrowing in the current fiscal year would not trigger the need for spending cuts.

[66] Thrifts in conservatorship were still operating institutions (run by the RTC) and needed to fund their assets. The greater the amount of funding provided to the institution through loans from the RTC, the less funding the thrift would have to seek in the deposit markets at higher cost. High-cost funds replacement therefore lowered the cost to the taxpayer. For a description of the conservatorship process, see FDIC, *Managing the Crisis*, 117–18.

[67] He was also concerned that the bill might be interpreted as applying to RefCorp, an interpretation that would put it in conflict with FIRREA, and that it might prohibit the RTC from providing the assurances and indemnities against lawsuits that are routinely provided to acquirers of institutions or assets. It might also be interpreted as banning putbacks of assets, thereby increasing the need for working capital, and might make it very costly for the RTC to securitize assets. All in all, Seidman felt the bill could put the RTC out of business (U.S. House Committee on Ways and Means, Subcommittee on Oversight, *Role of Federal Borrowing and Loan Guarantees* [October 31, 1989], 51ff.).

Whereas the RTC wanted working capital simply so the agency could do its job, politics played a significant role in the debate between the administration and congressional Democrats. As Rep. Stark told Seidman, deposits in S&Ls had to be honored, and the RTC would end up with large amounts of assets that no one wanted to see dumped; working capital was therefore required. But, he noted, "We have some political differences that you're not privy to or involved in."[68] In mid-November congressional Democrats and the administration agreed to postpone their disagreements over the issue of working capital: the Oversight Board and the RTC agreed not to seek to raise working capital during the congressional recess and to create a plan in consultation with Congress in 1990; and for its part, the House Ways and Means Committee agreed not to send the Stark bill to the House floor.[69]

This political compromise did not, however, relieve the RTC's very real operational concerns about a lack of working capital. By late November, the agency was adhering to its schedule for resolutions but was expected to have spent all the funds allocated to it for the fourth quarter and also for the early part of the first quarter of 1990. There was some concern that unless an agreement over working capital was arrived at quickly, the pace of resolutions would be affected.[70] By mid-December, RTC management became even more concerned, for they had seen indications that the RTC's lack of working capital and liquidity problems were now publicly known and could have adverse effects, notably in the agency's dealings with deposit brokers who might demand higher rates, particularly because they knew the RTC could abrogate contracts.[71] Seidman advised that the RTC should slow down its work and should not count on getting any working capital until the end of the first quarter. His prediction proved reasonably accurate.[72]

By early January 1990, the administration was narrowing down the potential mechanisms for raising working capital.[73] The creation of another off-budget entity had been rejected, and administration officials were suggesting a combination of Federal Financing Bank (FFB) borrowing and the sale of short-term notes backed by S&L assets.[74] Congressional Democrats supported only FFB borrowing, and without a quick decision from the administration, they would resume their push for the Stark bill. In mid-January, despite Seidman's belief that the RTC had to slow down, the Treasury contended that the RTC had sufficient funds to continue operations through the second quarter, and the House Banking Committee reportedly remained skeptical that the RTC needed more funds; one committee staff member suggested that the agency simply use the $50 billion in appropriated loss funds, noting "cash is cash."[75] At this point, however, the RefCorp had sold only $4.5 billion in bonds in October, and though it was to sell another $5 billion on January 17, it would need four additional offerings over the following year to raise all the funds provided for in FIRREA.[76] (See Figure 2.) As William Roelle (Director of the RTC's Resolutions and Operations

[68] Ibid., 92.

[69] Robert M. Garsson, "RTC Funding Fight Put on Hold until Next Year," *American Banker* (November 15, 1989).

[70] RTC Board of Directors Meeting, November 29, 1989.

[71] Several weeks earlier, when the agency had been unable to get a clear answer on how it could draw in a timely fashion on the $5 billion line of credit established by FIRREA, it had been forced to hold $1 billion in reserve that might have gone toward replacing high-cost funds (RTC Board of Directors Meeting, November 29, 1989).

[72] Ibid., December 19, 1989.

