CHAPTER 7

Loss Sharing

Introduction

Loss sharing is a feature that the Federal Deposit Insurance Corporation (FDIC) first introduced into selected purchase and assumption (P&A) transactions in 1991. The original goals of loss sharing were to (1) sell as many assets as possible to the acquiring bank and (2) have the nonperforming assets managed and collected by the acquiring bank in a manner that aligned the interests and incentives of the acquiring bank and the FDIC. Under loss sharing, the FDIC agrees to absorb a significant portion of the loss—typically 80 percent—on a specified pool of assets while offering even greater loss protection in the event of financial catastrophe, and the acquiring bank is liable for the remaining portion of the loss.

Loss sharing can provide benefits to all parties involved when compared to the conventional P&A structure, particularly where nonperforming assets are involved. For example, by keeping loss share assets in the banking (as opposed to the liquidation) environment, the FDIC may benefit by better preserving the value of the assets. Failed bank asset portfolios with loss sharing are more attractive to acquirers because the FDIC is absorbing a significant portion of the loss. Another benefit of loss sharing is that the asset management and disposition incentives of the acquirer and the FDIC become more rationally aligned as both parties are sharing in the loss. This common interest reduces the need for direct FDIC asset disposition oversight and helps provide a more streamlined disposition process for the loss share assets.

The FDIC has entered into 16 loss sharing agreements that were created to resolve 24 banks that failed between 1991 and 1993. Many of the failed banks were fairly large. While fewer than 10 percent of banks that failed during that period were resolved using loss sharing, those transactions accounted for 40 percent of the total failed bank assets.

Loss sharing has evolved into a vehicle that allows the FDIC to better manage some of the unique problems associated with the marketing of large banks. In the early 1990s,

large banks were difficult to market because of their sizable commercial loan and commercial real estate portfolios. The FDIC already had a record amount of assets in liquidation, and the explosive growth of commercial assets in liquidation had become a critical concern. Acquiring institutions had been extremely reluctant to acquire the assets in FDIC transactions.

One reason for that reluctance was that the time allotted to perform due diligence was limited, while the associated costs were high. The FDIC accommodated a number of potential acquirers who wished to perform due diligence at the failing bank, and all potential acquirers were required to complete their reviews before the bid submission date. That constraint often allowed little time for any given acquirer to have more than a cursory review of a complex commercial loan and real estate portfolio. A thorough due diligence of a large failed bank could also be rather expensive for a potential acquirer, with no assurance that it would be the winning bidder.

In addition, many acquirers were reluctant to purchase large portfolios of commercial loans. In many cases, the underwriting criteria of the failed bank were poor and may have been a primary reason for the bank's failure. Many potential acquirers wished to avoid the additional costs associated with managing and working out those problem assets.

Finally, because almost every region of the United States had experienced declining markets for commercial real estate in the late 1980s and early 1990s, there was considerable uncertainty regarding collateral values and future economic conditions. Even when acquiring banks were willing to purchase the commercial real estate loan portfolios, they typically would incorporate a large discount into their bid to compensate for the risk of further market declines.

Loss sharing was designed to address those concerns by limiting the risk associated with acquiring large commercial loan and real estate portfolios and to reduce FDIC costs and insurance fund outlays by having greater volumes of those banking assets owned and managed by the banking sector.[1] The FDIC accomplished its objective of selling those types of assets to the acquirer by absorbing a significant portion of any credit losses on commercial and commercial real estate loans, typically 80 percent for a certain period of time—ranging from three to five years—during which time the FDIC as receiver reimbursed the acquiring bank for 80 percent of net charge-offs (charge-offs minus recoveries) plus reimbursable expenses. During the shared recovery period, the acquiring bank paid the receiver 80 percent of any recoveries (less any recovery expenses) on loss share assets previously experiencing a loss. The shared recovery period ran concurrently with the loss share period and lasted another one to three years beyond the expiration of the loss sharing period.

Acquiring institutions would assume the remaining 20 percent of loss. By having the acquirer absorb a limited amount of the credit loss, the FDIC hoped to pass most of

1. Several of the earlier loss share agreements covered loan categories in addition to large commercial loans and real estate portfolios.

the failed bank's commercial and commercial real estate loans to the acquirer while still receiving a substantial bid premium for the bank's deposit franchise. Also, by having the acquirer absorb a portion of the loss, the FDIC was attempting to induce rational credit management behavior. Eventually, loss sharing was structured to include a "transition amount" so that if losses exceeded the projected amount, the FDIC and the acquirer would share the losses on a 95/5 basis, respectively. The transition amount was defined as the FDIC's estimate of the loss on the loss share assets acquired by the acquirer. The transition amount was used by the FDIC to address the acquirer's concerns about catastrophic losses resulting from limited due diligence time and uncertain collateral values stemming from deteriorating markets.

