

**STATEMENT OF ELLEN SEIDMAN
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ON THE CONDITION OF THE THRIFT INDUSTRY
BEFORE THE
COMMITTEE ON BANK, HOUSING AND URBAN AFFAIRS
UNITED STATES SENATE**

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I. Introduction

Mr. Chairman, thank you for the opportunity to appear before the Committee to discuss the financial condition and performance of the thrift industry. As the Director of OTS, I have come to appreciate how difficult it is to change perceptions. We often hear that perception is reality. Sometimes perception is reality, but not always. The thrift industry is a case in point. Today, many of those who do not follow the industry closely still perceive the industry as being deeply troubled. The memory of the thrift crisis lingers in the nation's collective consciousness. In 1988, one in five thrifts was insolvent. Equity-to-assets ratios averaged 3.5 percent. In that year alone the industry reported losses of \$13.3 billion.

Working together, President Bush and the Congress passed the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) to address the crisis, and clean-up problem thrifts. By 1991, the thrift industry had returned to profitability and began a long process of restoration, stabilization, and strengthening.

Where is the industry today?

Today's thrift industry is strong and growing. Profitability, asset quality, and other key measures of financial health are at or near record levels. The average equity-to-assets ratio is over 8 percent, and 98 percent of thrifts are well-capitalized. Problem

thrifts and loan loss rates are very low. Mortgage loan originations are at or near record levels. And only three thrifts have failed in the past five years.

Many factors are responsible for the current health of the thrift industry. Obviously, the nation's long-running economic prosperity and the quality of thrift management are two critical factors. We must also recognize the contribution of critical statutory and regulatory reforms that have been initiated over the last twelve years to strengthen the banking system. The reforms of FIRREA, and the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA), which mandated new capital standards, uniform standards for lending, operations and asset growth, and prompt corrective action, played a large role in strengthening the system. New supervisory tools and enforcement powers, such as the Examination Parity and Year 2000 Readiness for Financial Institutions Act, have given us the ability to intercede more quickly and forcefully if problems develop at an institution. At OTS we've worked hard, through recruiting, training, our new accreditation and professional development programs, and other new supervisory tools, to make certain our staff is equipped to deal with the challenges of an ever more complex industry.

II. Condition of the Thrift Industry

As of March 31, 2001, there were 1,059 OTS-regulated thrifts, holding assets of \$953 billion. Though consolidation continues to reduce the number of thrifts, asset growth has been strong, and industry assets are at the highest level since March 1991.

While there are some large thrifts that operate nationwide, most thrifts are small, community-based financial service providers. As of the first quarter of 2001, 71 percent of thrifts had assets less than \$250 million. Mutual thrifts comprise 39 percent of the industry, but have only about 7 percent of the industry's assets. The industry employs 182 thousand people, maintains over 61 million insured deposit accounts, and holds over \$668 billion in housing related-loans and securities,

including \$458 billion in whole single-family loans, representing over 48 percent of thrift assets.

A. Earnings and Profitability

In recent years, the earnings and profitability of the thrift industry have been strong – a trend that continued into the first quarter of this year. First quarter earnings were \$2.16 billion – the third best quarterly earnings on record. For the year 2000, the industry reported earnings of \$8.0 billion, just shy of the record earnings of \$8.2 billion posted in 1999.

The industry's return on average assets, a key measure of profitability, was a healthy 0.92 percent in the first quarter of this year and 0.91 percent in the year 2000. The industry posted yearly returns on assets above 0.90 percent for the last three years – a feat last achieved in the late 1950s.

In large part, the strength and stability of the industry's earnings can be attributed to diversification of income sources, and strong asset quality.

The industry's success over the past decade in expanding its line of products and services, such as mutual fund and annuity sales, trust activities, and transaction accounts, has enabled the industry to diversify its income stream and generate more stable earnings. Higher proportions of noninterest income helped stabilize thrift income and provided better insulation against interest rate fluctuations. Noninterest income as a percent of thrifts' gross income more than doubled over the past ten years to 12.4 percent for 2000 from 5.1 percent in 1990.

