Under this arrangement, FSLIC qualification examinations were expedited, using the resources of the FHLB System and the Federal Reserve. The Federal Reserve offered its assistance to help complete the FSLIC examinations as rapidly as possible. We believed we could facilitate this process because our examiners were already in place at the ODGF institutions and had gained familiarity with these institutions through the just-completed examinations conducted on March 16 and 17.

As of Friday, March 29, according to the State of Ohio, 26 of the former ODGF institutions have been reopened for the full range of banking functions, most with federal insurance. Confidence in these institutions seems to have been fully restored. There has been no evidence of unusual withdrawals or need for assistance through either the credit facilities of the FHLB of Cincinnati or the Federal Reserve discount window.

The federal deposit insurance applications of some ODGF institutions are still being considered. Other ODGF institutions have been informed of the changes and improvements that will be necessary to enable them to obtain federal insurance.

The State of Ohio is making intense efforts to develop an orderly plan for those institutions that might not qualify for federal insurance. It is my understanding that a final outline of such a plan is not yet complete. A solution may have to involve the sale of some ODGF institutions to other Ohio financial institutions and, perhaps, also to out-of-state institutions. The Federal Reserve Bank of Cleveland has not participated in the discussions involving plans for any single institution, except those for which Federal Reserve regulatory approval was required, such as the sale of Metropolitan Savings Bank of Youngstown to FNB Corporation, a Pennsylvania bank holding company, and the conversion of Scioto Savings Association into a state-chartered FDIC-insured commercial bank under the continuing ownership of its parent company, Society Corporation, an Ohio bank holding company.

While this process is underway, the state has authorized the ODGF institutions not yet qualified to reopen for full business to open for the limited purposes of giving each depositor access to a maximum of $750 per month and pledging assets to and borrowing from correspondent banks or the Federal Reserve discount window to fund the limited deposit withdrawals. Complete confidence in the ODGF institutions has not been restored, but the atmosphere is much calmer than it was two weeks ago.

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ECONOMIC COMMENTARY

Federal Reserve's Response to the Problems Experienced by ODGF Thrifts.

Statement by Karen N. Horn

I am pleased to appear before the Commerce, Consumer, and Monetary Affairs Subcommittee to discuss the Federal Reserve's response to the recent problems experienced by thrifts insured by the Ohio Deposit Guarantee Fund. This morning I will be reviewing for you the response of the Federal Reserve Bank of Cleveland.

I would like to begin by stating that the role of the Federal Reserve Bank of Cleveland throughout this period has been to assist the State of Ohio and other federal regulators in fashioning a solution. Our initial involvement was to insure that we could act quickly to provide liquidity assistance at the discount window and to make currency shipments—first to Home State and subsequently to other institutions insured by the Ohio Deposit Guarantee Fund (ODGF). We have acted at the request of the State of Ohio, and throughout this period the Federal Reserve Bank of Cleveland and the Federal Home Loan Bank (FHLB) of Cincinnati have shared information and staff in a cooperative effort to deal with the problems and to fashion solutions.

I would also like to recognize the substantial and supportive role of the correspondent banks in Cincinnati.

I believe the Federal Reserve has been helpful, and we will continue to assist the State of Ohio and other federal regulators until the problem is solved.

The Federal Reserve Bank of Cleveland first became aware of possible financial difficulties at Home State Savings Bank of Cincinnati, Ohio on March 4, 1985, when an official of Home State telephoned the Federal Reserve Bank of Cleveland to inquire about the procedures Home State should follow if it needed to borrow at the discount window. The Federal Reserve Bank of Cleveland did not have any financial information on Home State. It is a state-chartered savings and loan association, regulated and examined by the Ohio Division of Savings and Loan Associations, and prior to this time it had never borrowed at the discount window. We did know that Home State's deposits were insured by the ODGF, but we did not have access to any financial reports on Home State. On March 5, the press reported that Home State might suffer a large loss in connection with the failure of E.S.M. Government Securities, Inc. (E.S.M.), a Florida-based broker-dealer in government securities. The Federal Reserve began an effort to gather information on Home State's situation. Discussions with the FHLB of Cincinnati confirmed that Home State was not a member of the FHLB and that the FHLB also had little financial information on Home State.

Reports from Cincinnati on Wednesday, March 6, indicated a large volume of depositor withdrawals at Home State. On that same day, Federal Reserve examiners entered Home State to examine available collateral in the event that it became necessary for Home State to borrow at the discount window. Depositor withdrawals on Wednesday and Thursday were funded with Home State's own liquidity and lending by the ODGF.