The FDIC also expected to reduce resolution costs by keeping assets in the banking sector rather than placing them into a liquidation mode. The prevailing view was that certain failed bank assets would lose additional value if placed into a receivership or liquidation mode because of the break in the customer-bank relationship. (The loss in value from placing an asset in receivership was referred to as the liquidation differential.)

An additional benefit of loss sharing is that the structure softens the effect of the bank failure on the local market by keeping more of the failed bank's borrowers in a banking environment. The acquiring bank can more easily work with the borrowers to restructure problem credits or to advance additional funding where prudent. This "anticredit crunch" benefit avoids the exacerbation of declining collateral values that could be precipitated by having a significant amount of local failed bank assets falling into a liquidation mode.

Background

The FDIC entered the early 1990s with record levels of assets in liquidation and dwindling insurance reserves. The number of problem banks hovered near 1,100, and the amount of assets held by problem banks had increased from $236 billion in 1989 to a record $609 billion in 1991. A relatively large number of small banks failed during that period only to be replaced on the problem bank list by a nearly offsetting number of larger banks (See table I.7-1 and chart I.7-1.)

Many of the new problem banks were exceptionally large and were concentrated in deteriorating markets in the Southwest and Northeast. Additionally, the portfolio of problem loans that the FDIC was servicing had escalated to record levels, while insurance funds were at an all-time low and provided no liquidity. (See chart I.7-2.) The FDIC needed to develop a feature for resolution transactions that allowed the FDIC to keep more assets in the banking sector and to better align the interests of the FDIC and the acquiring bank. That alignment of interests would serve to rationalize the asset management incentives of the acquiring bank and also minimize the need for active FDIC asset oversight. If successful, that feature would accomplish the following:

Table I.7-1

Number and Average Size of Failed Banks and Problem Banks 1988–1991

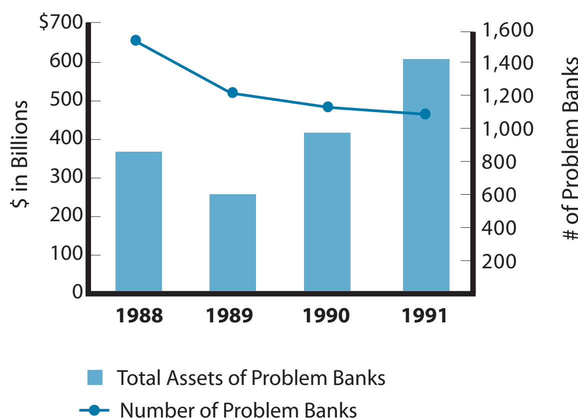
($ in Millions)

Year	Number of Bank Failures	Average Total Assets of Failed Banks	Number of Problem Banks	Average Total Assets of Problem Banks
1988	279	$189	1,406	$251
1989	207	142	1,109	213
1990	169	93	1,046	391
1991	127	492	1,090	559

Sources: FDIC Division of Research and Statistics and FDIC annual reports.

Chart I.7-1

Number and Total Assets of Problem Banks **1988–1991**



Source: FDIC annual reports, 1988–1991.

- Reduce resolution costs;
- Conserve FDIC cash reserves; and
- Limit the explosive growth of assets in FDIC liquidation, thus minimizing the need for the FDIC to hire additional staff.

On September 19, 1991, the FDIC used the loss share method for the first time with the resolution of Southeast Bank, Miami, Florida, which had nearly $10.5 billion in total assets. Southeast Bank was located in a less economically troubled region of the country (compared to the Texas or the New England markets) and had attracted the interest of several relatively strong prospective acquirers. As such, the FDIC believed that the situation represented an opportunity to experiment with a new form of resolution—an assistance agreement with loss sharing.

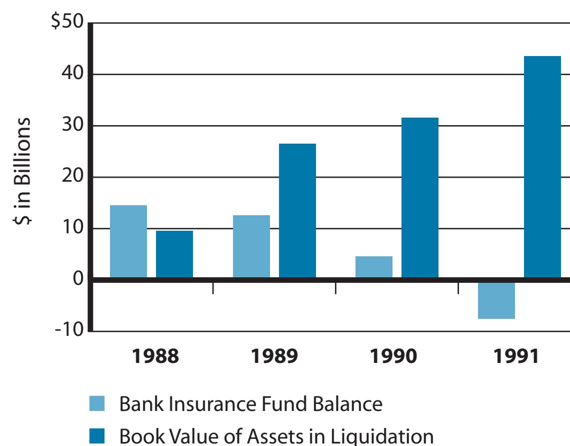
The FDIC worked virtually around the clock with prospective bidders to collectively develop a transaction structure with which all parties were comfortable. In that transaction, the acquiring bank would assume all assets, including classified and nonperforming assets (excluding owned real estate and in-substance foreclosure assets).[2] All loans acquired were designated as shared loss assets eligible for coverage

under the loss sharing provisions of the purchase and assumption agreement.

