

Consumer Finance Monitor (Season 6, Episode 13): How a Former FDIC Chairman is Reacting to the Silicon Bank Valley Failure, A Discussion with Special Guest Bill Isaac, Chairman, Secura/Isaac Group, and FDIC Chairman from 1981-1985

Speakers: Alan Kaplinsky, Scott Coleman and Bill Isaac

Alan Kaplinsky:

Welcome to our award-winning Consumer Finance Monitor podcast, where we explore important new developments in the world of consumer finance and what they mean for your business, your customers and the industry. This is a weekly show brought to you by the Consumer Financial Services Group at the Ballard Spahr law firm. I'm your host, Alan Kaplinsky, the former practice group leader for 25 years, and now Senior Council of the Consumer Financial Services Group at Ballard Spahr. And I'm very pleased to be moderating today's program. For those of you who want even more information, don't forget about our blog, consumerfinancemonitor.com, hosted the blog since July 21st 2011, the very same day that the CFPB became operational. So there's a lot of relevant industry content there. We also regularly host some webinars on subjects of interest to those in the industry. So to subscribe to our blog or to get on the list for our webinars, please visit us at ballardspahr.com.

And if you like our podcast today, let us know about it. Leave us a review on Apple Podcast, Google or whatever platform you use to access your podcasts. Also, please let us know if you have any ideas for other topics that we should consider covering or other speakers that we should consider as guests on our show. Well, let me give you a little bit of a flavor for what we're going to do today. Ordinarily, we cover topics that are purely consumer finance related. However, there has been so much tumble in the banking industry in the last two to three weeks. It's certainly a crisis of confidence, is the first words that come to my mind. And I decided we needed to cover this topic. And in thinking about the best way to cover it, I figured there was nobody better than our very special guest today, an old friend of mine who haven't talked to in a while before we decided to do this podcast.

But let me introduce to all of you, Bill Isaac. Bill is Chairman of Secura/Isaac Group, a global advisory firm serving the financial services industry. He has had an unparalleled career in the financial industry and public service, spanning over 50 years. He served as chairman of the Federal Deposit Insurance Corporation from 1978 through 1985, working very hard to maintain stability during the banking and thrift crisis of the 1980s when over 3000 banks and thrifts failed. He has written books about his time as FDIC chairman. He's also, after leaving a public service, he's served as chairman of Fifth Third Bancorp for a while and has... He is now back in the consulting business and has his own firm, Secura/Isaac Group. So Bill, very warm welcome to you.

Bill Isaac:

Thanks, Alan. Good to be with you again.

Alan Kaplinsky:

And let me introduce my colleagues, Scott Coleman, who is going to join us on our podcast today. For over 30 years, Scott has represented banks and bank holding companies in connections with mergers and acquisitions, non-bank expansion opportunities and capital reason. Scott has significant experience in a wide range of bank regulatory matters, including Regs O, WY, interstate banking and branching, lending limits, Basel III and regulatory capital guidelines. He also often represents bank stock lenders and subordinated debt purchasers. He's the Co-Leader of Ballard Spahr's newly formed task force that is

monitoring developments and providing strategic council to clients in the wake of the Silicon Valley Bank closure. So a warm welcome to you as well, Scott.

Scott Coleman:

Thank you, Alan. I'm excited to join you and to talk to Bill about these issues.

Alan Kaplinsky:

All right. So I'm going to start Bill with a softball question and we'll build momentum as we go along. But let me start with this, the failure of Silicon Valley Bank was a liquidity-based failure. The bank had insufficient liquid assets to meet depositor demands. It appears that it had a terrible mismatch of its demand deposits against investment securities of longer duration. This is a scenario, am I right, Bill, that this isn't anything new? We've seen it before.

Bill Isaac:

That's true, Alan. And there, really, are very few things that are new in banking. We pretend like there are but it's a lot of other things that we've done for a long time, sometimes using different names.

Alan Kaplinsky:

I think you had mentioned to me First Pennsylvania Bank was in a good example.

Bill Isaac:

Perfect example, I was at the FDIC beginning in 1978. Paul Volcker came to the Fed in 1979 and First Pennsylvania hit us in 1979. So we got to enjoy that episode together, episode that is remarkably similar to what went on at Silicon Valley Bank. First Pennsylvania bought a bunch of long treasury bonds and at fixed rates. I don't know why, because it was pretty clear we were in a high inflation environment, and that Paul Volcker was being brought in to raise rates. Why you would want to load up on a bunch of long treasuries during that low rate long treasuries, I don't know. But they did.