[73] Jerry Knight, "S&L Board Unveils Its Rescue Plan; Needed Funding Remains Uncertain," *Washington Post* (January 4, 1990). In fact, in late November, in discussions with RTC management, Kearney said the Oversight Board was ready to submit its working capital plans to the administration for discussion and was leaning toward direct borrowing from the Federal Financing Bank (FFB). (The FFB was created by Congress in 1973 to centralize borrowing by federal agencies and reduce the cost of such borrowing.) The RTC was also told that the OMB had "somehow decided that [using the FFB] may be off budget." Cooke told Kearney that the budget status was immaterial to the RTC; Kearney replied that it was immaterial to him as well (RTC Board of Directors Meeting, November 29, 1989). As indicated above, however, the budget-scoring issue was very important to both the administration and Congress.

[74] Paulette Thomas, "S&L Bailout Aides Scrap Plan to Create Off-Budget Agency to Raise Financing," *Wall Street Journal* (January 9, 1990).

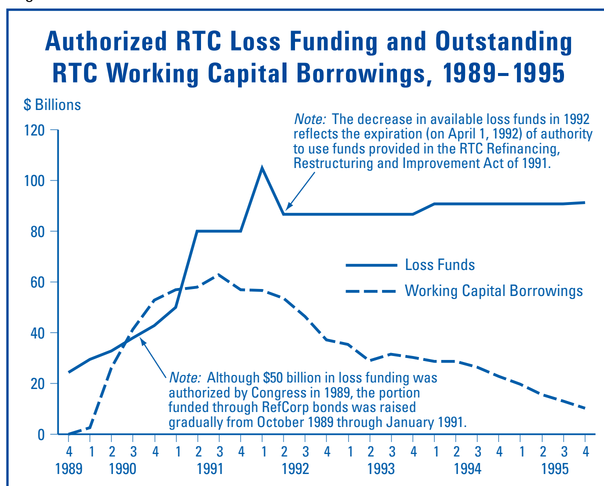
[75] Barbara A. Rehm, "RTC Plans to Dispose of 50 Thrifts in 1st Period," *American Banker* (January 16, 1990).

[76] The RefCorp was a mixed-ownership government corporation established by FIRREA to provide the RTC with $30 billion of its initial $50 billion in funding (see Davison [2005], 35-37. RefCorp bond offerings were made in October 1989 ($4.5 billion), January 1990 ($5 billion), April 1990 ($3.5 billion), July 1990 ($5 billion), October 1990 ($5 billion), and January 1991 ($6.9 billion). See Oversight Board press releases dated October 18, 1989; January 17, 1990; April 4, 1990; July 3, 1990; October 2, 1990; and January 2, 1991.

Division) noted, "Cash is cash [only] when you get it."[77] Shortly thereafter, the RTC indicated that in order to fund RTC operations, it might be forced to demand early repayment of the $11.3 billion lent to 169 thrifts. The demand could force the thrifts to depend once again on high-cost funds, driving up deposit interest rates across the United States.[78] Such an eventuality belied the Treasury claim that the RTC had enough cash to last into the second quarter, and indeed, not long afterward, John Robson informed Congress that the RTC would need an infusion of working capital funds during the first quarter of 1990.[79]

Despite the political jostling, it was most unlikely that the administration could persuade congressional Democrats to approve anything other than FFB borrowing. It was clear that working capital was necessary and would be provided; the politics surrounding the budgetary treatment of working capital were just as clear; and the administration undoubtedly preferred a method that would not increase the deficit.[80] In mid-February, the Justice Department ruled that the RTC had the authority to raise funds through the FFB, at last clearing the way for the RTC to be provided with working capital.[81] The announcement was immediately made that the RTC would raise $11 billion in the first quarter, with $8 billion going for carrying costs of receivership assets and $3 billion for the replacement of high-cost funds backing conservatorships.[82]

Figure 2



The RTC had been provided with working capital, but what the additional borrowing would mean for the budget was less clear. Since the fiscal-year 1990 budget was already in place, any 1990 borrowings might increase the deficit but would not require any action under Gramm-Rudman. In 1991, however, any substantial increase in the deficit resulting from RTC borrowing might make necessary significant offsetting budget cuts (something neither party would find palatable), barring a tax increase that Bush had already forsworn. The solution was to exclude RTC working capital from the GRH budget targets, a goal accomplished by a provision approved by the Senate Appropriations Committee in April. Reportedly, the administration, the Congressional Budget Office (CBO), and the Senate leadership supported the legislative change.[83] In the end, the Budget Enforcement Act of 1990 effected the exclusion, whose relevant provision also had the salutary effect of excluding