The winning bidder in that transaction was First Union National Bank of Florida. That acquiring bank was required to hold and manage the covered failed bank assets, with the FDIC agreeing to reimburse the acquirer for a major portion—in that case, 85 percent—of the loss on those assets for a set period of time. The 15 percent level of loss exposure was chosen to be high enough to have the acquirer responsibly manage the shared loss assets—to manage those assets as if its own money was on the line—but low enough to dampen the effect of any significant error in the initial loss estimate.[3]

Chart I.7-2

Comparison of the Bank Insurance Fund **and the FDIC's Total Assets in Liquidation 1988–1991**



Source: FDIC annual reports, 1988–1991.

That loss share agreement required the FDIC to agree to two major accommodations in its attempt to have loss sharing supplant the old large bank resolution structure (in which the FDIC alone shouldered the responsibility and risk for the failed bank assets). The first accommodation involved the FDIC's agreeing to take a note—the nonaccrual asset note—bearing a nominal rate of interest as a funding mechanism for the nonaccrual assets. The second accommodation involved the FDIC's offer to purchase perpetual preferred stock to offset the additional burden on the acquiring bank's capital that would be imposed on the acquirer as a result of its ownership of the classified assets. That stock purchase was designed with features that encouraged the acquirer to redeem the stock in the near term and enhance the marketability of the stock should it not be redeemed when expected.

In October 1991, loss sharing played a supporting role in the resolution of seven failed New Hampshire banks.[4] In that situation, the FDIC placed the majority of the failed bank assets with an outside contractor. It passed the smaller balance, one-to-four-

2. Before that transaction, many large bank resolutions had used a separate asset pool structure in which classified (problem) assets were segregated into a separate asset pool to be serviced by the acquiring bank. The FDIC retained all risks of ownership of the separate asset pool, including risks associated with loss in asset values, funding costs, and expenses. Direct FDIC oversight of the management and operating expenses of the separate asset pool was necessary because the FDIC was bearing all of the ownership risk.

3. For example, the original estimate of loss on covered assets in the Southeast Bank transaction was $869 million. As such, the acquirer's 15 percent risk exposure would amount to $130 million. Under loss sharing, if actual losses were substantially underestimated (say, by 50 percent), the acquirer would have an additional loss exposure of only $65 million, an amount that would be painful, but by no means fatal, to the acquirer of the failed bank.

4. See Part II, Case Studies of Significant Bank Resolutions, Chapter 10, The New Hampshire Plan.

family residential and consumer loans to the acquirers of the two failed banks using a loss share structure in which the FDIC would absorb 90 percent of the loss for a period of three years and receive 90 percent of the recovery on those assets for a period of four years.

The FDIC completed its next major loss sharing agreement in November 1991 with the resolution of Connecticut Savings Bank, New Haven, Connecticut. Much of New England was in recession at the time, including the New Haven area. Centerbank, Waterbury, Connecticut, acquired Connecticut Savings Bank under a loss sharing arrangement in which the FDIC absorbed 85 percent of the loss on commercial assets and 80 percent of the loss on consumer assets for a period of two years. The FDIC would receive 60 percent of the recovery on commercial assets and 40 percent of the recovery on consumer assets covered by that agreement for a period of three years.[5] (See table I.7-2 for an illustration of the variety of terms for the early loss share transactions.)

In mid-1992, the FDIC conducted a series of meetings to develop a standard loss share structure. The meetings focused on the following:

- Determining which asset types were most suitable for loss share coverage;
- Developing a "stop-loss" mechanism to limit the acquirer's exposure to unanticipated losses on the shared loss assets;[6] and
- Developing a more "standardized" structure for future loss share transactions to increase the comfort level with the loss share structure for potential acquirers, thereby enabling them to be more efficient in performing due diligence and pricing risk. A standardization of terms would also allow the FDIC greater efficiency in marketing problem institutions and would minimize the need for additional monitoring resources.