We have acted at the request of the State of Ohio, and throughout this period the Federal Reserve Bank of Cleveland and the Federal Home Loan Bank (FHLB) of Cincinnati have shared information and staff in a cooperative effort to deal with the problems and to fashion solutions.

The withdrawals on March 6 totaled $55 million. On March 7, a meeting was held at the Cincinnati Branch of the Federal Reserve Bank of Cleveland with representatives from the State of Ohio, ODGF, and Home State to discuss liquidity assistance for Home State from the Federal Reserve Bank of Cleveland. Based on collateral judged to be acceptable by the Federal Reserve Bank, credit was extended on Friday, March 8, and arrangements were put in place to extend further credit.

Karen N. Horn is the president of the Federal Reserve Bank of Cleveland. This Economic Commentary *is a transcript of Mrs. Horn's testimony before the Subcommittee on Commerce, Consumer, and Monetary Affairs of the Committee on Government Operations, U.S. House of Representatives, April 3, 1985.*

Depositor withdrawals had continued on March 7 and 8, reaching approximately $100 million for those two days. On Saturday, March 9, Home State did not open for business. Governor Celeste appointed a conservator for Home State and announced on Sunday night, March 10, that Home State would not reopen for business on Monday.

Although the problems at Home State were triggered by unique events growing out of its transactions with E.S.M., the severity of the public reaction made us concerned about possible deposit withdrawals at other ODGF-insured institutions. As I mentioned earlier, deposits at Home State were insured by the ODGF, a private fund that also insured 70 other state-chartered thrift institutions in Ohio. According to state officials, the insurance fund had assets of about $130 million prior to the run on Home State. Uncertainty regarding other ODGF-insured institutions was increased by reports on the use of ODGF funds to deal with Home State's heavy deposit withdrawals. Financial information on all ODGF-insured institutions was made available to the Federal Reserve Bank of Cleveland late Friday, March 8. Federal Reserve examiners and discount-window staff reviewed and analyzed this information on Saturday and Sunday, March 9 and 10, with the assistance of senior examination personnel from the FHLB of Cincinnati.

Growing concern that other ODGF institutions might confront problems on Monday led us on Saturday, March 9, to develop a plan to monitor and deal with deposit withdrawals at other ODGF institutions, should they occur. The plan had several dimensions: (1) having a timely and effective mechanism for sensing unusually heavy deposit withdrawals, (2) informing ODGF institutions of collateral and other requirements for borrowing at the discount window, and (3) planning and putting into place the logistics necessary to deliver currency, evaluate collateral, and obtain documents for borrowing at the discount window. The large number of ODGF institutions and the need for prompt and effective action, if action were required, made it imperative that we be prepared to deal with the problem by Monday, March 11, when the ODGF institutions opened.

Although the problems at Home State were triggered by unique events growing out of its transactions with E.S.M., the severity of the public reaction made us concerned about possible deposit withdrawals at other ODGF-insured institutions.

We were fortunate in being able to draw upon staff from other Federal Reserve Banks to assist in the contingency planning and logistics. The weekend planning effort concluded with meetings at 10:00 p.m. on Sunday, March 10, in both Cleveland and Cincinnati to brief Federal Reserve examiners on their role in the contingency plans. These plans called for examiners to be strategically placed near ODGF institutions throughout the state prepared to deliver borrowing documents upon request.

Also, late Sunday evening, March 10, following the Governor's announcement that Home State would not reopen on Monday, the Cleveland Federal Reserve Bank publicly restated its discount-window policy: "State-chartered savings and loans and savings banks, like all depository institutions, are eligible for liquidity assistance through the discount window... under normal terms and conditions." Our weekend efforts had made it possible to implement the policy, to monitor deposit flows, to lend at the discount window, and to ship cash throughout the weeks that followed to a large number of institutions, most of which had not dealt with our discount window and which normally received their currency from other sources.