And they met their death. We had to get rid of all the board members and all the... And as a senior management as happened recently at Silicon Valley Bank, and we had to give it some financial assistance. And eventually, we put it away, it was gone. And the oldest national bank charter in the United States, it was a wonderful bank and it disappeared because of some very bad decisions they made. And I see a big parallel between that and Silicon Valley Bank.

Alan Kaplinsky:

And I guess there is also somewhat of a parallel between what happened in the S&L Crisis where you had savings and loans that had on their books 30-year fixed interest rate mortgages. And on the deposit side, it was all short term and rates went up, they got killed.

Bill Isaac:

That's true, Alan. And also the mutual savings bank industry, which the FDIC oversaw, the same thing happened there. But there, there was more reason for that because they were pretty much required to do it by law. Their asset mix was basically long-term mortgages. And at that time, mortgages were fixed rates. We didn't have the variable rate mortgages, so they were loaded up with a bunch of long assets at relatively low rates that they couldn't do anything about. That was their line of business that the government said they should be dedicated to. And they didn't allow them a lot of freedom to do something else. And then they were funded by deposits from people on the street. And those deposits tend to be short, and they also were at fixed rates, but what happened was, when the interest rates in the marketplace went up, the value of the mortgages went down because as rates go up, a fixed rate mortgage is worth less because it's not going up.

And the deposit costs for the S&L went way up, so they were in a squeeze. Their income was fixed and their costs were going up, while the rates in the marketplace were going up. So it was a bad situation for the S&Ls and we had no choice, but they

mostly had to fail. And now we tried to react as quickly as possible and we got rid of interest rate controls and tried to deregulate as quickly as we could. But it was a very, very difficult situation for the S&Ls. And most of them went out of business. I think we lost, probably at least a couple thousand of them.

And taxpayers had to come in and subsidize the recovery efforts with \$150 billion taxpayer funds that they put up. And of course, the FDIC members, which now included some of the S&Ls because the old S&L agency went out of business, so the FDIC took it over. And the FDIC members, including the S&Ls that survived, and the banks all returned that \$150 billion to the treasury. So we really didn't have any taxpayer money in it for the long term.

Alan Kaplinsky:

Okay. So following the 07-08 financial crisis, which is the only other one we haven't talked about yet, you were critical of the sloganeering by politicians calling for the end of too-big-to-fail. Even president and former officials of the Fed and other agencies discussed steps needed to end too-big-to-fail, yet the decision to approve a systemic risk exception for Silicon Valley Bank would appear to be an expansion of the doctrine to smaller regional banks. And was that, in your opinion, the right decision to make?

Bill Isaac:

It's hard to say when you're sitting on the outside of the FDIC or the treasury who's ever dealing with it, and second guess, Sam, when you don't have all the facts they have. With that caveat, I would say, I think it was the wrong decision. And I think they had a much better decision they could have made, and I wish they had. Basically, first of all, when I was dealing with the S&L and the bank problems, we had a \$100,000 deposit insurance limit. It was originally 40. And then the treasury, I mean, the Congress raised it to 100, at the behest of the S&Ls. And so we had a \$100,000 limit. And it was really difficult to pay off everything that needed to be paid off at that low level. I mean, people were going to be taking a pretty big loss, some people, because there were a number of people who had more than \$100,000 in the bank.

So they raised us to 250. 250 is a very high limit. Keep in mind, the FDIC was supposed to be created to protect small depositors. We were concerned about the runs of the little depositors, smaller depositors. And so we weren't supposed to take care of all the fat cats that were in the banking system. We were supposed to take care of the public. And so anyway, what I would've done, because we're in a different world today than we were in the depression, and in a somewhat different world than we were in when I was at the FDIC, I think we've learned some new ways of doing things and we should have used those new ways of doing things. When I was at the FDIC, we came up with a technique called modified payoff. If when you're paying off the insured depositors, that's a payoff, that's [inaudible 00:14:02] insurance payoff.

We modified it and we said, we'll take care of the consumers and their \$100,000 limit, that's a payoff. And we'll also pay off the depositors who have more than that up to the 100,000 or 250 today. But in addition, we came up with another technique to alleviate some of the factors that make deposit payoffs so difficult, and that is, we tried to get as much money as we could, as quickly as we could to the large depositors, those over 100,000. And so we estimated how much we would likely almost certainly recover, and I think in one case that I recall, we made an estimate that we could recover 80% of all the assets overtime. So we sent checks to all the depositors, insured and uninsured for the 100,000, that'd be 250,000 today. And then we sent the folks who were over 100,000 or 250,000 today, we sent them 80% of their money right away.

