Click here for Full Issue of EIR Volume 12, Number 31, August 9, 1985

The S&L crisis: Big banks move in

by D. Stephen Pepper

In the final week of July, the following developments rocked the savings and loan industry: Bell Savings and Loan, a $1.7 billion institution in the high-tech city of San Mateo, California, became the 58th S&L to fail. Sunrise Savings, a $1.8 billion institution in the high-growth Fort Lauderdale area, was taken over by the Federal Home Loan Bank Board, and new interim management was brought in to run the institution, declared insolvent by federal regulators. Attorneys for the conservator of the Maryland Deposit Insurance Fund brought a $200 million damages suit for fraud against the management of Old Court Savings and Loan in Baltimore.

A pattern of fraud and mismangement emerges in many of these situations, but beyond the immediate circumstances of each case, they are being exploited to bring about a major transformation of the American banking system. Here, we look at the situation in Ohio and Maryland, then in Florida and California, and finally assess the changes being wrought.

In state after state, the collapse of institutions and the consequent threat to depositors are being used to introduce legislation to permit the major money center banks to come in and gobble up thrift institutions and to convert them into commercial banks. The latest example of this process is in Maryland, where Chase Manhattan has issued a firm offer to purchase three savings institutions, including the troubled Merritt Commercial Savings. Previously, Chase had taken advantage of the Home State scandal in the state of Ohio to buy up six thrifts, mostly centered in Cuyahoga County in northeast Ohio.

The Maryland situation follows the earlier Ohio pattern closely. In the latter state, the seemingly sudden collapse of Homestate S&L triggered a run on that bank, which soon spread to other institutions. The governor convened an emergency session of the legislature, and a bailout was soon rigged that had as one of its principal provisions the opening of Ohio banks to takeover from out-of-state, and the conversion of S&Ls to commercial banking.

In fact, investigation of Marvin Warner and his Homestate bank for corrupt practices goes back at least to 1980, when then U.S. Attorney in Cleveland James Sissel, had wished to launch an investigation for conspiracy under the RICO statutes because of "a pattern of criminal activity" involving guarantees for construction loans. At the time, the investigation was quashed by Washington attorney and Democratic Party influence-peddler Edward Bennett Williams, who intervened on behalf of Warner, then U.S. Ambassador to Switzerland, with the Carter Justice Department.

Two years later, state regulators issued warnings that a cease-and-desist order should be issued to Homestate, but once more nothing was done. The collapse of ESM securities triggered the collapse of the Homestate house of cards, and immediately rippled through the state's other 72 state-insured thrifts because the fund was insufficient to cover such a major collapse. In the ensuing panic, the legislature passed the now infamous "Chemical Bank" bill, which was intended to allow Chemical New York to move in. As it happened, Chase made its move, while Chemical was beaten out at the last minute by junk-bond operator Carl Lindner.

The Maryland "crisis" was managed as a summer rerun of the Ohio operation. Old Court Savings was operated by Jeffrey Levitt and his associates as if the bank deposits "were their own private slush fund," to quote the suit brought against them. The same has been said of Warner and Lindner. This malfeasance had been known for years, and in recent months, warnings by auditors and regulators were ignored. Then the announcement by Maryland Attorney-General Stephen H. Sachs led to the eruption of the "crisis," the dramatic return from abroad of Gov. Harry Hughes, the emergency legislation which embargoed withdrawals of more than $1,000 from Maryland's 102 privately insured S&Ls, and mandated that all institutions with more than $40 million in assets seek federal deposit insurance. At this time, more than two dozen institutions are still operating under the $1,000 limit. The insurance requirement is even more onerous; to qualify, an S&L has to have on hand by Jan. 1, net worth equal to 5% of its assets. Many thrifts can not raise the new capital, and face merger or liquidation.

With depositors still unable to recover their savings and bank officers struggling to raise capital, Paul Volcker intruded himself, holding a meeting toward the end of July with Governor Hughes. Volcker gave the green light for Chase's move when he assured the governor that the Fed, which must approve bank acquisitions, would approve any acquisition that satisfied the state of Maryland's requirements.

Not only is Volcker a former employee of Chase, but he is the chief architect of the high interest rate policy that wrecked the savings-and-loan industry. In recent testimony before the Senate Banking Committee, Edwin J. Gray, chairman of the Federal Home Loan Bank Board, indicated that fully one-third of the industry may not survive. So Volcker's policy comes full circle. Having created the conditions that wrecked the industry, he now steps forward as its saviour by approving the takeover of "troubled" institutions by the New York banks, his patrons.

© 1985 EIR News Service Inc. All Rights Reserved. Reproduction in whole or in part without permission strictly prohibited.