As a result of the meetings, the following was determined:

- The commercial and industrial loans and the commercial real estate loan portfolios (performing and nonperforming) would sell with a loss sharing provision because those assets typically involved high dollar balances and a greater variability in risk.
- The one-to-four-family mortgage and consumer loan portfolios (performing and nonperforming) generally would not be sold with loss share coverage because the

5. The FDIC would share any recovery on a loss share asset under a predetermined formula. Typically, the shared recovery coverage ratio would be identical to the shared loss coverage ratio for a specified pool of assets. In several of the earlier transactions, however, the FDIC agreed to provide the acquirer with a larger share of any recoveries as an incentive to better manage and collect on assets that had been charged off. Examples of the enriched level of recovery sharing on the credit card portfolio at Southeast Bank, as well as the commercial and, most notably, consumer loan portfolios at Connecticut Savings Bank, are detailed in table I.7-2.

6. Acquirers wanted to limit their risk exposure to unforeseen and catastrophic losses on loss share assets arising from their limited due diligence time and the uncertain value of collateral located in deteriorating markets.

Table I.7-2

Summary of Loss Share Transactions 1991

($ in Millions)

Failed Bank	Southeast of West Florida South-east Bank	Dartmouth Numerica S.B.* New Hampshire S.B.	Amoskeag BankEast Nashua Trust Bank Meridian	Connecticut S.B.
Acquirer	First Union National Bank of Florida	New Dartmouth Shawmut	First NH Bank	Centerbank
Acquisition Date	Sept. 19, 1991	Oct. 10, 1991	Oct. 10, 1991	Nov. 14, 1991
Total Assets At Resolution	$10,478	$2,269	$2,109	$1,047
Beginning Amount of Loss Share Assets	$7,941	$876	$622	$555
Term: For Shared Losses	5 years	3 years	3 years	2 years
For Shared Recoveries	7 years	4 years	4 years	3 years
Shared Loss Coverage	All loans except credit cards 85%/15%	1-4 residential (less than $191,250)	1-4 residential (less than $191,250)	Commercial 85%/15%†
	Credit cards Yr. 1 - 85%/15% Yr. 2 - 80%/20% Yr. 3 - 75%/25% Yr. 4 - 70%/30% Yr. 5 - 65%/35%	Consumer (less than $100,000) All categories 90%/10% Quarterly threshold	Consumer (less than $100,000) All categories 90%/10% Quarterly threshold	Consumer 80%/20%
Shared Recovery Coverage	All loans except credit cards Percentage same as loss share	Percentage same as loss share	Percentage same as loss share	Commercial 60%/40%†
	Credit cards 65%/35%			Consumer 40%/60%
Transition Amount	Not applicable	Not applicable	Not applicable	Not applicable

* S.B. : Savings Bank

† By P&A agreement definition, includes any nonconsumer (multi-family and 1-4 residential) loans.

Sources: FDIC Division of Resolutions and Receiverships reports.

risks for those types of assets were considered low and were more easily ascertainable.

- A nonaccrual asset note would be offered to the acquirer to help fund the nonaccrual commercial assets. That type of note was offered in some of the earlier transactions and paid a nominal rate of interest. (The possibility of adverse tax consequences soon ended the attractiveness of that option.)
- The FDIC would share in recoveries on the same basis that it shared in losses.
- The stop loss mechanism could best be implemented via use of the "transition amount," which represents the FDIC's best estimate of the loss on shared loss assets. It is set so that if asset losses exceed it, the FDIC's loss coverage is then increased to 95 percent, and the acquiring bank's exposure is reduced to 5 percent of the loss over the transition amount. The transition amount successfully addressed acquirers' concerns of unanticipated loss exposure because of limited due diligence time and uncertain economic factors in the future.

The General Structure of Loss Sharing

The following sections review the terms and conditions of the most recent loss sharing P&A agreements, which were the product of the FDIC's standardization effort described above. In addition, they include more detailed information regarding the treatment of shared loss assets, the shared loss and shared recovery mechanisms, transition amounts, reimbursement procedures for shared losses and recoveries, and the administration of the shared loss agreement.

Shared Loss Assets

Shared loss assets generally consist of commercial and commercial real estate loans. Consumer loans, home equity loans, and residential mortgage loans usually are not covered in shared loss assets because those loans are of better quality. The relatively small balances of those loans, coupled with their large number of transactions, also make monitoring costs very expensive.

Shared loss assets initially are recorded at the failed bank's book value and, thereafter, the value of a shared loss asset may be increased by additional advances, capitalized expenditures, and accrued interest (subject to certain limitations); the value may decrease by the amount of principal payments received and charge-offs recorded. Capitalized expenditures are permitted only on owned real estate, and such expenditures must be capitalized in accordance with generally accepted accounting principles. (Environmental expenditures are excluded from loss share coverage.) Advances cannot exceed certain specified percentage limitations (generally 10 percent of the book value as of the

commencement date) and are not allowed on any loan on which the acquiring bank has recorded a charge-off.