Smaller thrifts, as a whole, did not fully participate in the overall industry earnings expansion. While remaining stable, smaller thrift earnings have lagged overall industry earnings for the last three years. Part of the reason for smaller thrifts' lag in

earnings is that they hold higher than average proportions of lower yielding assets – cash, U.S. Treasury securities, and non-mortgage related investment securities. As of the first quarter, thrifts with assets under \$100 million held 16.8 percent of their total assets in lower yielding assets compared to the industry average of 7.4 percent. In addition, the majority (56 percent) of mutual thrifts had first quarter assets under \$100 million. Mutual thrifts are not under shareholder pressure to maximize profits and pay dividends. However, mutual thrifts often “share” profitability with their owners – depositors – through higher interest rates and lower fees on deposit accounts. Mutuals are also active participants in the economic development of their communities. This sharing of profitability lowers net earnings.

B. Asset Quality

The overall quality of thrift asset portfolios is strong and key measures of problem loans are at or near historic lows. Troubled assets (loans 90 or more days past due, loans in nonaccrual status, and repossessed assets) were 0.62 percent of assets in the first quarter, slightly above the recent low of 0.58 percent at September 30, 2000. The ratio of troubled assets-to-total assets has remained below one percent since September 1997.

As might be expected in the current economic environment, the level of delinquent loans has been increasing. The industry’s noncurrent loan ratio increased in the three most recent quarters, albeit from a record low level. However, less seriously delinquent loans – those 30-89 days past due – were 0.70 percent of assets in the first quarter, down from 0.74 percent at the end of 2000.

The majority of the overall increase in thrift noncurrent loans was due to a rise in delinquent business-related loans, namely, commercial loans, nonresidential mortgages, and construction loans. Although the dollar amount of the typical business-related loan is larger than the typical consumer-related loan, the industry’s

total investment in business-related loans is small – less than 10 percent of all thrift assets. Thus, the overall increase in noncurrent loans reflects the delinquency of a small number of loans at a few thrifts.

Loan charge-off rates have also remained at low levels. Net charge-offs as a percent of total assets were 0.19 percent (annualized) in the first quarter, down slightly from 0.20 percent in 2000. The low charge-off rates reflect the high quality of thrift loan portfolios, which are heavily concentrated in single-family mortgages. Charge-off rates for single-family mortgages are generally very low compared to other types of loans. The loan charge-off rate was 0.05 percent of all single-family mortgages in the first quarter (annualized), or \$50 per \$100,000 of loans.

Thrifts' loan loss reserves have remained relatively constant at approximately one percent of total loans since 1999, reflecting the low levels of troubled assets and charge-off rates. The industry's reserve ratio is somewhat lower than that of the commercial banking industry. Again, this is due to thrifts' higher percentage of assets held in mortgage loans, which have lower loss rates than commercial loans.

C. Capital

Capital measures for the industry are strong, stable, and well in excess of minimum requirements. Equity capital was 8.1 percent of assets in the first quarter, with 98 percent of the industry exceeding well-capitalized standards.¹ Only four thrifts were less than adequately capitalized at the end of the first quarter, and each is operating under an OTS-approved capital restoration plan.

¹ On November 3, 2000, OTS and the other federal banking agencies requested public comment on an advance notice of proposed rulemaking that considers establishment of a simplified regulatory capital framework for non-complex institutions. And on September 27, 2000, OTS and the other federal banking agencies requested public comment on proposed revisions to capital rules for residual interests in asset securitizations or other transfers of financial assets.

D. Funding Sources

While capital ratios remain strong, the industry has become somewhat more dependent on wholesale funding as deposit growth has slowed due to changing savings and investment patterns and strong competition from mutual funds. Although deposits remain the primary source of funding for the industry, the ratio of total deposits-to-total assets has declined steadily over the past decade. In 1990, deposits funded 77.0 percent of thrift assets. By the end of first quarter of 2001, the ratio had declined to 57.0 percent.

Though the dollar volume of deposit growth has slowed, the number of deposits has increased since 1998, from 50.4 million in 1998, to 61.2 million as of the first quarter of 2001. The average size of small-denomination deposits (those under \$100,000) was \$6,900 as of the first quarter of 2001, compared to \$8,000 in 1998, reflecting the industry's increase in non-interest bearing checking accounts that typically carry relatively small balances. Such deposits increased by 28 percent to \$36.8 billion in the first quarter, from \$28.7 billion at the end of 1998.