[77] Barbara A. Rehm, "RTC Plans to Dispose of 50 Thrifts in 1st Period," *American Banker* (January 16, 1990).
[78] Steve Klinkerman, "RTC Efforts to Get Cash Could Raise Thrift Rates," *American Banker* (January 19, 1990).
[79] U.S. House Committee on Banking, Finance and Urban Affairs, *Oversight Hearings* (January 23-25, 1990), 27-28.
[80] Barbara A. Rehm, "Administration Plans to Find Capital for RTC," *American Banker* (February 1, 1990).
[81] Robert M. Garsson, "Justice Says RTC Can Use Federal Bank for Capital," *American Banker* (February 16, 1990).
[82] "S&L Rescuers Are Cleared to Use Short-Term Funds," *Wall Street Journal* (February 16, 1990). The Treasury announced that it would increase the amounts of its weekly auctions of short-term bills and 52-week bills to raise the needed funds ("U.S. to Boost Level of Borrowing to Fund S&L Industry Bailout," *Wall Street Journal* [February 21, 1990]). Much of these funds was not spent during the first quarter because thrift resolutions slowed; however, as the RTC contemplated a major drive to resolve 141 institutions in the second quarter, it was authorized to borrow up to $45.3 billion ("Thrift Agency Is Cleared to Borrow $45.3 Billion," *Wall Street Journal* [April 12, 1990]).
[83] David Rogers, "Bill Seeks to End Count of RTC Fund under Deficit Law," *Wall Street Journal* (April 26, 1990). Treasury Secretary Brady, in response to a question in May, noted, "You don't want to complicate an already complicated set of budget negotiations . . . by swinging it back and forth with respect to working capital. It could be $50 billion worse this year and $30 billion better the next year, and it would raise havoc with the Gramm-Rudman target" (U.S. Senate Committee on Banking, Housing, and Urban Affairs, *Hearing on the Semiannual Report* [May 23, 1990], 67). This was also the position of the chairman of the Federal Reserve Board, Alan Greenspan, who in January had said that the basic purpose of Gramm-Rudman-Hollings was to raise total domestic savings and that since RTC working capital was a transfer of assets, it would have no effect on domestic savings and should be excluded from the GRH calculations. He was also concerned about the false effects that receipts from asset sales might have on the budget in later years. See U.S. Senate Committee on Banking, Housing, and Urban Affairs, *Second Oversight Hearing* (January 31, 1990), 76-77.

any further legislative appropriations for RTC losses from the budget deficit reduction process.[84]

The $18.8 Billion Loophole

The working capital saga was not quite over, however. Although the mechanism through which the RTC would borrow was agreed to, the possibility still existed that the agency would be unable to borrow enough working capital to fund its operations. In June 1990, Treasury Secretary Brady—even as he asked for appropriations for loss funds beyond the $50 billion already provided—informed Congress that before the RTC spent the $50 billion for losses, it was likely to run up against the obligation limit set by FIRREA at the insistence of Rep. Gonzalez. The obligation limit (also known as the note cap) was intended to restrict total RTC obligations to the sum of its cash, unused loss funds, and 85 percent of the fair market value of assets it acquired.[85] This meant essentially that the RTC had to hold unused loss funds in reserve in an amount equal to 15 percent of the fair market value of its assets.[86] These funds would serve as a capital cushion for repayment of debt obligations in the event that RTC's estimates of fair market values proved to be too optimistic. The Oversight Board characterized the situation as requiring immediate attention, and the RTC held out the possibility of needing to "dramatically step up asset sales to fund resolutions." Others argued that the administration was simply applying pressure to have RTC borrowing excluded from the budget (which, as noted, did occur), and a Senate Banking Committee staffer said that although the RTC would run into the obligations limit before the end of the year, the danger was not imminent.[87] This prediction was fairly accurate, but the fear that the RTC would have to radically slow the pace of its resolutions stirred action.

