

Hassenfeld Institute for Public Leadership
at Bryant University

Crisis of Confidence:

Responding to the Rhode Island
Credit Union Debacle

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Melissa S. Prosky, Ph.D.

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Study Questions for the RI Credit Union Crisis Case Study

1. Identify the decision points when state or federal action might have changed the outcomes (for better or worse) of the RI credit union crisis.
2. Who are the primary stakeholders, and what were their concerns?
3. What were the conditions (fiscal, political, etc.) unique to Rhode Island, and what were the conditions that may be common to other states?
4. Identify the issues of ethics, accountability and oversight throughout the case study and evaluate responses by state and federal leaders and authorities.
5. In this pre-internet era, who were the most effective communicators during the crisis, and how did they take advantage of existing communication channels? How could state and federal leaders have communicated more effectively?
6. Identify the issues where the state requested federal assistance and discuss how the federal government responded.
7. Did the actions taken by public leaders ensure that a similar situation would not result in the future?
8. What have you learned about responding to a potential crisis in your jurisdiction?

Cast of Characters

Rhode Island State Government

Executive Branch

Harry Baird- Director, Department of Administration (1991-1994)

R. David Cruise- Chief of Staff to Governor Bruce Sundlun (1991-1993)

Edward DiPrete- Governor (1985-1991)

Richard Gaskill- Executive Director, Depositors Economic Protection Corporation (DEPCO) (1991-1993)

Maurice C. Paradis- Director, Department of Business Regulation

Edward D. Pare, Jr.- Superintendent of Banking for the Rhode Island Department of Business Regulation (1991-1998)

Nicolas Retsinas- Director of Policy for Governor Bruce Sundlun

Robert Stitt- Retired bank lawyer and author of the 1985 report that warned of a potential RISDIC crisis

Bruce Sundlun- Governor (1991-1995)

Tom Vartanian- Partner at Fried, Frank, Harris, Shriver & Jacobson (represented the Governor's office)

Arlene Violet- Attorney General (1985-1987)

Sheldon Whitehouse- Executive Counsel to Governor Bruce Sundlun (1991); Director, Department of Business Regulation (1992-94)

Legislative Branch

John D'Amico- State Senator (R-Cranston)

Frances Gaschen- State Representative (D-Cumberland)

Federal Government

Executive Branch

Stephanie Blucher- Attorney for the Office of Thrift Supervision (OTS)

Nicholas Brady- Secretary of the Treasury (1988-1993)

Richard Breeden- Chairman, Securities and Exchange Commission (SEC) (1989-1993)

Layne Bumgardner- Director, National Credit Union Administration (NCUA) Region I

George H.W. Bush- President of the United States (1989-1993)

John Downey- Deputy Director for Regional Operations, OTS (1990-1995)

Paul Fritts- Executive Director of Supervision and Resolutions, Federal Deposit Insurance Corporation (FDIC)

Kenneth Gideon- Assistant Secretary of the Treasury for tax policy (1989-1992)

Mark Hurley- Special Assistant to Director Timothy Ryan, OTS

Roger Jepsen- Chairman, NCUA (1985-1993)

Shirley Peterson- Commissioner, IRS (1992-1993)

D. Michael Riley- Director of Examination Insurance, NCUA

John Robson- Deputy Undersecretary of the Treasury (1989-1992)

Timothy Ryan- Director, OTS

L. William Seidman- Chairman, FDIC (1985-1991)

Dwight Smith- Deputy Chief Counsel, OTS

John Stone- Director, Division of Supervision for the FDIC Washington office

William Taylor- Chairman, FDIC (1991-1992)

Federal Government

Legislative Branch

John Chafee- Senator (R-RI) (1976-1999)

Christine Ferguson- Counsel and Deputy Chief of Staff to Senator John Chafee (1981-1995)

Henry Gonzalez- Representative (D-TX) (1961-1999) and Chairman of the House Banking Committee (1989-1995)

David Griswold- Chief of Staff to Senator John Chafee

Gerald Kleczka- Representative (D-WI) and Member of the House Banking, Finance, and Urban Affairs Committee (1984-2005)