Shared loss loans may be amended, modified, renewed, or extended, and substitute letters of credit may be issued in lieu of original letters of credit. The amount of principal remaining to be advanced on a line of credit, however, may not be increased beyond the original amount of the commitment. Paydowns on revolving lines of credit may be readvanced up to the original amount of the commitment. Terms may not be extended beyond the end of the final quarter through which the receiver has agreed to reimburse losses under the agreement.

Shared loss coverage ceases upon the sale of an asset or upon the making of advances or amendments that do not comply with the restrictions described above. Shared loss coverage also ceases if the acquiring bank exercises collection preference regarding a loan held in its own portfolio that is made to or attributable to the same obligor as a shared loss loan.

Shared Loss Arrangement

During the shared loss period, usually the FDIC as receiver reimburses the acquiring bank for 80 percent of net charge-offs (charge-offs minus recoveries) of shared loss assets plus reimbursable expenses. The acquiring bank generally pays the receiver 80 percent of recoveries less recovery expenses on covered assets previously experiencing loss.[7]

Losses are defined as charge-offs or write-downs of the value of shared loss assets recorded in accordance with examination criteria. Losses on the sale of real estate are included, but losses on the sale of shared loss loans are generally excluded.[8]

Recoveries are defined as collections of (1) charge-offs of shared loss assets and reimbursable expenses, (2) charge-offs recorded by the failed bank (including charge-offs of consumer and residential loans recorded by the failed bank, whether or not such loan categories are designated as shared loss assets under the agreement), and (3) gains on the sale or disposition of real estate.

Reimbursable expenses are defined as out-of-pocket expenses paid during the shared loss period to third parties (excludes payments to affiliates) to effect recoveries and to manage, operate, and maintain owned real estate, less income received on other real estate (amount may be negative). Expenses that are not covered include (1) income taxes; (2) salaries and related benefits of employees; (3) occupancy, furniture, equipment, and data

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7. The term of the shared loss period varies from two to five years. The term of the shared recovery period runs concurrently with the shared loss period with an additional one to three years. The loss sharing and recovery sharing percentages may also vary by transaction and by asset category.

8. While losses on the sale of loans are generally excluded to limit the receiver's exposure to interest rate risk, in cases where circumstances indicate that allowing the acquiring bank to sell loans may be in the receiver's best interest, coverage may be extended to include losses on the sale of loans; however, limitations regarding the dollar amount of loans that may be sold and the amount of resulting losses that may be eligible for reimbursement are established.

processing expenses; (4) fees for accounting and other independent professional consultants (other than legal fees and consultants retained for environmental assessment purposes); (5) overhead or general and administrative expenses; and (6) expenses not incurred in good faith or any extravagant expenses.

Transition Amounts

The transition amount is determined by using an estimate of the loss expected on the assets subject to coverage. Net losses in excess of the transition amount are reimbursed at 95 percent instead of 80 percent; however, the payment of the additional 15 percent reimbursement is deferred until the end of the agreement.

Certificates and Payments

Acquiring banks are required to file certificates within 30 days of the end of each calendar quarter during the shared loss period and recovery period. Dollar amounts for the following items must be reported on the certificate: (1) charge-offs, (2) recoveries, (3) net charge-offs, and (4) reimbursable expenses. If the shared loss amount is positive, the receiver will reimburse 80 percent of the amount within 15 days of receipt of the certificate. If the shared loss amount is negative, the acquiring bank must remit 80 percent of the amount with the certificate.

During the recovery period, the amount of recoveries and recovery expenses must be reported on the certificate. The recovery amount is equal to recoveries less recovery expenses. The acquiring bank must remit 80 percent of the recovery amount with the certificate.

Administration of the Shared Loss Agreement

The acquiring bank is required to manage, administer, and collect shared loss assets consistent with usual and prudent business and banking practices and in a manner consistent with internal practices, procedures, and written policies. It must use its best efforts to maximize collections and use its best business judgment in effecting charge-offs. It must maintain separate accounting records for shared loss assets. The acquiring bank is prohibited from contracting with third parties to provide services if the assuming bank normally provides the service regarding its own assets that are not subject to loss sharing.

Within 90 days after each calendar year end, the acquiring bank must furnish the FDIC a report signed by its independent public accountants containing specified statements relative to the accuracy of any computations made regarding shared loss assets. It must also perform a semi-annual internal audit of shared loss compliance and provide the FDIC copies of the internal audit reports and access to internal audit work papers.