And if the FDIC would have trouble coming up with that much money that fast, we would send them a certificate, receivership certificate, which they could take to the Fed and the Fed would give them the money. So we got them a lot of money right away. And that alleviated so much of the pain that could have come from a bank failure. Why they didn't do that today, I don't know. I think it was a mistake not to do it. I don't think we should be giving people who have 10 or \$20 million in a bank all their money. I think they should have to wait for some of it. They're not in hardship.

Alan Kaplinsky:

Don't you think that the reason behind it wasn't so much that they felt sorry for some of these big joint ventures and private equity firms that had millions and millions on a deposit, but that they were afraid that if they didn't do something like this, that this crisis that began with silicon was going to spread rapidly to other banks? And of course, it was too late for Signature Bank,

but then we saw all these banks in the Midwest like PacWest and other banks, where there were runs occurring there. And at least I believe that they did it because they wanted to stop the bleeding or they wanted to stop the bank runs.

Bill Isaac:

That's always the excuse. Nobody wants to test it, but unless you do that, people are never going to doubt that they have full insurance coverage and you've destroyed our free enterprise banking system. If nobody takes losses, even the richest and smartest people in the world had money in there and they knew better. They knew this bank was mismatched on interest rates, and they should have been willing... In fact, I was on the phone yesterday speaking with a group and there was a woman on the call who was asking me about this and she said... I don't remember what her company was, I think it was a teacher's pension fund or something. And I told her about the modified payoff, that they could have gotten 80% of their money right away and maybe the rest of it later if we collected it all. And she said, I think that would've been fair.

We were really worried we were going to have to wait for a bunch of it, anything over the insurance limit, and we wouldn't have liked that at all. But if you could have gotten us 80% of our money right away with the hope of getting some later, I think that would've been a fair resolution. And I do too. But if we don't get people used to that, it's never going to be that way, and we're either going to give small banks a lot of problems if we don't bail their depositors out all the time, and make it unfair, so the money's going to go to the big banks more than the small banks. So we've got to have a system that we can use on everybody and we can't pay everybody a hundred cents in a dollar if we are going to have a free enterprise dynamic banking system that the government doesn't have to control completely.

Alan Kaplinsky:

I have a slightly different point of view, but we'll get to that a little bit later because I've got a lot of other questions I want to ask you. In addition to the approval by bank regulators of the systemic risk exception for Silicon Valley Bank and then later Signature Bank, the Fed established the so-called Bank Term Funding Program, offering loans of up to one year in duration to banks, savings associations, credit unions and other eligible depository institutions, pledging US Treasury Agency debt and mortgage backed securities and other qualifying assets as collateral at par or face value, not at market value. Is there anything more? I mean, you've talked already about you would've preferred to see the depositors over 250,000 be paid in installments with a large amount paid upfront and then maybe a tail distribution at the end if there is enough proceeds that are generated from the sale of the bank. But first of all, what you think of that funding program? Did you think that was a good idea?

Bill Isaac:

I think it was a pretty good idea, and that's what the Fed is for. The Fed is to provide liquidity. And so they could take some losses on that, but hopefully not. Hopefully, people can hang on for a while and the interest rates will come back to a place where the market value of those assets increases. But the Fed is there to help in liquidity situations and I think they've done a good job over the years. So I don't have an issue with that. I have an idea that I think could be better, at least in a different way.

When I was leaving the FDIC, before I left, I had the FDIC staff do a book, deposit insurance in a deregulated environment or something like that. And they prepared to study of all the things we would change having learned when we went from the highly regulated rate controlled, everything was controlled from the depression, until around the '70s. And then we started to go to a market system and it drove the S&Ls out of business, the savings banks out of business and so forth. And so I had the staff write up a study of what we would change in the deposit insurance system because the deposit insurance system was created for a highly regulated environment and it was done that way on purpose because we didn't want to take the risk of the depositors' losses and put that on the government when we were going to be in a market oriented economy.

So we put the regulations in place and we couldn't put the regulations in place because inflation, excessive inflation was killing the participants in the marketplace. So one of the ideas they came up with, and I think it was probably the best of the ideas, and we didn't get it put into legislative language before I left the FDIC, it's still sitting there. Nobody thought to bring it up. But I believe it's absolutely essential when businesses open checking accounts, transaction accounts, checking accounts, at banks, if they are interest-free accounts, so they can't be high risk accounts. They're just ordinary checking accounts.

They don't pay interest. They're to make payroll payments and other kinds of business expenses for consumers and businesses alike. If you have a business checking account that doesn't pay interest, you have full deposit insurance, period. Most of the crises that go on when we're in a situation like today or in 2008 or in 1980 or 1978, whenever that one started, it would eliminate almost all these contagion problems that we have. And it doesn't really cost anything because you're giving people back their free money.