Ronald Machtley- Representative (R-RI) (1989-1995)

Claiborne Pell- Senator (D-RI) (1961-1997)

Michael Platner- Tax and International Trade Counsel to Senator John Chafee

Jack Reed- Representative (D-RI) (1991-1997)

Ed Quinlan- Press Secretary for Senator John Chafee

Patrick Rogers- Legislative Assistant to Senator John Chafee

Michael Ryan- Rhode Island Director for Senator John Chafee (1986-1994)

Private Financial Institutions

Anthony Aragona- President, East Providence Credit Union

Theodore Barnes- President, Old Stone Bank

Edward Maggiacomo- President, Greater Providence Deposit and Trust

Joseph Mollicone- President of Heritage Loan and Investment Company

Raymond Pezza- Attorney representing the Providence Teachers Credit Union

George Rutland- Chairman and CEO of Northeast Savings Bank

Acronyms

DEPCO- Rhode Island Depositors Economic Protection Corporation

EPCU- East Providence Credit Union

FDIC- Federal Deposit Insurance Corporation

NCUA- National Credit Union Administration

OSB- Old Stone Bank

OTS- Office of Thrift Supervision

RISDIC- Rhode Island Share and Deposit Indemnity Corporation

RTC- Resolution Trust Corporation

Abstract: During the 1991 Rhode Island credit union crisis, officials at all levels of government responded to the situation in different ways. The case study highlights examples of state-federal relations during this difficult period in Rhode Island history. It is not an exhaustive chronicle of all events that occurred during the credit union calamity. Officials across different branches and levels of government collaborated to work with the IRS, secure a federal loan from the U.S. Treasury, conduct financial examinations, and prepare for a major bank merger.

Background

In 1971, the Rhode Island Share and Deposit Indemnity Corporation (RISDIC¹), a private corporation, started providing insurance to Rhode Island credit unions. For years, some member institutions engaged in questionable banking practices. In 1985, then- Rhode Island Attorney General Arlene Violet appointed retired bank lawyer Robert Stitt to complete an investigation of the State's privately insured credit unions. He found the risks associated with private insurance unacceptably high. The report was shared among few individuals, including then- Governor Edward DiPrete and members of his staff. The following year, Senator John D'Amico (R-Cranston) and Representative Francis Gaschen (D-Cumberland) proposed legislation that would have required all of the State's financial institutions to obtain federal insurance, thereby putting RISDIC out of business. Although he supported the bill, Governor

¹ In 1977, the FDIC forced the organization (then called Rhode Island Share and Deposit Insurance Corporation), to change the name in order to avoid confusion about its lack of federal affiliation.

DiPrete chose not to lobby for its passage. The legislature soundly defeated the proposal.² On February 14, 1990, Jefferson Loan and Investment Bank failed, and was taken over by RISDIC due to fraudulent lease contracts. RISDIC subsequently took over Heritage Loan and Investment Company on October 18, 1990. In this case, the losses on the loan portfolio were the chief culprit. Furthermore, Joseph Mollicone, the President of Heritage, fled the State with \$13 million in embezzled funds on November 8, 1990.³

News of instability among the RISDIC member institutions spread, leading to some runs on the institutions, especially among knowledgeable insiders. Institutions quietly submitted applications for federal insurance. On December 19, 1990, Governor-elect Bruce Sundlun was called into a meeting at DiPrete's office. It was then that Sundlun learned the true state of the RISDIC-insured institutions from officials representing the FDIC, National Credit Union Administration (NCUA), and the Federal Reserve Bank of Boston.⁴

In short, the situation was one of desperation.⁵ On December 31, 1990, the RISDIC Board of Directors voted to dissolve itself due to the lack of funds for covering the deposits. As a private corporation, there was no automatic coverage of loss from any governmental body. For the 45 RISDIC institutions, there was no other plan in place.⁶

Declaration of a Bank "Holiday"

On January 1, 1991, the day of his inauguration, Governor Sundlun ordered a bank holiday.⁷ All 45 RISDIC-insured institutions, regardless of financial health, were closed.⁸ This resulted in the immediate freezing of \$1.7 billion in assets. By February 1, 27 of the institutions re-opened with federal insurance. However, these represented a relatively small proportion of the frozen assets. The remaining closed institutions accounted for an estimated \$1.2-\$1.3 billion and represented over 350,000 accounts, a significant incidence for a state with only one million

² Select Commission to Investigate the Failure of RISDIC-Insured Financial Institutions, *Report of the Select Commission to Investigate the Failure of RISDIC-Insured Financial Institutions Phase IV: The Failure of Governmental Oversight* (Providence, RI: The Commission, December 1992).