With deposits declining as a source of funding, the thrift industry has become more dependent on wholesale funding, primarily in the form of Federal Home Loan Bank (FHLB) advances. At the end of the first quarter, FHLB advances funded 22.8 percent of total thrift assets, up from 7.4 percent in 1991. In addition, other types of borrowings, such as repurchase agreements, subordinated debt, and federal funds purchased, funded 8.9 percent of assets, up from 5.5 percent in 1991.

E. Interest Rate Risk

Interest rate risk remains a key concern in the thrift industry. Interest rate risk is a natural by-product of the industry's basic business of making long-term mortgages, which are generally funded with shorter-term deposits and other borrowings.

Interest rate risk was at the forefront of supervisory concern during 1999 and early 2000 as rising interest rates and a sharply inverted yield curve combined to put downward pressure on the industry's profit margins. Interest rate risk in the industry, however, has eased considerably since then. Interest rates have fallen dramatically and the yield curve has returned to a more normal shape. Thrift management also took steps to change their asset mix to reduce interest rate risk. Thrifts are now reporting wider net interest margins and generally lower levels of interest rate risk exposure.

OTS, alone among the federal bank regulators, has implemented a stress-test based supervisory strategy for evaluating the interest rate risk of the institutions we regulate. As a result, both we and the institutions are able to effectively assess and deal with any increase in interest rate risk sensitivity arising from changing interest rates or funding through non-core deposit sources, including FHLB advances with embedded options. As of the first quarter, 73 percent of all thrifts were classified as having low levels of interest rate risk, 18 percent as having medium levels, and 9 percent as having higher levels. Those in the higher risk level category are given close supervisory scrutiny.²

F. Problem Thrifts

The number of problem thrifts – those with composite safety and soundness examination ratings of 4 or 5 – remains low. There were 14 problem thrifts at the end of the first quarter, up from 10 in September 1999 – the lowest level since OTS's inception. Assets of problem thrifts have also remained low and stood at 0.5 percent

² On April 12, 2001, OTS issued a new Regulatory Handbook section on Derivative Instruments and Hedging that included an expanded discussion of risks of using derivatives, a discussion of OTS policy on derivatives that incorporates sensitivity analysis or stress testing from TB13a, and a discussion of FASB's SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities.

of industry assets as of the first quarter. Thrifts categorized as being in “problem status” are subject to increasingly strong supervisory action to ensure that management and the board of directors move aggressively to resolve the institution’s problems.

Thrifts that are rated composite “3,” while not considered problem institutions, warrant more than the normal level of supervisory attention. The number of institutions with 3 ratings rose from a recent low of 67 in 1998, to 98 by the end of 2000. (The commercial banking industry had a similar increase in 3-rated institutions during this period.) By the end of the first quarter, the number had declined to 90. Of these, 91 percent were “well-capitalized,” and thus have a capital cushion that increases their ability to work through their difficulties in an orderly manner.³

Supervisory attention is also focused on thrifts identified in other types of examinations, such as compliance, Community Reinvestment Act (CRA), and information technology (IT), as needing improvement. As of the first quarter, there were 67 thrifts rated 3 or below in compliance, including 6 thrifts rated 4 or 5. Sixteen thrifts were rated less than satisfactory in their CRA examination. Reflecting the rapid changes in technology, focus on privacy and security concerns, and increased demand for technologically savvy managers, 35 thrifts were rated 4 or 5 on their IT exam, and 24 were rated 3. In all cases, we work with these institutions to help them return to strong ratings.

³ On April 30, 2001, OTS proposed amendments to its assessment rule that would more accurately reflect the increased costs of supervising 3-, 4-, and 5-rated institutions.