Alan Kaplinsky:

Yeah, I mean, I have no idea what the deposit mix was like at Silicon Valley Bank, how much of it was DDA accounts, how much of the DDA accounts were bearing interest, how many were non-interest bearing. At least I haven't seen that information yet. But an interesting-

Bill Isaac:

I haven't either, I haven't either. But I know that a big problem that concerned everybody there and in the other transactions lately is how do we make payroll? How do we make sure our people, our workers are getting paid? We have this money sitting in your bank and it's for payroll purposes, you won't give it back. And that's not fair, it's not fair to anybody. And a deposit insurance was supposed to help ordinary people, not fat cats. And the people who are getting these payroll checks are ordinary people for the most part, and they ought to be paid those monies. So I think that's a very important change. And if we made that change, I think a lot of the problems we've been dealing with today and in previous years would never have happened.

Alan Kaplinsky:

Yeah. Do you think, I mean, the people who have DDA accounts and where they're getting paid interest right now, that given the choice, if you said to them, we also have a DDA account, we don't pay any interest on it, but in the event we fail, which we don't think is going to happen, of course, but in the event we fail, even if it's over 250,000, you're going to get everything back right away.

Bill Isaac:

It could be 10 million. I don't care how much it is. I mean, some of my colleagues would prefer to see some limit on it. I don't much care because it's not hot money, it's not causing trouble. It's there not to get a big return. It's there to be safe.

Alan Kaplinsky:

So Scott, you've got a question, I know, for Bill about a book that you read that Bill authored.

Scott Coleman:

I do. Bill, I just actually finished rereading your book, "Senseless Panic: How Washington Failed America," talking about the financial crisis and the events afterwards. And I noted that in your book, you were fairly critical of FASB's mark-to-market accounting and the application of those accounting rules to financial institutions. Are you still concerned about mark-to-market accounting today? And isn't that really part of the story here at Silicon Valley Bank? They had gains, well, actually, they had other comprehensive income losses in their investment portfolio. Historically, those were not considered in measuring regulatory capital for financial institutions until Basel III changed the rule for advanced approaches, larger financial institutions where, in fact, the OCI losses do have a capital impact. Do you have a concern that mark-to-market accounting still creates that fear out there that can cause a liquidity failure like this?

Bill Isaac:

Scott, let me go into the background because that's important to what I'm talking about in terms of mark-to-market accounting. We had mark-to-market accounting in the 1930s, in the Great Depression, and all of the bank examiners and the federal officials and the accountants and everybody, the treasury, they were saying, this is a terrible problem because in the Great Depression, the markets crashed, and banks were having to write down all of their assets to their current value. And that

defeated the whole purpose of what a bank's all about. A bank is supposed to be intermediating between the bank and its borrowers. People come to the bank and they give them their money and the bank pays interest on it, and then the bank takes that money and loans it to people who need it for housing or maybe businesses, for their operations.

And the lending that they do is always higher than they pay for the deposits. And that probably means, and it's also usually longer duration than the deposits. That's the purpose of a bank, is to intermediate, to bring those parties together, the consumers who have the money and want a return on it, and the borrowers who need the money and are willing to pay a higher rate on it. And the consumers don't want to give it for a long time, usually. They want to have it available, and the borrower, the business needs to use it in its operation, it needs to build a factory. How do you build a factory and then give it back to the depositors whenever they want it? You can't do that. And so FASB, the Financial Accounting Standards Board in the US, which is a terrible organization, and I say that purposely, I'm not exaggerating.

It's run by the accounting industry and it shouldn't be, it should be run by the government, and it should be run by the bank regulators quite frankly because they actually know what is supposed to go on in the banking industry. Anyway, they, and the SEC, don't like this system that the banks have for accounting, which is absolutely essential. But anyway, we're back into depression, that President Roosevelt and all the people couldn't figure out how to get the economy going again. And somebody had the bright idea, why don't we get rid of this mark-to-market accounting thing because nobody wants to lend money if they have to market to market all the time. It's scary. And so in their wisdom, the treasury, the President, I don't know if the Congress was involved or not, but they all change the rules, and banks don't have to do mark-to-market accounting.

They book the loans that they make at the time and the investments they make, they book them and they hold them at carrying value, whatever they paid for them, unless there's a permanent impairment, not just a market thing, but a permanent impairment. So somebody went broke, they're never going to pay it back, so you have to write it off. But if it's just the market movements, you don't worry about it. And what you try to do then, you manage your bank in a way so that those market movements are not deadly. You don't do what Silicon Valley Bank did, where they bought a whole bunch of long, really long stuff, way out of proportion to their balance sheet and it was at low fixed rates. And so they really put themselves in a very difficult situation and they were required to write it off and they should have and they went broke, and they should have because they made some bad moves.