³ Testimony of Former Governor Bruce Sundlun, of Rhode Island to the Legislature of the State of Washington Concerning the Desirability of Federal Insurance for Credit Unions Operating in the State of Washington, November 30, 1995, Governor Bruce Sundlun Papers, Box 52, Folder 339, University of Rhode Island Special Collections and University Archives, Kingston, RI.

⁴ Bruce Sundlun, "Commentary- Cleaning up the Credit-Union Crisis," *Providence Journal*, November 18, 2001, E10.

⁵ For example, the NCUA found that 97% of the loans (\$301.3 of \$310.4 million) from Marquette Credit Union, based in Woonsocket, should have been classified as substandard, doubtful or loss. See Lawrence Ingrassia and John R. Wilke, "Road to Trouble: How Lax Regulation Threw Rhode Island into Banking Turmoil-- Credit Unions, Deposit Insurer had Ties to Legislators, who Let Abuses Continue-- A Lobby that Always Won," *The Wall Street Journal*, March 6, 1991, A1.

⁶ Rhode Island law required that all depository institutions carry deposit insurance.

⁷ Rhode Island Proclamation of January 1, 1991, Executive Order 91-2.

⁸ This included 35 credit unions, 7 loan and investment companies, and 3 bank and trust companies.

people.⁹ This meant that numerous families were locked out of their funds. That same month, Sundlun signed into law legislation that established the Rhode Island Depositors Economic Protection Corporation (DEPCO). The purpose of DEPCO was to take over the assets of the troubled financial institutions, with the goal of paying back depositors as quickly as possible.¹⁰ It would be not be until June of 1992 that all remaining depositors would have access to the majority of their funds.¹¹

Filing Taxes: A Convoluted Nightmare

One of the most immediate concerns in the aftermath of the bank holiday involved the filing of taxes in 1991 for the previous year. The timing of the state-ordered closing complicated the efforts of residents to file and pay their taxes in an accurate and timely manner. On January 14, the IRS branch for the Providence district issued a pamphlet that provided clarifications for various scenarios. The subjects discussed related to the issuance of 1099 paperwork, payment of taxes, and retirement accounts.¹²

⁹ Differing estimates were offered concerning the amount of funds frozen and the number of corresponding accounts. Governor Sundlun stated that there were 375,000 accounts representing \$1.2 billion, while Senator John Chafee had the figures of 358,000 accounts reflecting of \$1.3 billion in frozen deposits. See Testimony of Former Governor Bruce Sundlun, of Rhode Island to the Legislature of the State of Washington Concerning the Desirability of Federal Insurance for Credit Unions Operating in the State of Washington, November 30, 1995, Governor Bruce Sundlun Papers, Box 52, Folder 339, University of Rhode Island Special Collections and University Archives, Kingston, RI; Memo from Pat Rogers to Senator John Chafee regarding Financial Institutions Crisis, February 1, 1991, The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 17, Folder 231, University of Rhode Island Special Collections and University Archives, Kingston, RI.

¹⁰ Rhode Island (State). Legislature. General Assembly. *An Act Establishing the Rhode Island Depositors Economic Protection Act* (91-H5102). February 8, 1991. The Act established a special revenue fund for DEPCO consisting of .5% of the existing sales tax, effective July 1, 1991. Beginning February 1, 1992, this amount was increased to .6%. Although the sales tax itself was set to drop from 7% to 6.5% on July 1, 1991, this phase-out never took place due to the ongoing fiscal challenges. In addition, the Act limited borrowing (apart from revenue bond financing) to \$150 million. The February 1992 modification removed the limit.