G. Continuing Role of the Thrift Industry

1. Community Lenders with Residential Focus

Although thrifts can make consumer and, in limited quantities, commercial loans, they remain primarily focused on residential mortgage lending. Thrifts originated over 21 percent of all single-family mortgages made in the United States in the first quarter. Moreover, thrifts are the dominant originator of adjustable rate mortgages (ARMs). In the first quarter, roughly 69 percent of all new ARM originations were made by thrifts.⁴

The industry originated \$74.3 billion in single-family mortgages in the first quarter, the second highest quarterly volume on record. Since the end of 1995, the industry has originated over \$1 trillion in single-family home loans.

Single-family mortgage loans and related securities comprised almost two-thirds of thrift assets in the first quarter. In addition, 4.7 percent of thrift assets were held in multi-family mortgages, bringing the percentage of assets held in residential-related loans and securities to 70.1 percent.

While thrifts are primarily residential mortgage lenders, they have become more active in consumer and commercial business lending. The industry's ratio of consumer loans-to-assets was 6.3 percent in the first quarter, up from 4.5 percent at the end of 1990. Utilizing the expanded small business lending authority granted by the Economic Growth and Regulatory Paperwork Reduction Act of 1996, the industry's ratio of commercial loans-to-assets stood at 3.0 percent in the first quarter, up from 1.5 percent at the end of 1997.

⁴ Mortgage origination market share estimates based on data from the Mortgage Bankers Association of America and the Federal Housing Finance Board.

Thrifts also help their communities by making mortgages on hospitals, nursing homes, farms, churches, stores, and other commercial properties. Such loans comprised 4.0 percent of thrifts' assets in the first quarter.

2. Full Range of Financial Services

Besides loans and deposits, thrifts provide a wide range of savings and investment products to their communities. The industry's sales of mutual funds and annuities, and trust assets administered, have risen dramatically over the past five years. Total sales of mutual funds and annuities were \$2.9 billion in the first quarter of 2001, and \$12.8 billion for the year 2000, compared to \$6.4 billion in 1995. Trust assets administered totaled \$427.4 billion as of the first quarter versus \$13.6 billion at the end of 1995.

III. Risks Facing the Industry

A. Credit Risk

While the overall financial condition of the thrift industry is strong, the current economic slowdown suggests that rising levels of delinquent loans are a distinct possibility. In terms of credit risk, the industry's largest exposure is in residential mortgage loans. Fortunately, however, the housing market is very strong in most areas of the country and delinquencies on single-family residential loans have remained at very low levels. Barring a serious downturn in the economy, which seems unlikely, the overall credit quality of residential mortgage portfolios should remain healthy.

The slowdown in economic activity, however, is bound to have an adverse effect on marginal credits, particularly overextended consumers and commercial borrowers.

Thrifts are not immune to weakness in the business sector since 3.0 percent of thrift assets are held in commercial loans. Nor is the industry immune to problems in the consumer sector. In recent years, debt service burdens of consumers have generally grown more rapidly than their incomes, and the rate of consumer savings of disposable income has been disturbingly low.

Not surprisingly, banks and thrifts have been tightening credit standards, building loss reserves, and otherwise fortifying their balance sheets. As we have learned from experience, however, it is not sufficient to rely solely on bank and thrift managers to ensure the safety and soundness of the system. Vigilant supervision is important, particularly in a banking system such as ours where deposit insurance, together with ever-tougher competition, can blunt market discipline and encourage undue risk-taking by some institutions.

Given the current economic environment, we are placing increased emphasis on credit review in our examination process. OTS examiners are focusing on thrifts' credit quality, reserve policies, and capital adequacy. The loan monitoring, loan collection, and work out procedures of thrifts are being given increased scrutiny. Particular attention is being given to business-related loans originated during the height of the economic expansion.

B. Liquidity Risk/Funding Changes

We are also closely monitoring thrifts' liquidity, although it should be stressed that liquidity problems are rare in the industry, and when they do occur, are invariably triggered by weaknesses such as problem loans.⁵ As long as an insured depository institution is solvent and has eligible collateral, liquidity is available. Nevertheless, the thrift industry as a whole has become decidedly more dependent on wholesale

⁵ On March 15, 2001, OTS issued an interim rule to implement the recent repeal of the statutory liquidity requirement. The rule removes the existing regulation that requires savings associations to maintain an average daily balance of liquid assets of at least 4 percent of its liquidity base.

funding in recent years, and loan-to-deposit ratios have been increasing. These trends reflect the recent slow pace of deposit growth as well as our very competitive financial markets in which banks and thrifts must carefully balance the trade-off between liquidity and profitability.⁶

C. Operational Risk

Operational risk, which includes the risk of loss due to technical failures and human error, seems to be an ever present and growing concern in the financial services industry. The growth of internet banking, the outsourcing of core banking functions, and the rapid pace of technological and financial innovation has created new challenges and concerns.