But as long as you're managing this book, you're hedging and doing things to keep it from going down excessively in value, your assets, you can ride with those market movements. The SEC and the FASB did a terrible thing in trying to change that. And I testified against it, I argued against it and so forth. I wasn't chairman then, it was after I was chairman. And so the Congress finally came in, held hearings. I testified alongside FASB and the SEC, on the other side of the fence, of course.

They came up with a somewhat of a compromise. I wouldn't have done their rule at all. I thought we were doing just fine since Franklin Roosevelt and the folks, the first SEC all agreed on this, way back in 1938. They did just fine. Why did they change it? I don't know. Some college professor probably had a wild idea, but they should not have changed it and they should go back to the way it was, or most of the way back, but not as far back as we should be. You probably didn't expect that heated or long of an answer, but I do feel very strongly about the issue.

Alan Kaplinsky:

Yeah, no, thanks, Bill. So Bill, Silicon Valley Bank failed, Signature Bank failed, there are concerns about some other banks that don't look exactly like Signature or Silicon Valley Bank, but have a lot of uninsured deposits and have a very negative interest rate gap, do you think that, are we done yet? Is this bank crisis over or do you expect this to continue on for some time with additional bank failures occurring?

Bill Isaac:

I'm not a psychic and I'm not sure I could answer that question, but I hope that the worst of it is behind us. But I've been around this industry long enough to know that if I make that statement, I'm being silly if I overstate it, because we never know what's going to pop up. I would tell you that I believe that we have the ability in this country, our government has the ability and the banking system has the ability to overcome these things and not let them bring us down. It'd be painful and people turn on all their TVs and watch their screens and worry that they're going to lose all their savings and so forth. It hasn't

happened yet since the 1930s, and we survived the '30s, by the way. But it was pretty severe in the 1980s, late '70s and '80s when I was chairman, far more severe than it has either one of these more recent episodes, 2008, 2009, that wasn't as severe as the '80s and this one's not as severe as the '80s.

We survived them. And we can be creative, there's things we can do if we have to. And what you're trying to do is as little as you have to. You don't want it to get out of control. And so you will do what it takes to not get totally out of control. And I experienced that in the '80s. I mean, Paul Volcker and I were talking all the time trying to figure out what was going on, what did we need to do to control it. One of the biggest challenges we had was Continental Illinois. And people say that these banks today are the second and third largest or something like that, in history. They are in terms of the size of the number, but they are not in terms of their size and relationship to the economy and the banking system. The banking system today has somewhere around 20, is it 28 trillion? Or some very large amount of trillions of dollars.

The largest bank in the United States, in 1984, when we were dealing with Continental Illinois, it was 40 billion, Continental was. That doesn't sound like very much today, you would say, that's just a community bank. But at the time, it was by far the... Well, it was a top seven bank. It was the 7th largest bank in the country. Citibank, the largest at that time, was a hundred billion. So it was roughly half the size of the largest bank in the country. And so measuring these things in terms of their asset size doesn't make any sense because of inflation. We have trillions and trillions of dollars in our banking system today because we've inflated our balance sheets so much because we've overspent. We've got \$40 trillion of debt in this country owned by the government, I mean, owed by the government. The Federal Reserve owes 9 trillion.

It was 800 billion when I was chairman of the FDIC. 800 billion versus \$9 trillion today. And the deficit in the economy, the federal deficit was 5.5 trillion when Clinton left office 20 years ago, 5.5 trillion. Today, it's over 31 trillion with no end in sight. It's growing out of control because we have a Congress that is absolutely irresponsible, and we have an administration, or administration's plural. We've been doing this for 20 years. Bush, Obama, Trump and Biden, every one of them, and their congresses, have taken us from a total of, let's say, \$6.5 trillion, if you throw in the Fed money, in the year 2000, to \$40 trillion today. How do you do that and sleep at night? How do you look at your grandkids and say, oh, you're going to have a great life? There's no end in sight if we don't get this under control.

And so it really falls on the Congress and the administration to fix this problem. The problem is not anything that's going on at Silicon Valley Bank. That's a piece of the puzzle. But the problem is that Congress is spending massive amounts of money that it doesn't have. It's borrowing it, and the Fed is putting out massive amounts of money that it's printing and that creates inflation. And inflation robs from the poor. The people who don't have a lot of income get killed by inflation. And it robs the people who are on fixed incomes, social security, the retirees, those are the people that are getting hurt. Why don't these people in Congress and in the White House start thinking about our country and our future, our children and our grandchildren? And they're not, and I'm really upset about it. I really am. I'm not making this up. I'm not running for office, I'm 80 years old.