¹¹ William B. English, "The Decline of Private Deposit Insurance in the United States," *Carnegie-Rochester Conference Series on Public Policy* 38 (1993), 71-72.

¹² Specific questions included: Will the credit unions and banks that were closed on January 1st be required to send out 1099's? What should I do if I don't receive a 1099 INT? Since the interest I received in 1990 is in a frozen account and I do not have access to it, will I be expected to report this when I file my federal tax return? Will I have to pay taxes on interest credited to my frozen account? Will I have to pay interest if my taxes are late since I had no control over the credit unions and banks closing and freezing my account? I retired at the end of 1990 and deposited my distribution from a qualified plan on December 31st. This money is now frozen and I don't think I will have its in time to roll it over within the required 60-day period. What can I do? I was 70 ½ years old last year and should start withdrawing from my IRA. My IRA is frozen and I am not able to do this. Will I have to pay a penalty? I am unable to pay my estimated taxes due on January 15th because my bank account is frozen. What should I do? See

The answers reflected the need to file taxes using the best information available, to estimate when necessary, and pay what was possible. Individuals were reminded that they would have three years to amend their tax returns. The Providence branch contacted the national IRS office for advice about relief for interest on late tax payments. Those receiving a penalty letter would be able to contact the problem resolution office. For recent retirees, the time that those funds were frozen in a financial institution did not count toward the 60-day rollover period. Finally, individuals unable to make IRA withdrawals had the opportunity to provide an explanation on an IRS form.¹³

Negotiating with the IRS

As the crisis dragged on into March, Senator John Chafee (R-RI) contacted Treasury Secretary Nicholas Brady about possible administrative relief for Rhode Island taxpayers. He asked questions about the following scenarios: Individuals unable to make their fourth quarter estimated tax payments for 1990; complications involving IRA rollovers and withdrawals; and the two-year rollover period for individuals who sold their primary residence.¹⁴ Michael Platner, tax and international trade counsel to Senator Chafee, wrote a memo to his boss detailing his efforts to work with the Treasury Department and the IRS on solving problems through administrative procedures.¹⁵ Platner noted that he had been in contact with Legislative Affairs at the Treasury Department over the previous three weeks in order to expedite a response to the Senator's March 14 letter.¹⁶

On April 11, Kenneth Gideon, Assistant Secretary of the Treasury, provided a detailed response to Senator Chafee's letter. He cited relevant sections of the Tax Code in responding to each of the concerns. For example, Section 6654 (e)(3)(A) stated that "the estimated tax penalty shall

"Federal Taxes and The Rhode Island Banking Crisis," January 14, 1991, The Senatorial Papers of John H. Chafee, Series: Subject File, Box 108, Folder 1102, University of Rhode Island Special Collections and University Archives, Kingston, RI.

¹³ "Federal Taxes and The Rhode Island Banking Crisis," January 14, 1991, The Senatorial Papers of John H. Chafee, Series: Subject File, Box 108, Folder 1102, University of Rhode Island Special Collections and University Archives, Kingston, RI.

¹⁴ Letter from Senator John Chafee to Secretary Nicholas F. Brady, March 14, 1991, The Senatorial Papers of John H. Chafee, Series: Subject File, Box 108, Folder 1102, University of Rhode Island Special Collections and University Archives, Kingston, RI.

¹⁵ The memo outlined four areas of concern. First, alleviating penalties and interest for Rhode Islanders that could not make the January 15 estimated tax payment and might not be able to pay the rest of their 1990 tax liability by April 15. Second, relief from the rule that allowed for only one IRA rollover in a 12-month period. Third, relief for those that turned 70 ½ but were unable to take minimum distributions from their IRA. Finally, he mentioned the possible suspension of the two-year period for purchasing a new residence in which to roll-over the gain from the sale of the previous residence.

