The Big Fix Synopsis:

The widespread failure of Savings & Loan institutions in the late 1980s was the Great Depression of its time. By 1990, deposits in over 350 thrifts disappeared as banks declared they were insolvent. Hundreds of other thrifts teetered on the edge of bankruptcy. The federal bailout needed to stabilize the financial markets was, at its time, the largest in U.S. history and resulted in a tax increase that George Bush swore to his voters would not occur. As taxes increased to reduce a federal deficit inflated by the bailout of the S&L industry, the economy spiraled into recession. Taxpayers feeling the crunch of an economic recession were left to carry the financial burden created by the S&L debacle.

The causes of the S&L debacle have been the subject of much scholarship, analysis and government inquiry. Most sources agree that the convergence of legislation that increased the investment power of thrifts, fraudulent and dangerous banking practices within the industry and the failure of regulatory agencies resulted in a financial crisis that cost taxpayers $300 billion. Bank examiners, however, had publicly stated as early as 1987 that the majority of thrift failures were the result of management misconduct, insider lending, and outright fraud. Their examinations, recommendations and requests for action were either ignored or interfered with.

The Big Fix is a source on the S&L debacle that painted a portrait of a largely overlooked factor in the implosion of the Savings & Loan industry---Congressional protection to S&L industry highflyers who were bankrupting their thrifts. The meticulous research in James Ring Adams's book documented some of the costliest episodes in the S&L debacle. From Florida to Ohio to Texas to Kentucky, each episode followed a similar pattern. Banks owned by prominent figures in the S&L industry were used as personal piggy banks--wealth was acquired through fraud. Prominent figures in the S&L industry were, also, prominent campaign contributors and used their fortunes to cultivate personal friendships with politicians.

The relationship of S&L industry high-flyers to state and federal politicians bought the industry favorable legislation, friends in charge of regulatory agencies, and political interference with examiners and regulators who threatened to shut down troubled thrifts. Congressional response to an S&L industry that had been struggling since the 1970s was to pass the Garn-St. Germain Act in 1982, which increased the investment powers of thrifts and federal insurance on deposits. California, Texas and Florida had the most liberal legislation regulating the S&L industry.

In Florida, Savings & Loan institutions were regulated by the State Comptroller's Office, a position that was particularly vulnerable to the lobbying prowess of the S&L industry. The World Financial Corporation (WFC), owned by a former CIA operative, was responsible for bankrupting financial institutions from Colombia to the Persian Gulf in the late 1970s. Despite active investigations into the WFC from federal law enforcement and financial regulatory agencies, the WFC continued operations until it imploded. It was a pattern that would be repeated throughout the 1980s as drug smugglers and money launderers ran financial institutions in Florida into the ground while bank examiners and federal investigators voiced their objections in vain.

William Isaac, FDIC Chairman during the S&L debacle, formerly worked for a bank that held joint investments with the WFC. Before he was responsible for supervising 13,000 commercial banks, William Isaac was interacting with some of the shadiest figures in Florida's financial industry. The Butcher Brothers of Tennessee claimed credit for William Isaac's rise to power in the FDIC. In 1982, the Butcher Brothers were responsible for the largest series of bank closures since the Great Depression. Jake and C.H. Butcher built a network of thrifts in the heartland whose assets swelled through fraud such as round-robin loans and other creative accounting techniques. Their banks were in trouble since the late 1970s, however, their political clout enabled the operation of their thrifts until the inevitable collapse cost federal insurance funds $1 billion.

In 1985, Ohio declared the first emergency bank holiday, the forced closure of commercial and S&L banks to prevent a bank run, since the Great Depression. The financial entanglements of Ohio's Home State Savings with Florida's E.S.M. Government Securities caused the crisis. E.S.M. and Home State Savings, owned by Marvin Warner, the Carter administration's Ambassador to Switzerland, engaged in a reciprocal arrangement to generate false profits and hide losses from their respective fraudulent financial practices. When the situation erupted and Home State collapsed, the losses were four times the amount in the Ohio Deposit Insurance Guaranty Fund (ODGF). The panic created caused bank runs on other ODGF members transforming the failure of Home State Savings into an industry wide crisis that catapulted the Ohio economy into recession.

Texas was the heart of the Savings & Loan debacle. Texas laws were among the most lenient in the country; thrifts were granted the power to invest 100% of their assets. By 1988, 40% of the state's 213 thrifts were bankrupt and responsible for more than one half of the S&L industry's recorded loss of $2.3 billion in the fourth quarter of the fiscal year. Texas thrifts were pioneers in the art of bank fraud—from the 'rent-a-bank' scheme of buying and selling thrifts to hide bad assets to land-flip schemes that overvalued property to obtain inflated loans; Texas thrifts were involved in it all. The bankruptcy of Empire Savings & Loan of Mesquite, TX initiated investigations that revealed a network of 40 S&Ls in Texas involved in fraudulent activity that stretched from Florida to California and intersected with organized crime. Despite the findings of investigations, politically connected TX thrifts remained in operation, increasing the cost of the eventual bailout.

The greater the fraud perpetrated by Savings & Loan industry high-flyers the greater their investment in political campaigns. The influence the S&L industry bought through campaign contributions was wielded to not only pass favorable legislation and block regulatory initiatives. Congressmen were oftentimes called upon to interfere with bank examiners who were threatening to shut down corrupt thrifts. By 1986, losses from the S&L industry were pushing the Federal Savings & Loan Insurance Corporation (FSLIC), responsible for backing deposits in Savings & Loan institutions, into bankruptcy. The legislation needed to keep the FSLIC afloat was held hostage by congressmen who pressured the Bank Board, responsible for regulating the industry, to prevent their examiners from taking action against troubled thrifts. Congressional interference into the investigation of Charles Keating, owner of Lincoln S&L, which cost the FSLIC $2.5 billion when it was put into receivership in 1989, sparked a political scandal that tarnished careers. The House Ethics Committee, however, determined after its investigation that congressional interference with regulators was proper and consistent with the role of a member of congress.

The Competitive Equality Banking Act of 1987 increased the reserves of the FSLIC, however, in less than two years the fund was once again bankrupt. By 1989, large-scale federal intervention was needed to save the Savings & Loan industry. Congress hammered out the Financial Institution Reform, Recovery, and Enforcement Act (FIRREA) in 1989 to prevent the financial crisis caused by the S&L industry from escalating into a Great Depression. FIRREA made billions of dollars available to cover the deposits of failed thrifts and did a complete overhaul of the regulatory structure of the financial industry. The FSLIC and its governing agency, the Federal Home Loan Bank Board, were abolished; its responsibilities were distributed to various bureaucratic bodies. FIRREA promised to not only save the S&L industry but also prevent future financial crisis. The Bank Board regulators who were obstructed from taking action against corrupt thrifts knew better. The next financial disaster was only a matter of time.