Additionally, the FDIC may perform an audit, of such scope and duration as it may determine to be appropriate, to ascertain the bank's compliance with the assistance agreement.

The FDIC provides formal procedures to resolve any disputes that may arise in connection with the loss sharing arrangement. The parties are required to make a good faith effort to resolve a dispute within a 45-day period. Any disputes that cannot be resolved within that period are submitted for arbitration. Arbitration issues regarding charge-offs are resolved by the acquiring bank’s chartering authority. Other disputes are resolved by determination of a review board. Determinations by the chartering authority or review board are conclusive and binding. See tables I.7-3 and I.7-4 for a summary of loss share transactions for 1992 and 1993.

Negative Aspects of Loss Sharing

One of the negative aspects of the loss sharing structure is that it requires the FDIC and the acquirer to take on additional administrative duties and costs in managing the loss sharing assets throughout the life of the agreement. For some acquirers, the added administrative duties and costs may be unacceptable, and they may lose interest in bidding. Generally, the FDIC has considered loss sharing only if the pool of loss sharing assets is of a significant volume, greater than $100 million. Furthermore, many healthier, smaller banks may not have the appropriate experience in working out problem credits. As a result, they may either lose interest in bidding or, if they acquire the assets, they may not have the ability to manage them in the best interests of all involved.

Analysis and Conclusion

The FDIC used loss sharing a total of 16 times to resolve 24 banks that failed between September 1991 and January 1993. Those 24 failed banks had total assets of $41.4 billion, of which approximately $18.5 billion were covered by loss sharing. Loss share transactions were extremely successful in keeping failed bank assets in the banking sector and out of the liquidation mode. Table I.7-5 illustrates that success by comparing the amount of assets passed to acquirers through the 24 loss share transactions to the amount of assets passed in the 175 banks that failed during 1991 and 1992 and were resolved using conventional P&A transactions. The loss share transactions accounted for $41.4 billion in failed bank assets and were able to pass to the acquirers $18.5 billion (45 percent) under loss sharing and another $17.8 billion (43 percent) without loss sharing. As a result, $36.3 billion (88 percent) of failed bank assets were passed to acquirers and only $5.1 billion (12 percent) of those failed bank assets were retained by FDIC for liquidation. The 175 P&A transactions during 1991 and 1992 that did not involve loss sharing accounted for $62.1 billion in failed bank assets and were able to pass

Table I.7-3

Summary of Loss Share Transactions 1992

($ in Millions)

Failed Bank	**Attleboro Pawtucket S.B.***	**First Constitu-tion**	**Howard S.B.**	**Heritage Bank for Savings**	**Eastland S.B.**	**Eastland Bank**	**Meritor S.B.**
Acquirer	New Bedford Institute for Savings	First Federal	First Fidelity	Fleet of MA	Fleet of RI	Fleet of RI	Mellon Bank
Acquisition Date	Aug. 21, 1992	Oct. 2, 1992	Oct. 2, 1992	Dec. 4, 1992	Dec. 11, 1992	Dec. 11, 1992	Dec. 11, 1992
Total Assets at Resolution	$595	$1,580	$3,258	$1,272	$473	$72	$3,579
Beginning Amount of Loss Share Assets	$338	$241	$865	$347	$294	$8	$755
Term: For Shared Losses	3 years	5 years	5 years	5 years	3 years	3 years	5 years
For Shared Recoveries	5 years	7 years	7 years	7 years	5 years	5 years	7 years
Shared Loss Coverage	1-4 residential Commercial†	Commercial	Commercial	Commercial	Commercial	Commercial	Commercial
	ORE‡	ORE	ORE	ORE	ORE	ORE	ORE
	Recoveries plus expenses	Recoveries plus expenses	Recoveries plus expenses	Recoveries plus expenses	Recoveries plus expenses	Recoveries plus expenses	Recoveries plus expenses
	All categories 80%/20%; greater than transition amount: 95%/5%	All categories 80%/20%; greater than transition amount: 95%/5%	All categories 80%/20%; greater than transition amount: 95%/5%	All categories 80%/20%; greater than transition amount: 95%/5%	All categories 80%/20%; greater than transition amount: 95%/5%	All categories 80/%20%; greater than transition amount: 95%/5%	All categories 80%/20%; greater than transition amount: 95%/5%
Shared Recovery Coverage	Percentage same as loss share	Percentage same as loss share	Percentage same as loss share	Percentage same as loss share	Percentage same as loss share	Percentage same as loss share	Percentage same as loss share
Transition Amount	$49.3	$49.2	$130	$53	$38	$2	$60

* S.B.: Savings Bank

† Commercial includes multi-family loans.