¹⁶ Memo from Michael Platner to Senator John Chafee regarding Tax Issues Involves in Credit Union Situation, April 4, 1991, The Senatorial Papers of John H. Chafee, Series: Subject File, Box 41, Folder 427, University of Rhode Island Special Collections and University Archives, Kingston, RI.

not be imposed where the Secretary determines that by reason of casualty, disaster, or other unusual circumstances, imposition of the penalty on an individual would be against equity and good conscience.” He restated information from the January Providence IRS publication indicating that taxpayers should pay what was possible and to contact the office in case of a penalty notice. Citing Section 6651 (a)(2), Gideon wrote that penalties for failure to pay the balance of their 1990 federal taxes would not be imposed as long as this was based on reasonable cause and not willful neglect. However, the IRS would not be able to provide relief from interest incurred from underpayment in taxes. The following concern pertained to a prohibition on multiple IRA rollovers. He suggested that DEPCO might request a ruling on the issue.

Gideon next addressed taxpayers unable to take their required minimum IRA distribution. He said that IRS Employee Plans Technical and Actuarial Division planned to make an announcement that the 50% penalty would not apply to recipients with frozen accounts, as long as they withdrew the amounts upon reopening of the institutions.

Finally, the IRS could not provide administrative relief on the two-year residence replacement. According to Section 1034 (a) of the Code, Congress did not authorize the IRS to waive or suspend requirements or “apply a ‘facts and circumstances’ rule in individual cases.” Therefore, even if the taxpayer intended to replace their residence during the time period, the agency could not provide relief.¹⁷

That same day, Senator Chafee provided a news release detailing his communications with the IRS and areas of further work. He optimistically stated, “I believe the IRS has done everything they can within their legal authority to assist the citizens of Rhode Island who have [been] devastated by the credit union crisis.” He reiterated the previous points made about avoiding penalties for underpayment of estimated tax, balance due in April, and minimum IRA distribution requirements. Although the IRS would not be able to provide relief from interest on the underpayment of taxes, Chafee stated that he would propose legislation to provide for abatement given the situation. With respect to IRA rollovers, the IRS permitted only one per year, while DEPCO allowed for three rollovers per year. Chafee stated that he would work with the Governor’s office to develop a formal ruling request from the IRS. Finally, regarding the rollover of gain from the sale of the personal residence, Chafee noted that he would pursue legislation to provide the IRS with authority to provide administrative relief under unusual circumstances.¹⁸

¹⁷ Letter from Kenneth W. Gideon to Senator John Chafee, April 11, 1991, The Senatorial Papers of John H. Chafee, Series: Subject File, Box 108, Folder 1102, University of Rhode Island Special Collections and University Archives, Kingston, RI.

¹⁸ Senator John Chafee Press Release- “IRS to Ease Filing Requirements,” April 11, 1991, The Senatorial Papers of John H. Chafee, Series: Subject File, Box 108, Folder 1102, University of Rhode Island Special Collections and University Archives, Kingston, RI.

The Rhode Island Congressional Delegation Pleads for Federal Support

From the start of the crisis, members of the Rhode Island Congressional delegation proposed numerous bills targeted to assisting their State.¹⁹ Out of these, there was one notable legislative success during the 102nd Congress that sought to help the State end its credit union crisis. On January 3, 1991, Representative Henry Gonzalez (D-TX) introduced H.R. 6- Financial Institutions Safety and Consumer Choice Act of 1991 in the House. Senator Donald Riegle (D-MI) subsequently introduced S. 543— The Federal Deposit Insurance Corporation Improvement Act of 1991 on March 5, 1991. Each bill contained an amendment authorizing the Secretary of the Treasury to provide an emergency loan to Rhode Island, not to exceed \$180 million. Senator John Chafee introduced this amendment on August 1, 1991, while Representatives Jack Reed (D-RI) and Ronald Machtley (R-RI) did the same on October 31, 1991.²⁰

In their speeches to the House, both members implored their colleagues to vote in favor of the amendment. Machtley stated:

“Our State was one of the 13 original colonies. We have been here for a long time. We intend to work our way out of this problem ourselves to pay our depositors the monies which are owed. But we need a Federal guarantee, as Chrysler in New York did, so that we, in fact, can go to the bank and borrow money at a cheaper interest rate. I suppose if there is such a thing as an economic Third World state, perhaps Rhode Island might fall into it. I have constituents come up to me on any given day and tell me problems of tuition monies which are frozen, life savings which are frozen, elderly have actually contemplated suicide because of the crisis...”