The solution to the difficulty lay in an oversight: FIRREA's note cap formula implicitly calculated unused loss funds as the excess of the $50 billion authorized by FIRREA over RefCorp funds received to date. However, RefCorp funding could only account for up to $31.2 of the $50 billion; the note cap (erroneously) omitted a reference to the $18.8 billion in Treasury funding that had also been provided in FIRREA. The RTC, to reassure Congress that it would not take advantage of the error, had been including the Treasury funding in its borrowing limit calculations regardless (i.e., as if it were no different than RefCorp funds). Until mid-1990, this compensatory calculation was of little consequence, but Treasury projected that if the RTC continued the calculation in this manner, the obligations limitation would become a real constraint by the fourth quarter.[88] Undersecretary Robert Glauber told the House Banking Committee that a literal reading of FIRREA would deduct only RefCorp contributions received from the $50 billion in FIRREA-authorized funds to determine the amount of unused loss funds available to back new obligations. This would permit the remaining $18.8 billion to offset the note cap's required reserve of loss funds (15 percent of the fair market value of assets) originally intended to ensure that RTC could repay its working capital borrowing. In effect, the RTC would be able to borrow for working capital up to 100 percent of the fair market value of assets acquired.[89] He added that "in the absence of action by Congress, we would be faced with the choice between using the $18.8 billion to raise working capital and shutting down the resolution activity of the RTC," but he said that the RTC would not take the former course without congressional approval.[90] House members at the hearing, confronted by the simultaneous request for significant additional loss funds, paid scant attention to the working capital issue, but a deci-

[84] Budget Enforcement Act of 1990, Sec. 13101 (specifically, see sec. 252[b]), 104 STAT 1388-581.

[85] U.S. House Committee on Banking, Finance and Urban Affairs, *Semiannual Report and Appearance by the Oversight Board* (June 14, 1990), 15. This description is a simpler way of presenting the limitation. More formally, the sum of contributions received from RefCorp plus outstanding obligations could not exceed the RTC's available cash plus 85 percent of the fair market value of its other assets by more than $50 billion. Reacting to the 1988 FSLIC deals, Rep. Henry Gonzalez had insisted on including a provision that would limit the RTC's outstanding obligations.

[86] U.S. House Committee on Ways and Means, *Additional Financing Costs* (September 19, 1990), 35.

[87] Debra Cope and Robert M. Garsson, "Brady Expected to Warn Congress RTC May Run Out of Cash by Fall," *American Banker* (June 13, 1990).

[88] U.S. House Committee on Banking, Finance and Urban Affairs, *Funding the Resolution Trust Corporation* (July 30, 1990), 15, 139.

[89] As $18.8 billion is equivalent to 15% of $125.33 billion, the latter figure was the effective limit on RTC working capital borrowing. Outstanding FFB working capital borrowings peaked in 1991 at approximately $63 billion.

[90] Ibid., 15-16.

sion to acquiesce in the literal interpretation would allow Congress to delay a highly contentious vote on new loss funding until after the November elections.[91]

Nevertheless, it took some time to get there. In late August Nicholas Brady noted in a letter to Rep. Dan Rostenkowski that although the administration had no specific proposal for adjusting the note cap, any funding legislation had to deal with the obligations limitation. A month later, Seidman again warned that without action, RTC resolutions would have to be tied to asset sales and would slow to "only a handful of institutions per quarter." Although the RTC had not yet run up against the limit, Seidman reiterated that it would soon become a constraint. He suggested that rather than omit the $18.8 billion in Treasury funding from the calculation, FIRREA be amended to allow the RTC to borrow 100 percent of the fair market value of its assets, noting that "since the ultimate costs will be the Government's in any event, it does not seem that the Government is taking any real risk [if such a change is made]."[92]

Once again, however, Congress was concentrating much more on the increase in loss funds than on operating capital. The assumption was that somewhere in the new funding legislation Congress would address the working capital issue; however, as discussed below, Congress adjourned without agreeing to any new RTC funding. Just before the adjournment, the House Banking Committee on a voice vote approved allowing the RTC to use the $18.8 billion drafting error and the Senate followed suit.[93]