Alan Kaplinsky:

And I wonder, when does it ever end?

Bill Isaac:

It doesn't until we, voters, make it end. It can be stopped. You don't have to spend this kind of money, you don't have to. And Congress hasn't always done that. Congress used to have a budget committee. The House spends all the money. The Senate just approves. The House is the one that says, we're going to spend all the money and the Fed gets to spend money. But the House used to have a system where there was a budget committee that was in control of all the budgets. I mean, they approved anything that went to the Senate, the budget committee did, and they could jig it around and increase it, decrease it and so forth. Now, we have, I don't know, 12, 15 budget committees, each of whom does its own budget and the budget committee can't stop them from doing it.

We've really got to fix this. This is a number one priority in this country because we can't have a military if we can't pay for it and where are we going to be without a military in this world? We can't take care of people who need it in this country, poverty programs and the like if we don't have money. We can't keep on spending money we don't have. Eventually, nobody's going to loan us money and all of these programs are going to go away. And that's not going to hurt me, I'll be gone. It's not

going to hurt you guys, but it is going to hurt a lot of people, millions, millions and millions of people. I hate to think that I left this world without doing something to try to stop that from happening. I really feel strongly about it.

Alan Kaplinsky:

Yeah. Scott, I want to ask you, you do a lot of work for community banks in the Midwest. I know you've got a lot of banks that you represent. I'm sure you've been talking to some of them in the last couple weeks. Are they feeling anything out of this banking crisis that appears to be affecting the larger regional banks? And I've heard that when you read about the crisis, they do mention small banks being potentially affected by it and real concern they are. But I'm wondering what you're hearing when you talk to your clients.

Scott Coleman:

I've talked to a lot of clients in the last two weeks, and while the news of the failures was sobering, they aren't seeing a lot of immediate impact, and in fact, a few of them may have reached out to their client base or to some of their large depositors. But by and large, the clients I've talked to have said that they have not seen any deposits leave their community banks. They have not heard a lot of calls from customers. And in fact, they've seen, in some cases, an influx of deposits from the larger regional banks, and whether that makes sense or not, we can debate because they also have the same issues of uninsured deposits. And they're probably not in a position where the regulators are going to determine them to be systemically significant and give them a risk exception.

But by and large, no. Asset quality remains, very good. Capital remains, very good. And they're sobered but still positive about the future. The one thing I will say is, and we will see this happen with the regulators, is several of my clients have gotten calls from their primary regulator asking them more questions about their deposits and about their uninsured deposits and how well they have a handle on it and what they know about the relationship. And those were questions that probably should have been asked all along when the bank regulators were examining liquidity. But they're definitely happening now.

Alan Kaplinsky:

Yeah. I think that one thing that your clients are able to benefit from is that most of them are privately owned or not owned. They don't have publicly traded securities. When you have publicly traded securities, that is a different story, I think, because then you've got potentially short sellers who are trying to take advantage of the overall crisis and they can create a problem because if the shareholders see the prices of their bank stock declining, they panic and the word gets out to depositors and then depositors end up panicking.

Scott Coleman:

Yeah, I think that's true. And I think what we saw with Silicon Valley is there was a lot more focus on their balance sheet early on because it's all public. They can see when they sell the investment portfolio and they post that huge loss and it's magnified, whereas with a privately held bank, it may not be as obvious. Although it's not exactly germane to the question you asked. The one thing I've seen that's interesting in the last couple weeks is I've gotten far more questions from other Ballard business clients about their banking relationships and understanding deposit coverage than we've seen in years. People wanting to understand what the limits mean, how things can be handled if they're in joint accounts, how pass-through coverage works, how sweep accounts work. And that is something that we actually see, is the public is in tune with this right now.

Alan Kaplinsky:

Yeah. So Bill, now I'm going to really put you on the hot seat. All the questions up to now have been very easy.

Bill Isaac:

Alan, what did I ever do to you to deserve to be put on a hot seat?

Alan Kaplinsky:

Let's put aside the mismanagement of Silicon Valley Bank. I think we all agree, it's, you scratch your head and wonder what the hell were they thinking about? I've heard some people say that they were just thinking very short-term because their bonuses were tied to profitability and they were putting things in longer term assets in order to increase the interest rate spread. It's hard for me to believe that, that was the motivation. But my question for you is, where in the hell were the regulators? The Federal Reserve Board, these are both a Silicon Valley Bank, Signature Bank, State-chartered Fed member banks, so not supervised by the FDIC, supervised and examined regularly by the Federal Reserve Board, this problem didn't happen overnight.