Reed added:

“The State has assumed responsibility for this crisis, and has taken the initial necessary steps to return savings to the depositors. However, this crisis is taking place within the context of a devastating regional recession, and the State needs assistance in fulfilling its obligations. The credit union debacle has exacerbated the State’s fiscal crisis. Last year the State faced the highest percentage deficit of any State in the country and balanced its budget through a series of drastic cutbacks and deferments. This fiscal year, the State will face an estimated \$30-\$40 million revenue shortfall and could face a deficit of \$200 million for fiscal year 1993. Between January 1, 1990 and January 1, 1991, Rhode Island lost nearly 10,000 jobs. Today, Rhode Island’s unemployment rate has reached 9.6%. There was a 56% increase in the number of bankruptcies filed between March 1990 and March 1991. In the past two years, Rhode Island has fallen to 48 among the 50 states and

¹⁹ These included bills to increase the rollover period for the principal residences for taxpayers whose assets were frozen in financial institutions, consideration of student aid decisions, and relief for small businesses.

²⁰ Members of the respective chambers approved the amendments on the day of their introduction.

the District of Columbia in job growth. In this unmatched economic situation, it is incumbent that the Federal Government stand behind Rhode Island as it squarely faces these daunting challenges. The hard-working citizens of Rhode Island have never been a burden to the Federal Government. They have paid their dues. They have contributed \$107 million to bail out the Nation's failed thrifts, even though not one penny has been used to bail out a failed Rhode Island thrift. The Federal Government has assisted Chrysler and New York City in their time of need, and the people of Rhode Island are now asking the Government not to turn its back; they are asking for assistance at no cost to the taxpayer which will help the State fulfill its responsibilities..."²¹

Although the House bill ultimately failed, the Senate version passed on November 21, 1991. On November 26, Governor Sundlun contacted Senator Chafee about the status of the loan provision, which at that point was in conference committee. He expressed concerns about the lending requirements, while also expressing appreciation for the work already completed. Sundlun wanted to make certain that DEPCO would have the flexibility to negotiate with the Treasury Department.²² The following day, the conference committee approved the amendment. As Chafee noted, "As a result of the federal guarantee, the State would be able to borrow funding at a significantly lower interest rate than the State would be able to secure absent the guarantee. The State would have some flexibility with regard to collateral requirements. The State would pay an annual fee of one half of 1% of the outstanding loan principal."²³ President George H.W. Bush signed the bill into law on December 19, 1991.²⁴

Federal involvement did not end with the passage of the law. On February 24, 1992, Senator Chafee hosted the first meeting between federal and state officials since the bill signing. That meeting included DEPCO Executive Director Richard Gaskill and senior representatives of the U.S. Treasury Department. As required by the legislation, the loan guarantee had to be made by December 19, 1992. Treasury officials briefed DEPCO about the loan requirements. In the meantime, the State needed to complete an independent evaluation of the quality of assets

²¹ United States Congress, House, *Providing for Consideration of H.R. 6, Financial Institutions Safety and Consumer Choice Act of 1991*, 102nd Cong, 1st Sess, October 31, 1991.

²² Letter from Governor Bruce Sundlun to Senator John Chafee, November 26, 1991, Governor Bruce Sundlun Papers, Box 67, Folder 82, University of Rhode Island Special Collections and University Archives, Kingston, RI.

²³ Senator John Chafee Press Release- "Chafee, Senate-House Conferees Approve Banking Bill with Rhode Island Loan Guarantee Provision," November 27, 1991, The Senatorial Papers of John H. Chafee, Series: Press Releases/Subject File (1977-1999), Box 3, Folder 37, University of Rhode Island Special Collections and University Archives, Kingston, RI.