On October 30, the RTC wrote to the Oversight Board asking that it be allowed to take advantage of the $18.8 billion drafting error and stating that otherwise, operations would come to a halt before the end of the year.[94] Two days later the Oversight Board agreed, providing the RTC with sufficient working capital and access to loss funds to continue resolving institutions until Congress could return to the issue in the new session.[95] Gonzalez and Riegle had both written to the Oversight Board encouraging this action.[96] This interpretation of FIRREA could conceivably have been challenged in the courts, but Gonzalez noted that with Congress having failed to pass any new funding for the RTC, he believed no one in Congress would object to the decision.[97] Once the decision was made, David Cooke told the RTC Board that the agency could move quickly to market the larger institutions it had planned to resolve during the fourth quarter, and that it could now continue through February 1991.[98]

Table 1 shows what the limitations on outstanding obligations would have been under the note cap formula (see note 85) from March 31, 1990, to March 31, 1991. As the table shows, without approval to take advantage of the loophole, the RTC would have exceeded the obligations limitation before year-end. With the changed calculation, however, the agency easily complied with the limitation.[99] In hindsight, the RTC's position would have been easier if FIRREA had dealt more directly with working capital—if doing so had even been possible. Congressional attitudes in 1990 illustrate the difficulties that would have

[91] "Treasury Scrambling for Funds for RTC," *National Mortgage News* (August 6, 1990).
[92] U.S. House Committee on Ways and Means, *Additional Financing Costs* (September 19, 1990) 5, 34. See also Paulette Thomas, "Seidman Totals Growing Costs of S&L Rescue," *Wall Street Journal* (September 20, 1990).
[93] Barbara A. Rehm, "House Bank Panel Votes Added Funds to RTC," *American Banker* (October 24, 1990).
[94] RTC Board of Directors Meeting, October 30, 1990.
95 Stephen Labaton, "Loophole to Be Used to Keep Bailout Afloat," *New York Times* (November 2, 1990).
[96] U.S. General Accounting Office, *Obligations Limitation: Resolution Trust Corporation's Compliance as of September 30, 1990* (1991), 4-5.
[97] "RTC to Borrow Working Capital; Regulators Avoid Funding Halt," *BNA's Banking Report* 55 (November 5, 1990), 747-48.
[98] RTC Board of Directors Meeting, November 2, 1990.
[99] The GAO noted that the exclusion of Treasury contributions "effectively eliminated the 15 percent cash reserve feature and resulted in a potentially misleading assessment" of the RTC's ability "to fund any future losses resulting from assets sales at less than their recorded value," and suggested that FIRREA be amended to fix this problem (U.S. GAO, *Obligations Limitation as of December 31, 1990* (1991), 6-7. The GAO would later note that the Resolution Trust Corporation Funding Act of 1991, which provided an additional $30 billion in loss funds (see the relevant section of this article for a discussion of the 1991 law), made the FIRREA obligations limitation formula even more misleading because the 1991 law did not amend the formula; thus, the additional funding was excluded from the calculation. In fact, Congress never changed the note cap formula, even as further laws (not only in 1991 but also in 1993) provided additional loss funds, and the obligations limitation never again became a constraint on RTC operations. Indeed, the GAO ceased publishing a calculation of the obligations limitation. (However, both the Senate and the House had included a revised obligations limitation formula in their abortive attempts to pass new funding legislation at the end of 1990 For the 1990 bills, see S. 3222 and H.R. 5891, 101st Cong., 2nd sess.)

attended adding anything to FIRREA that might have been portrayed as additional funding. Moreover, since the number of institutions and the volume of assets the RTC was dealing with were moving targets, any working capital provisions in FIRREA would likely have proved inadequate. And the Bush administration might have believed that it could borrow working capital quietly off-budget after the fact, although given the scrutiny attached to the RTC, any such attempt would likely have failed.

The struggle over working capital demonstrates how politicized RTC spending was and how enmeshed the agency was in budget brinksmanship at a time when the federal budget was in serious deficit. Irrespective of this, however, the number of insolvent institutions and the associated costs of resolving them kept rising. Had FIRREA not inadvertently included the $18.8 billion loophole, the RTC's operations might have been seriously impaired by the end of 1990, and Congress would undoubtedly—although perhaps grudgingly—have been forced into a swift about-face. However, as discussed below, the politics of RTC funding often led to impasse.