It was a problem that really began over a year ago when everybody was predicting that the Fed, there was inflation. First, people thought it was transitory inflation but at some point, Powell said, nope, I was wrong. This is a real problem and we're going to tackle it. I'm assuming they have been talking to Signature Bank during this 14, 15 month period. The regulators look awful here. I mean, I know you're going to say, well, let's give them the benefit of the doubt. We don't know exactly what communication was going on. I'm not going to give them the benefit of doubt. So what do you think about that?

Bill Isaac:

You're starting to sound like a psychic, you're predicting what I'm going to say, and I'm not sure you know what I'm going to say, but first of all, I'm not a Fed basher. I had a very close relationship with Paul Volcker. He didn't always agree on everything but I think he was one of the greatest Americans to ever walk this earth, and I miss him a lot. And I think he did an enormously good job in solving a huge inflationary problem in the 1980s. And we remained friends till the day he died. So I'm not going to be a Fed basher. I will tell you though, that the Fed's policies, there's two things I'm going to talk about, regulation and monetary policy. Let's start with monetary policy. The Fed, I think their monetary policy was all screwed up from about 2008 or 10 to today until Jay Powell finally decided to start raising rates and killing inflation.

They were kidding themselves that there wasn't going to be inflation, that it wasn't real. Everybody was saying that except for Larry Summers, who was, I think... I can't remember. I think he was Obama's treasury secretary, might have been Clinton's. But anyway, Larry Summers has been blowing the whistle, Former Secretary of the Treasury, on inflation for some time. And nobody was listening to him, and that's a shame, he had it right. And if Paul Volcker was still alive, and in fact, I know before he died, he and I had... We visited frequently and he couldn't believe what the Fed was doing in that period before he died. He was really down about it. He spent all that hard work trying to, in a lot of pain for everybody, to kill that inflation in the '80s. And then they undid it all after 2000 with their really bad policies, crazy policies that I couldn't even understand.

I really couldn't. It was a new age monetary policy, I would call it, and not the good old reliable stuff. So monetary policy was bad. Jay Powell, to his great credit, started to correct it and deal with it, and he still is. And I applaud him for that. And we all ought to applaud him instead of fighting him the way we are. And that's my opinion on monetary policy. Let's go to regulatory activities. The California Banking Department, and I'm a consultant and I'm supposed to get along with people, but they did a miserable job at Silicon Valley Bank. It was not regulated properly, as did the San Francisco Fed. They should have gotten on top of it much sooner than they did. I understand that they did get on top of it. Let's say a year ago, they started, they realized this mismatch was there and it was going to be a big problem. Why they didn't move harder and faster, I don't know. Why they didn't think about it earlier, I don't know. But that problem was brewing and the bank regulators were not doing anything about it.

Alan Kaplinsky:

Bill, do you think that the fact that the CEO of Silicon Valley was on the board of directors of the San Francisco Federal Reserve Bank, that, that might be one reason they were hesitant to apply as much pressure as they should have?

Bill Isaac:

It could have been but bank presidents are frequently on fed boards. Sometimes important bank presidents are on fed boards. And I haven't seen it be a big factor. In fact, if the Fed saw a big problem on the bank, whose CEO was on the board of the Fed, they could have asked him to leave, or her, I don't know who the CEO was, but that person could have been asked to

leave or that person could have said, I got a bit of a conflict, I'm going to leave the board. And they should have, so the Fed wouldn't feel awkward in doing his job. He wasn't on the board of the California Banking Department as far as I know. Why weren't they doing their job? And I think that there was just a laxity out there. And you see that from time to time.

You don't usually see it in the Fed, but you did there. I dealt with Continental Illinois and that was a big problem that didn't have to happen. There was a lot of laxity there. And even in the private sector, I think it was Fortune magazine, put Continental Illinois on the cover of their magazine two or three years, Bank of the Year, as it was getting ready to fail. And so people get caught up in this euphoria of the times and they forget about what's important. So I mean, I'm not going to try to condemn people, they're trying to do their job, they're trying to make good decisions. I'm not trying to be critical of them as human beings. I'm just saying that mistakes were made and they ought to own up to them and make sure they don't happen again.

Alan Kaplinsky:

So do you think, as a result of what's happened, I mean, most of the focus has not so much been on the mistakes that the regulators made, although there has... The media is certainly paying attention to that, but the calls from politicians, senators, congressmen, is we've got to do a better job in regulating banks. We need more regulation. Well, how do you react to that?