Advances in technology have also created opportunities for thrifts, especially in the areas of marketing and broadening customer services. Thrifts also utilize technology to increase their understanding of certain credits, enabling better product pricing. The use of technology for these purposes is encouraged but must be done so responsibly.

Our IT examiners, and increasingly, technology-trained safety and soundness examiners, focus on how well thrifts' use of technology are designed and monitored to minimize operational risk and ensure thrift and customer security and privacy.

⁶ On May 11, 2001, OTS and the other federal banking agencies issued an advisory on the risks of brokered and other rate sensitive deposits. On June 8, 2001, OTS issued Examiner Guidance on wholesale borrowings. On June 19, we issued a Thrift Bulletin that outlines sound principles for liquidity management. That bulletin, among other things, stresses the importance of liquidity policies and procedures, management oversight, contingency planning, and scenario analysis.

Given the recent financial difficulties experienced by many “high tech” companies, thrifts’ contingency planning is receiving increased supervisory attention.⁷

D. Increasingly Competitive Environment

The increasingly competitive environment in the financial services industry has forced thrift executives to search not only for ways to cut costs but also for new business opportunities, which often have a more extreme risk/return profile than the traditional thrift business. Subprime lending, whether home equity or credit cards, is one such business. Well-managed subprime lending, with responsible marketing, pricing and terms, is an important element in expanding credit access. But the business is fraught with danger for consumers, institutions, and the deposit insurance funds when an excess of zeal for short-term profitability overcomes responsible management and monitoring, including adequate reserving and capitalization.⁸

Guiding an institution through these shoals successfully is, of course, the responsibility of each institution’s management and board of directors. The willingness of management and directors to understand and manage risk is one of the primary underpinnings of a safe and sound operation. A key part of OTS’s supervisory strategy is to hold regular meetings with senior thrift managers. OTS regional supervisory staffs meet regularly with thrift senior managers during onsite examinations and to discuss items of supervisory interest. OTS also holds meetings and conferences with senior managers from multiple thrifts to share ideas and discuss trends affecting the industry. During the past 18 months, OTS held 24 town meetings involving 240 thrifts; 20 Financial Management Seminars with 740 attendees; five

⁷ On June 11, 2001, OTS published a request for comment pursuant to section 729 of the Gramm-Leach-Bliley Act. OTS and the other federal banking agencies are studying their regulations on the delivery of financial services. The purpose of the study is to report findings and conclusions to Congress, together with recommendations for appropriate legislative or regulatory action to adapt existing requirements to online banking and lending.

⁸ On January 31, 2001, OTS and the other federal banking agencies issued expanded guidance intended to strengthen the examination and supervision of institutions with significant subprime lending programs. The guidance supplements previous subprime lending guidance issued March 1, 1999.

Directors' Forums that attracted 1,275 attendees; and a Leadership Conference attended by over 400 thrift CEOs and directors from about 250 institutions.

Thrift senior managers at these meetings voiced several common issues. First and foremost was that thrifts operate in a very competitive environment, especially in the conforming single-family mortgage market. This means thrifts need to think and plan strategically, especially given the country's changing economy and demographics. To ensure long-term profitability and earnings growth, many thrift managers are focused on finding new markets to serve and analyzing new business lines. These managers strongly feel that niche markets, emerging markets, and markets neglected or forgotten after "mega mergers" reduced local banking presence offer good opportunities for profitable expansion.

Each thrift must adopt its own strategy to compete in an increasingly competitive environment. Our examination focus is to ensure that thrifts have the requisite managerial expertise, sound policies and procedures, and adequate systems before entering new lines of business. We also follow up to ensure that institutions effectively manage and monitor these business lines once entered.