The 1990 Legislative Stalemate

As noted, FIRREA's $50 billion in loss funds was almost immediately recognized as insufficient. In January 1990, Seidman told Congress that although the $50 billion would cover insolvencies into 1991, it was obvious that more would be needed, perhaps another $24 billion. The reaction of Democratic Rep. Frank Annunzio was not encouraging: there was, he said, "No way you are getting money from the Congress."[100] Republican Rep. James Leach noted, "Congress would rather not deal with the thrift issue ever again . . . but it probably has no choice."[101] Both of Leach's points would turn out to be true. The RTC did not get its money from Congress in that session, and Congress did have to deal with the issue again in the following session.

In March, the House Banking Committee RTC task force predicted that the RTC would require

[100] Paulette Thomas, "Latest Estimates Show Thrift Bailout May Cost $24 Billion over Allocation," *Wall Street Journal* (January 25, 1990).
[101] Robert M. Garsson, "2nd Thrift Bill Takes Shape, but Congress Is Reluctant," *American Banker* (January 22, 1990).

Table 1

Limitation on Outstanding Obligations 3/31/1990–3/31/1991 ($ Millions)

	A Contributions Received	B Outstanding Obligations	C Cash and Equivalents	D 85% FMV Assets	(A+B–C–D) Adjusted Obligation Level	Maximum Level
3/31/1990[a]	29,526	2,760	3,181	13,728	15,377	50,000
6/30/1990[a]	33,021	30,162	4,043	29,593	29,547	50,000
9/30/1990	19,221	48,864	5,113	40,985	21,987	50,000
9/30/1990[a]	38,021	48,864	5,113	40,985	40,787	50,000
12/31/1990	24,248	54,777	5,177	40,930	32,918	50,000
12/31/1990[a]	**43,048**	**54,777**	**5,177**	**40,930**	**51,718**	**50,000**
3/31/1991	31,286	58,532	5,060	43,713	41,045	50,000

Note: For an explanation of the formula used to calculate the obligations limit, see note 85.

Sources: U.S. GAO, *Obligations Limitation . . . as of March 31, 1990; June 30, 1990; September 30, 1990; December 31, 1990; March 31, 1991* (1990, 1991, 1992)

[a] Calculation includes $18.8 billion in Treasury contributions.

$30 billion more in loss funds.[102] In April, the GAO followed with another increased estimate of the cost.[103] In May, the Bush administration presented Congress with a revised estimate of the costs, stating that the current worst-case scenario might entail another $57 billion. Commentators at the time felt that Treasury was at last presenting realistic estimates of the cost, perhaps to ensure that no higher estimates would have to be announced as the 1992 presidential campaign got under way. Treasury Secretary Brady told Congress that the administration would accept either an open-ended appropriation or some set figure, and would leave it up to Congress to decide.[104] Democrats criticized the administration for its conduct and were particularly unreceptive to the notion of open-ended appropriations.[105] Even some Republicans were unhappy with such a course."[106] Although it does not appear that the administration was seriously considering another off-budget vehicle, one Democrat fired a warning shot with a bill providing that any future funding had to use direct Treasury appropriation.[107] As summer ended, Seidman informed the House Ways and Means Committee that the RTC would need $30–$40 billion in new loss fund appropriations for the next fiscal year, noting, "Unfortunately, when it comes to loss funds, there really are no alternatives . . . [they] will have to come from the American taxpayer."[108] Seidman's request was endorsed by both the GAO and CBO, both of which argued that the slowdown caused by lack of funds could significantly increase the cost of the S&L cleanup.[109]

With the session drawing to a close, Congress finally turned to the problem of the loss funds. On October 10, Brady wrote to both of the Banking Committees, noting that "RTC case resolution will virtually cease within the next two months unless additional funds are provided." He requested legislation providing $40 billion and removing the FIRREA note cap provisions; alternatively, if Congress chose to maintain the note cap, he requested $57 billion. The Senate Banking Committee moved quickly to mark up a bill (S.3222) providing the $57 billion. There was some Democratic dissent, but the Senate was clearly willing to appropriate the amount requested by the administration.[110]