Bill Isaac:

I'm glad you asked that question because that's the one question that's missing today so far. What should Congress do about this? They should stop doing all the things they usually do, which is they ring their hands and they bring in people and they criticize them and bang them around, and then they pass laws and regulations and more laws and more regulations. And most of those laws are not useful, and in many ways, they're harmful, particularly to smaller banks. It's time for us to sit down and have a behind closed doors. So nobody has to be out there trying to show off for the public. It's time to sit down and talk about what really needs to be done here so we can stop this cycle.

I've been in this business for a little over 50 years. I experienced very serious economic problems in 72 to 74, from 78 or seven through 92, there was a bit of a rough patch in the early 2000s, not too bad. And then this miserable problem that didn't have to happen in 2008, nine and 10, and now again today. It's happening with increasing frequency and it shouldn't. We can be smarter than that, and we're not being. We really can do better and we should really put our heads to it and try to do better.

Alan Kaplinsky:

Yeah. So let's end with, I said earlier in our discussion that I disagreed with you about the issue whether the cap on insurance coverage should be lifted or not. And yeah, I disagree on that because I'm very worried that this contagion will not stop until the Americans, and I'm talking about the fat cats, as well as the little guys for whom insurance coverage was intended, as you point out. We know one thing, if that's lifted, and everybody is covered, that's the end of the banking crisis. Liquidity crisis goes away. And fortunately, we don't have a credit problem right now. And I'm not saying we ought to lift the ceiling permanently and ought to be done as we did back in, I think it was 08, 09, the ceiling was lifted for some period of time. All the other things that we're doing don't resonate with a deposit.

Depositors, I don't think, even the fat cats can't be expected to do appropriate due diligence on every bank that they're putting money into. First of all, not all the information is available to them. Even those that are publicly traded, where you can get 10-Ks and 10-Qs and you can get the financial information, all the supervisory information is not available. That's just between the regulator and the bank. A lot of the institutions are mutually owned and they're all you have to rely upon as you can look, who's going to look at bank call reports? You can't expect that, I don't think of anybody.

Bill Isaac:

I agree with you that sometimes it's appropriate for a limited period of time, and they did that in 2008 or nine, I think, for you to call the timeout and say, everybody, calm down. Roosevelt did it in the 1930s. They called a banking holiday. And instead of calling a banking holiday today, what you would do is you would say, okay, everybody's insured for a while and stop worrying until we get this calmed down. But that should be very temporary. It should rarely happen. And if you keep on trying to

protect people who clearly can protect themselves, don't tell me that somebody that's got \$10 million in a bank doesn't know how to protect themselves. That's just ridiculous. And so the ordinary people can't really figure out a bank, somebody really rich can either figure it out himself or herself, or hire it done.

And so I don't buy that. But when there's a true panic and nobody wants to reason, then you have to call the timeout and you can say, okay, everybody's protected for the next six months or the next year. So we can get you all calmed down. But I would never keep on raising these limits and coming up with more deals like they did where these two banks, Silicon and Signature, all the depositors were protected across the board. That was just wrong. Those banks weren't important enough to cause that. And all two of them weren't important enough. If that were happen across the board, yeah, okay, we may need to calm everybody down because they're losing control of themselves. It's a panic. But that seldom happens. I never had a real panic in the 1980s, even though the problems were very serious.

Alan Kaplinsky:

Yeah. I think the one thing I would just add is, back then, there was no social media. Communications were a lot slower.

Bill Isaac:

We weren't using the telegraph to communicate back then in the '80s, Alan. We had lots of communications, we had TV stations following us wherever we went. You go to Oklahoma City, there'd be a whole bunch of... There'd be 200 reporters and TV cameras and all sorts of things there. And there was the Nightly News, Walter Cronkite, and all these people. Don't tell me there wasn't media back then. It's a little quicker now and a lot less reliable, because there's way too many people in it today that don't know what they're doing and don't speak the truth. They have an agenda. Those are the differences. But the speed of light hasn't changed since the 1980s.

Alan Kaplinsky:

Okay. Well, Bill, let's end on that note. Really want to thank you for taking the time today, and I hope you considered all my questions softballs.

Bill Isaac:

I think this was one of the better interviews I've been through. You guys are terrific.

Alan Kaplinsky:

Maybe my next career ought to be is a talk show host.

Bill Isaac:

Yes, that's right. You can be the new Johnny Carson, to show my age. But anyway.

Alan Kaplinsky:

So thank you very much.

Bill Isaac:

It's been fun and it's been, I hope, interesting to people and I'm glad to do it. So thank you very much.

Alan Kaplinsky:

Also want to thank my colleague, Scott Coleman, who participated today, even though he is on vacation in Germany, and the time difference is quite significant. So Scott, thank you very much for being involved.

Scott Coleman:

It was a pleasure to be here and talk to you both. I really enjoyed it.

Alan Kaplinsky:

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