Public confidence in ODGF institutions continued to decline. As financial institutions opened on Monday, March 11, the evidence of the loss in depositors' confidence was almost immediate. At first the loss of confidence was largely confined to Cincinnati, where Home State is located. As the week progressed, the number of ODGF institutions suffering heavy cash drains increased, and the volume of withdrawals rose sharply. On Thursday, March 14, for example, the seven most affected institutions in the Cincinnati area lost more than $60 million in deposits—almost triple the amount withdrawn on Wednesday. Several institutions had lost one-fifth of their deposits between Monday morning and Thursday night, and there was clear evidence that the crisis was spreading to ODGF-insured institutions in other cities. The more public confidence fell, the more serious the problem became. Federal Reserve examiners were sent upon request to many institutions to begin reviewing collateral as deposit withdrawals and the potential for borrowing at the discount window increased. The Federal Reserve and other commercial banks shipped currency to institutions that were experiencing heavy withdrawals, but cash alone was not enough to restore confidence; without confidence, even the strongest financial institution can be severely impacted.

Our active and visible role was to provide liquidity assistance to ODGF institutions at the discount window. In performing this function, the Federal Reserve Bank of Cleveland has not modified the normal eligibility requirements for discount-window assistance in any way. The Monetary Control Act of 1980 made the discount window of the Federal Reserve Bank available to any depository institution that holds transactions accounts or nonpersonal time deposits. Regulation A of the Board of Governors, which prescribes standards for the operation of the discount window, provides for lending to eligible depository institutions under two basic programs. One is the adjustment credit program; the other supplies credit for seasonal and other limited purposes for more extended periods. Adjustment credit is available on a short-term basis to assist borrowers in meeting temporary requirements for funds while an orderly adjustment is being made in their assets and deposit liabilities.

All Federal Reserve advances must be secured to the satisfaction of the Reserve Bank providing the credit.

Our active and visible role was to provide liquidity assistance to ODGF institutions at the discount window. In performing this function, the Federal Reserve Bank of Cleveland has not modified the normal eligibility requirements for discount-window assistance in any way.

Satisfactory collateral includes securities of the U.S. government and of federal agencies and, if of acceptable quality, residential mortgage notes and other assets. Although collateral is generally held in safekeeping at the Federal Reserve Banks or acceptable third-party custodians, in this instance, field warehouses were set up in most ODGF institutions where collateral was identified, evaluated, and earmarked for possible use in securing discount-window borrowings.

The Federal Reserve played another very important role during the ODGF savings and loan problem—we served as a facilitator. During the early morning hours of Friday, March 15, when the full dimensions of the problem became clear, Governor Celeste decided to close all ODGF member institutions for a three-day period. Following that decision, the Governor requested that the Federal Reserve assist him in calling a meeting of large Ohio banking and thrift institutions to discuss the situation with them and propose a solution to the problem. A meeting with representatives of 13 Ohio depository institutions—banks and S&Ls—was convened that morning at the Federal Reserve Bank of Cleveland. At that meeting, Governor Celeste explained his decision to close the ODGF institutions and discussed a legislative proposal that would require the ODGF institutions to obtain federal insurance before reopening. He also presented a proposal for dealing with the ODGF institutions that would not qualify for federal insurance. The state subsequently decided it would be useful to discuss the situation with out-of-state banks, and two meetings were held with out-of-state institutions at the Federal Reserve Bank of Cleveland—one on Saturday, March 16, at 9:00 p.m. and another on Sunday, March 17, at 11:00 a.m.

In the past two weeks, some elements of a solution have fallen into place. Each ODGF institution was examined on a case-by-case basis to determine its financial condition and the likelihood of its qualifying for federal insurance. The State Superintendent of Savings and Loan Associations requested assistance from the Federal Reserve, the Federal Deposit Insurance Corporation (FDIC), and the Ohio Division of Banks in conducting these examinations. This process began on Saturday, March 16,

The results of the preliminary examinations made it clear that a large number of these institutions were well-managed, in sound financial condition, and, consequently, viable candidates for federal deposit insurance.

with examiners provided by the Federal Reserve Bank of Cleveland and, eventually, by every other Federal Reserve Bank. Examiners were assigned to each of the ODGF institutions. Virtually all examinations were completed on Sunday, March 17, enabling us to conduct a preliminary review of the condition of each institution to supplement and update the information obtained the previous Friday from the state. The results of the preliminary examinations made it clear that a large number of these institutions were well-managed, in sound financial condition, and, consequently, viable candidates for federal deposit insurance. Others, for a variety of reasons, would have difficulty qualifying for federal deposit insurance. The FHLB Board agreed to review, on an expedited basis, the Federal Savings and Loan Insurance Corporation (FSLIC) insurance applications of ODGF member institutions.