The House, however, was not. House Banking Committee chairman Gonzalez was angered by Nicholas Brady's refusal to appear before his committee; the refusal prompted him to cancel a planned hearing on October 17. He responded by stopping work on a markup of the RTC funding bill. With congressional elections imminent, politics likely played a role here: Gonzalez and House Democrats wanted another opportunity to associate the funding request with the administration, and Brady undoubtedly did not relish the thought of appearing before the committee and serving as a target for attacks on the handling of the cleanup. Gonzalez claimed that the administration wanted to "slip this through without any real oversight," saying he had never seen a request for authorization of funds "without the accompanying willingness of an agency or department head to defend [it] . . . in open session." The Treasury Department's view was that the committee had all the information it needed to make its decision and that it was the committee's responsibility to act.[111]

Gonzalez eventually relented—somewhat. The House Banking Committee moved on a bill that would provide only interim funding of $10 billion

[102] Paulette Thomas, "Resolution Trust Expected to Offer an Alternative to Cheap Liquidation," *Wall Street Journal* (March 20, 1990).
[103] Robert M. Garsson, "Pols Shrug Off GAO Estimate of Bailout Cost," *American Banker* (April 10, 1990).
[104] Nathaniel C. Nash, "Savings Failures Expected to Soar, the Treasury Says," *New York Times* (May 24, 1990).
[105] Charles Schumer, "The S&L Horror Show: Act II," *New York Times* (July 24, 1990).
[106] "Treasury Scrambling for Funds for RTC," *National Mortgage News* (August 6, 1990).
[107] See H.R. 5029, *Resolution Trust Corporation Financing Amendments of 1990*, introduced on June 13, 1990, by Rep. Paul Slattery. The bill was never acted on.
[108] Paulette Thomas, "Seidman Totals Growing Costs of S&L Rescue—Congress, in Election Year, Concocts New Tax Ideas Aimed at Paying the Tab," *Wall Street Journal* (September 20, 1990).
[109] Stephen Labaton, "Savings Bailout Chief Asks for $100 Billion," *New York Times* (September 20, 1990).
[110] U.S. Senate Committee on Banking, Housing, and Urban Affairs, *Resolution Trust Corporation Funding Act of 1990* (October 19, 1990).
[111] Stephen Labaton, "Savings Bailout May Be Hindered By Political Impasse Over Money," *New York Times* (October 19, 1990), and "A Patrician and Populist Clash in Savings Bailout," *New York Times* (October 22, 1990).

(although it also addressed the $18.8 billion loophole discussed above).[112] The bill also required that any additional request for funds be submitted to both Banking Committees and contain a complete six-month financial plan detailing how the monies would be spent.[113] The measure was approved by the committee on October 23, but not without opposition: Democratic Rep. Doug Barnard said that "if you want to keep them on a real short leash, you shouldn't give them anything." Even some Republicans positioned themselves against RTC funding, with Rep. Toby Roth arguing against passing even the $10 billion interim funding.[114]

The Senate realized that, with little time left in the session, there was not much likelihood of reconciling two very disparate bills. Accordingly, it amended its bill by replacing it with a measure essentially identical to that passed by the House committee (providing only $10 billion in interim funding). Riegle noted that this would keep the RTC on a very tight leash and ensure that RTC funding would be one of the first measures to confront the new Congress. He expressed some dismay that they were not providing more money.[115]

The bill passed the Senate on a voice vote. However, the House failed to pass the legislation. Reports suggested that the bill had been toppled by a procedural objection from Annunzio, but at the time some thought that there might not have been enough votes for passage anyway.[116] The House's inaction ensured that Congress would not block the use of the $18.8 billion loophole, for use of the loophole allowed Congress to postpone dealing with the loss-funding issue without forcing the RTC to cease resolving thrifts and would give legislators the ability to address funding early in the new Congress.[117]

[112] See H.R. 5891.
[113] See U.S. House Committee on Banking, Finance and Urban Affairs, *Resolution Trust Corporation Funding Act of 1990* (October 27, 1990).
[114] Stephen Labaton, "House Panel Approves More Funds for Bailout," *New York Times* (October 24, 1990).
[115] *Congressional Record.* S. 17722 (October 27, 1990).
[116] Paul Duke, Jr., "Congress Fails to Provide More Funding for S&L Bailout, Raising Threat to RTC," *Wall Street Journal* (October 29, 1990).
[117] Gonzalez said he wanted to begin hearings after the election and before the new Congress was seated (Barbara Rehm and Robert M. Garsson, "Gonzalez Urges Hearings This Fall on RTC," *American Banker* [October 31, 1990]).

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