‡ ORE: Owned real estate.

Sources: FDIC Division of Resolutions and Receiverships reports.

just $24.3 billion (39 percent) of failed bank assets to the acquirer. As a result, $37.8 billion (61 percent) of those failed bank assets were retained for liquidation by the FDIC.

Even though 122 banks, with total assets of $44.6 billion, failed in 1992, the FDIC, by using loss sharing, was able to halt the skyrocketing growth of assets in liquidation at $43.3 billion at year-end 1992. The FDIC was able to manage the situation by using loss sharing to keep assets out of the liquidation area, as well as by implementing improved asset disposition measures for assets that were in the liquidation phase. (See table I.7-6.)

The loss sharing transactions were less expensive than the P&A transactions without loss sharing. The 24 failed loss share banks had total assets of $41.4 billion and were resolved by the FDIC at a cost of $2.5 billion, or 6.1 percent of assets at the time of resolution. The 175 banks resolved by P&A without loss sharing had $62.1 billion in failed bank assets and were resolved by the FDIC at a cost of $6.5 billion, or 10.4 percent of assets at the time of resolution.

Loss share transactions were less expensive than conventional P&A transactions for large banks (total assets over $500 million), as well as for small banks (total assets under $500 million). The FDIC resolved 16 large banks with loss sharing and another 16 large banks using conventional P&A transactions. The large loss share banks had total assets of $39.2 billion and cost the FDIC $2.1 billion (5.38 percent of assets) to resolve. The large failed banks on which loss share was not used had total assets of $47.1 billion and were resolved at a cost of $4.1 billion (8.66 percent of assets). The FDIC resolved 8 smaller banks with loss sharing and 159 with conventional P&A transactions. The smaller loss share transactions had $2.2 billion in total assets and were resolved at a cost to the FDIC of $200 million (9.55 percent of assets). The 159 conventional P&A transactions had total assets of $15 billion and cost the FDIC $2.4 billion (15.82 percent of assets) to resolve. (See table I.7-7 for a summary of the cost of resolution on P&A transactions in 1991 and 1992.)

The FDIC's projected payments on the loss share assets are less than its original estimate of $1.4 billion. As of December 1997, the FDIC expected to make loss share payments of more than $1 billion, or just 74.3 percent of the amount originally forecast.

By December 1997, the loss sharing period for 21 of the 24 failed banks covered by loss sharing agreements had either been completed or terminated. Less than $310 million of shared loss assets remained, representing less than 2 percent of the beginning book value for loss share assets. The estimated loss and recovery share payments on those remaining assets were included in the above cost calculations.

The loss share transaction has been successful for the FDIC in the past and, should the need arise, is likely to be used in the future.

Table I.7–4

Summary of Loss Share Transactions 1993*

($ in Millions)

Failed Bank:	First City-Dallas First City-Houston	First City-Austin	Missouri Bridge Bank (Merchants Bank) (Metro North State Bank)	New First National Bank of Vermont	CrossLand Fed
Acquirer	Texas Commerce	Frost National Bank	Boatmen's First Nat'l Bank of Kansas City	The Merchants Bank	CrossLand Fed
Acquisition Date	Feb. 13, 1993	Feb. 13, 1993	April 23, 1993	June 4, 1993	Aug. 13, 1993
Total Assets at Resolution	$4,901	$347	$2,846	$225	$7,234
Beginning Amount of Loss Share Assets	$1,694	$58	$953	$160	$2,820
Term: For Shared Losses	5 years	5 years	5 years	3 years	5 years
For Shared Recoveries	7 years	7 years	7 years	5 years	8 years
Shared Loss Coverage	Commercial†	Commercial	Commercial	1-4 residential Agriculture Commercial	Commercial
	ORE‡	ORE	ORE	ORE	ORE
	Recoveries plus expenses	Recoveries plus expenses	Recoveries plus expenses	Recoveries plus expenses	Recoveries plus expenses
	All categories 80%/20%; greater than transition amount: 95%/5%	All categories 80%/20%; greater than transition amount: 95%/5%	All categories 80%/20%; greater than transition amount: 95%/5%	All categories 80%/20%; greater than transition amount: 95%/5%	All categories 80%/20%; after net charge-offs exceed $179
Shared Recovery Coverage	Percentage same as loss share	Percentage same as loss share	Percentage same as loss share	Percentage same as loss share	Percentage same as loss share
Transition Amount	$81.2	$5.3	$92	$41	Not applicable

* All of the banks in this table (excluding New First National Bank of Vermont) were resolutions involving bridge banks that were created when each constituent bank failed in 1992. New First National Bank of Vermont was created in January 1993 following the failure of First National Bank of Vermont. CrossLand Savings was a savings association that failed in January 1992 and was operated in conservatorship as CrossLand FSB. All of the P&A transactions with loss sharing occurred in 1993.