²⁴ United States Congress, Senate, *S. 543, Federal Deposit Insurance Corporation Improvement Act of 1991*, 102nd Cong, 1st Sess, December 19, 1991.

under DEPCO control.²⁵ On May 14, 1992, Chafee set up a meeting at the Treasury Department involving officials representing the State. At that time, state officials indicated that the loan guarantee option would likely be the mechanism through which the state would repay depositors at the “final four” institutions (Marquette Credit Union, Rhode Island Central Credit Union, Central Credit Union, and Banner Loan and Investment). Follow up meetings occurred throughout May and June to discuss outstanding issues.²⁶ On June 18, Senator Chafee urged the State of Rhode Island and the U.S. Department of the Treasury to structure an agreement between the Federal Financing Bank and DEPCO. He thought it would be the most effective way to get depositors their funds back before the June 30 deadline imposed by DEPCO.²⁷ On June 26, 1992, U.S. Treasury Secretary Nicholas Brady officially signed off on the documentation providing a \$125 million loan from the Federal Financing Bank. This enabled 27,000 depositors the ability to access their funds, 18 months after the banking holiday.²⁸

“Magnitude of Problems” Found in Examinations

In the months leading up to the bank holiday, RISDIC-insured financial institutions became increasingly concerned about the organization’s stability following the costly takeovers of Jefferson Loan and Investment Bank in February 1990 and Heritage Loan and Investment Company in October 1990. Layne Bumgardner, Director of NCUA Region I (based in Albany) first became aware of the problems with RISDIC on November 9, 1990. One week later, he met with NCUA Chairman Roger Jepsen and Director of Examination Insurance D. Michael Riley, along with representatives from the RI Department of Banking, the RI Credit Union League, and the RISDIC-insured credit unions. On that day alone, the NCUA received 17 insurance applications.²⁹ In total, the agency received 33 credit union insurance applications. Over a five-

²⁵ List of Participants: February 24, 1992 Meeting Between The Depositors Economic Protection Corporation (DEPCO) and the United States Department of Treasury, and Questions to be Discussed during February 24, 1992 Meeting between DEPCO and Treasury, February 24, 1992, The Senatorial Papers of John H. Chafee, Series: Press Releases/Subject File (1977-1999), Box 10, Folder 129, University of Rhode Island Special Collections and University Archives, Kingston, RI; Senator John Chafee Press Release- “Chafee Hosts Meeting with DEPCO, U.S. Treasury Officials to Discuss Federal Loan Guarantees for Credit Unions,” February 24, 1992, The Senatorial Papers of John H. Chafee, Series: Press Releases/Subject File (1977-1999), Box 10, Folder 129, University of Rhode Island Special Collections and University Archives, Kingston, RI.

²⁶ Discussion of DEPCO Matters with U.S. Treasury, May 14, 1992, The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 16, Folder 205, University of Rhode Island Special Collections and University Archives, Kingston, RI.

²⁷ Senator John Chafee Press Release- “Chafee Urges State Treasury to Complete Loan Agreement,” June 18, 1992, The Senatorial Papers of John H. Chafee, Series: Press Releases/Subject File (1977-1999), Box 10, Folder 129, University of Rhode Island Special Collections and University Archives, Kingston, RI.

²⁸ Remarks by Senator John H. Chafee Regarding The Federal Loan Guarantee to Rhode Island, June 26, 1992, The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 16, Folder 205, University of Rhode Island Special Collections and University Archives, Kingston, RI.

²⁹ Institutions interested in obtaining federal insurance were required to submit to examination.

week period, NCUA examiners spent over 4,000 hours for on-site reviews across all institutions. The agency dispatched highly experienced personnel to examine the five largest credit unions: Marquette, Davisville, RI Central, East Providence and Columbian. By December 7, 1990, the group had completed enough work to recognize that there was no way the agency could provide insurance absent financial assistance from RISDIC or the State. Five days later, Bumgardner, along with the field examiners and the supervisor responsible for large credit union examinations, briefed the RI Banking Department on their findings. In later testimony before Congress, he stated:

“In all of my years with NCUA, I have never observed the magnitude of the problems exhibited by these credit unions. The officials of these institutions had rolled the dice - and lost. Concentrations of large speculative commercial and residential real estate secured loans abounded. Marquette Credit Union and Rhode Island Central Credit Union each had over 90 percent of their total loans in these types of risky investments.”³⁰

When federal regulators met with Governor-elect Sundlun on December 19, the cost associated with institutional losses was approaching \$500 million. By December 21, the NCUA completed the examinations of all 33 credit unions that had applied for insurance. On January 7, 1991, 22 newly insured credit unions opened without incident, as there were no significant withdrawals or panic. The NCUA dispatched 40 examiners to ensure a smooth transition.