IV. OTS Focus During the Next Twelve Months

A. Ensure problem thrifts have capable management

Onsite examinations and regular offsite financial monitoring are two of the tools we use to keep on top of issues and institutions, and ensure thrift management and boards of directors are adequately addressing weaknesses. Two other supervisory tools that we use to monitor problem institutions are the Regional Managers Group meetings, which happen 10 times a year, and high risk video-conferences, which happen 3 times a year for each region – a total of 15 3- to 5- hour meetings to discuss high risk or high profile institutions each year. These tools enable us to learn from

each other, enhance consistency across the country, and stay on top of problem institutions, while retaining primary responsibility for supervision in our regions.

B. Functional Regulation

OTS has made a considerable effort in the last several years to reach out to other state and federal functional regulators to coordinate and streamline potential overlapping regulatory interests. These activities involve meetings, regular communications, and joint activities and programs, often through various supervisory coordinating entities such as the National Association of Insurance Commissioners (NAIC), the National Association of Securities Dealers (NASD), and the North American Securities Administrators Association (NASAA).

We have worked extensively over the last several years with the NAIC to coordinate the regulatory overlap that has developed with increased insurance company acquisitions of thrift institutions. As a result of this coordination, OTS has in place information sharing agreements with 45 state insurance regulators. These efforts include frequent appearances by OTS and NAIC officials at programs sponsored by OTS and by the NAIC or by individual NAIC state members. We have also sponsored several joint programs. OTS senior managers have attended NAIC training sessions on the state insurance regulatory system. Likewise, the state insurance commissioners, their staff, and NAIC staff attended an OTS-sponsored training program about the thrift regulatory system.⁹ Our Regional Directors have working relationships with insurance commissioners in States in their region where insurance companies that own thrifts are domiciled.

OTS regional staff also coordinate closely with their regional counterparts at the NASD on issues of common interest involving securities activities by thrift service

⁹ OTS and the other federal banking agencies issued final consumer protection rules for the sale of insurance products by depository institutions on December 4, 2000. The final rule implements section 305 of the Gramm-Leach-Bliley Act. As required by the statute, the agencies consulted with the NAIC.

corporations engaged in securities brokerage activities. Similarly, we have developed a good working relationship with staff of the NASAA that enables us to coordinate and leverage our resources to achieve success in areas of mutual interest. We continue to work with the SEC on policy matters (such as the privacy regulations required under the Gramm-Leach-Bliley Act) and, occasionally, on matters involving specific institutions.

C. Coordination with other Federal Banking Agencies (FBAs) and State Banking Regulators

OTS also works closely with other FBAs and state bank regulators, both through the Federal Financial Institutions Examination Council (FFIEC) and individually, where appropriate, to identify emerging issues in the financial institutions industry and to coordinate supervisory activities. This activity occurs both in Washington and at the regional level, directly with other regulators and through the Conference of State Bank Supervisors (CSBS). Topics of mutual interest include emerging risks, adverse trends, and other supervisory matters. This is a mutually beneficial relationship that keeps all parties apprised of potential problems, emerging issues, and possible overlaps of regulatory authority that may pose potential regulatory burdens or gaps in regulatory coverage.¹⁰ For example, in connection with proposed OTS regulations on mutual savings associations and mutual holding companies, we have met with seven state banking commissioners. CSBS was very helpful in arranging these meetings.

In matters involving preemption, we notify the appropriate state regulator to obtain their views when an institution asks us to opine that HOLA preempts a particular

¹⁰ OTS supervises 148 state-chartered savings associations and 32 thrift holding company structures whose thrifts subsidiaries are all state-chartered. This role, which is similar to that of the FDIC and the Federal Reserve with respect to state-chartered commercial banks and savings banks, requires significant coordination with state bank regulators on a day-to-day basis in our regions.

state regulatory action. If we issue an opinion we send a copy to the state regulator and CSBS.