† Commercial includes multi-family loans.

‡ ORE: Owned real estate.

Sources: FDIC Division of Resolutions and Receiverships reports.

Table I.7-5

Analysis of P&A Transactions With and Without Loss Sharing 1991 and 1992

($ in Billions)

	P&A with Loss Sharing*		P&A without Loss Sharing	
Number of Failed Banks	24		175	
	Total Assets	Percentage	Total Assets	Percentage
Passed with Loss Sharing	$18.5	45	$0	0
Passed without Loss Sharing	17.8	43	24.3	39
Total Assets Passed	36.3	88	24.3	39
Assets Retained by the FDIC	5.1	12	37.8	61
Total Failed Bank Assets	**$41.4**	**100**	**$62.1**	**100**

* Includes the January 1993 resolution of First National Bank of Vermont with assets totaling $225 million.

Sources: FDIC Division of Research and Statistics and FDIC annual reports.

Table I.7-6

Book Value of Assets in FDIC Liquidation at Year End

($ in Billions)

Year	Asset Balance
1990	$30.9
1991	43.3
1992	43.3
1993	28.0

Sources: FDIC Division of Research and Statistics and FDIC annual reports.

Table I.7-7

FDIC's Cost of Resolution as a Percentage of Assets of P&A Transactions for Failing Banks 1991–1992

Failed Banks with Total Assets over $500 million

	Average Cost of Resolution (%)	Median Cost of Resolution (%)
With Loss Sharing	5.38	7.77
Without Loss Sharing	8.66	12.21

Failed Banks with Total Assets under $500 million

	Average Cost of Resolution (%)	Median Cost of Resolution (%)
With Loss Sharing	9.55	6.06
Without Loss Sharing	15.82	17.10

Sources: FDIC Division of Research and Statistics and FDIC annual reports.

Table I.7-8

FDIC Loss Share Transactions 1991–1994

($ in Millions)

Transaction Date	Failed Bank*	Location	Total Assets	Resolution Costs	Resolution Cost as Percentage of Total Assets
09/19/91	Southeast Bank, N.A†	Miami, FL	$10,478	$0	0.00
10/10/91	New Dartmouth Bank	Manchester, NH	2,268	571	25.19
10/10/91	First New Hampshire	Concord, NH	2,109	319	15.14
11/14/91	Connecticut Savings Bank	New Haven, CT	1,047	207	19.77
08/21/92	Attleboro Pawtucket S.B.	Pawtucket, RI	595	32	5.41
10/02/92	First Constitution Bank	New Haven, CT	1,580	127	8.01
10/02/92	The Howard Savings Bank	Livingston, NJ	3,258	87	2.67

Table I.7-8

FDIC Loss Share Transactions
1991–1994
($ in Millions)
Continued

Transaction Date	Failed Bank*	Location	Total Assets	Resolution Costs	Resolution Cost as Percentage of Total Assets
12/04/92	Heritage Bank for Savings	Holyoke, MA	$1,272	$21	1.70
12/11/92	Eastland Savings Bank‡	Woonsocket, RI	545	17	3.30
12/11/92	Meritor Savings Bank	Philadelphia, PA	3,579	0	0.00
02/13/93	First City, Texas-Austin, N.A.	Austin, TX	347	0	0.00
02/13/93	First City, Texas-Dallas	Dallas, TX	1,325	0	0.00
02/13/93	First City, Texas-Houston, N.A.	Houston, TX	3,576	0	0.00
04/23/93	Missouri Bridge Bank, N.A.	Kansas City, MO	1,911	356	18.62
06/04/93	First National Bank of Vermont	Bradford, VT	225	34	14.97
08/12/93	CrossLand Savings, FSB	Brooklyn, NY	7,269	740	10.18
Totals/Average			**$41,384**	**$2,511**	**6.07**

* The banks listed here are the failed banks or the resulting bridge bank from a previous resolution, however, it is the acquirer that enters into the loss sharing transaction with the FDIC.

† Represents loss sharing agreements for two banks: Southeast Bank, N.A., and Southeast Bank of West Florida.

‡ Represents loss sharing agreements for two banks: Eastland Savings Bank and Eastland Bank.

Source: FDIC Division of Research and Statistics.