D. Keep supervisory staff well trained and informed

Another aspect of our regulatory oversight is OTS's focus on dynamic, needs-based employee training. We have inventoried the skill sets possessed by all of our examiners and, utilizing that information, are able to identify needed areas of training. This typically involves a periodic assessment by regional supervisors of upcoming and emerging issues at institutions in the region, an assessment of the strength of regional examiners in the skills required to address these needs, and training targeted to address areas of need. Our new Professional Development Program, geared to enhancing individual competencies and skills; specialty examiner tracks; accreditation programs; and a soon-to-be-piloted management development program, keep employee skills at top levels.

OTS examiners typically receive training several times annually. Our training is designed for maximum impact with minimum disruption to the day-to-day operations of the agency. Training is delivered in various forms, including computer-based programs, video-conferencing, outside programs, and by pooling specialized examiner resources so individuals can share their expertise nationally within the agency. Both our trust and IT examiners, although regionally based, work across the country, and the agency's credit card specialists are always on call to deal with this specialized set of risks. During 2000, examiners worked cross-regionally for a total of almost 800 days, and we had 19 details to Washington. These exchanges enhance the skills and perspective of both the sending and recipient offices.

In addition to our internal training activities, we work closely with the other FFIEC agencies to identify areas that warrant more extensive and coordinated training

initiatives. This past year, the FFIEC piloted the concept of just-in-time training on CD to get training on hot issues such as subprime lending and privacy out quickly to a wide audience. We hold staff conferences and teleconferences to promote sharing of ideas and experiences among supervisory staff. We are also improving our information systems to simplify and expedite access to internal and publicly available thrift and market information.

E. Early warning systems

We are increasing our use of offsite early warning systems to help pinpoint potential problem areas. In addition to our Net Portfolio (NPV) Model, OTS examiners and analysts utilize our Risk Assessment Model (RAM) and our recently implemented Risk Monitoring System (RMS) to assist offsite financial analysis. Both risk identification models utilize financial “triggers and hits” to quickly identify areas that need special attention and analyses. The RMS also provides our examiners and analysts with direct links to thrift web sites, thrift stock price data, SEC filings, and general economic information, all used to closely monitor and analyze thrift operations between onsite exams.

V. Items for Legislative Consideration

We are developing a list of legislative proposals for your consideration that would reduce regulatory burden on the thrift industry, streamline and improve OTS supervisory authority, and make technical corrections. The items we are studying include:

- Statutory authority for a Deputy Director of OTS. This would avoid the potential for gaps in OTS regulatory and enforcement authority if there is a vacancy in the office of the Director. This is particularly important because of the delay inherent in filling vacancies for Presidential appointments.

- Permitting federal thrifts to merge and consolidate with their nonthrift subsidiaries directly. Today a federal thrift may only merge with another depository institution. We have recently learned of a situation where current law will cost the institution an estimated \$11 million to structure a merger in a way that is consistent with existing law.
- Modernizing thrift community development investment authority to permit investments to promote the public welfare and remove obsolete provisions based on HUD programs that have been off the books for 20 years.
- Eliminating the requirement that a service company subsidiary of a thrift must be organized under the laws of the state where the home office of the thrift is located. This geographic restriction was imposed before interstate branching, the Internet, and telephone banking, and today simply serves no useful purpose.
- Enhanced small business and consumer lending authority to enable thrifts to better serve the credit needs of their communities.
- An exception from broker-dealer registration by thrifts equivalent to the exception that banks have under the Securities Exchange Act of 1934. The SEC has issued an interim rule accomplishing this result, but it may be appropriate to confirm the change by statute.
- An exception from investment adviser registration by thrifts equivalent to the exception that banks have under the Investment Advisers Act of 1940. The SEC has announced it is considering rulemaking to address this issue, but, as with the broker-dealer exception, a confirming statutory amendment appears appropriate.

After final policy reviews and consultation with other affected agencies, we plan to submit a package of legislative proposals with a recommendation for their enactment.

VI. Conclusion

Over the past several years, the thrift industry has expanded and diversified while achieving strong financial results. At OTS, we have used this time to ensure that our staff and technology is poised to deal with new risks and to assist the institutions we supervise as they move into new areas, so they are properly focused on long-term profitability and responsible service to their customers and communities. The challenges continue, but both the industry and the agency are well-positioned to meet them.