A parallel series of events occurred with respect to RISDIC-insured banks that had applied for FDIC insurance. Paul Fritts, FDIC Executive Director of Supervision and Resolutions, stated that five Rhode Island banks submitted applications in November, 1990. On January 3, 1991, the FDIC Board of Directors denied all of the applications. As was the case with the credit unions, these institutions engaged in risky investment activity, among other issues. All were promptly notified about their denied applications.

Once the Governor declared the bank holiday, financial institutions that had received rejection letters continued their quest to obtain federal insurance.³¹ On January 9, Raymond Pezza, an attorney representing the Providence Teachers Credit Union, contacted Governor Sundlun to let him know that he was able to meet with an NCUA official to discuss the agency's rejection of

³⁰ United States Congress, House, Committee on Banking, Finance and Urban Affairs, Subcommittee on General Oversight and Investigations, Closure of 45 Privately Insured Financial Institutions in Rhode Island, 102nd Cong, 1st Sess, April 17, 1991.

³¹ The chronology of events, submitted for the record as part of the April 17 Congressional hearing also mentioned Sheldon Whitehouse, Executive Counsel to Governor Sundlun, and Maurice Paradis, Director of the RI Department of Business Regulation met all day with NCUA examiners and representatives of credit union applicants on January 8, in an unsuccessful attempt to obtain NCUA insurance. See United States Congress, House, Committee on Banking, Finance and Urban Affairs, Subcommittee on General Oversight and Investigations, Closure of 45 Privately Insured Financial Institutions in Rhode Island, 102nd Cong, 1st Sess, April 17, 1991.

their application for insurance.³² On March 25, Senator Chafee informed NCUA Chairman Roger Jepsen about the severity of the crisis, in advance of the agency's upcoming examination of the East Providence Credit Union (EPCU).³³ EPCU President Anthony Aragona distributed a memo to his credit union's employees regarding communications with the Governor's Office. Apparently, members of the credit union were contacting Sundlun to complain that the Governor was holding up the NCUA examination. Aragona wanted to make it clear that the Governor had been working to move the process along, and that consideration of a potential merger was causing the slowdown.³⁴

During the May 24 Congressional field hearing held in Rhode Island, John Stone, Director of the Division of Supervision for the FDIC Washington office, testified on his agency's roles and provided updates.³⁵ Stone reviewed the seven factors that the FDIC considered when considering deposit insurance applications. These included: financial history and condition, capital structure adequacy, future earnings prospects, general character of the management, convenience of community needs, whether purpose is consistent with statute, and whether its assets are sufficient to meet liabilities. With respect to updates, Stone mentioned that both Union Deposit Loan and Investment Bank and Savers Bank and Trust Company withdrew their second round insurance applications after negotiating the sale of their loan portfolios to pay off depositors. On April 18, heads of the liquidated institutions submitted an application for insurance as a new bank. At the time of the field hearing, the FDIC application was in process. Stone mentioned that the agency had not received any new applications from the Greater Providence Deposit Corporation or Blackstone Valley Loan and Investment Bank. Blackstone Valley was in the process of a depositor payout. The FDIC was in the process of reviewing the application of the Chariho-Exeter Credit Union in preparation for a possible merger with First Bank and Trust. He cautioned that there were significant deficiencies in the application relating to negative capital position and adequacy of management. Finally, Stone mentioned that his staff had met with Governor Sundlun's office on at least four separate occasions to resolve issues. For example, in early May, officials from the FDIC, NCUA, Federal Reserve and the Office of Thrift Supervision (OTS) met with the Congressional delegation and other State

³² Letter from Raymond R. Pezza to Governor Bruce Sundlun, January 9, 1991, Rhode Island Depositors Economic Protection Corporation (DEPCO) records, Box 38, Folder 14, Rhode Island State Archives, 2002-09, Rhode Island Depositors Economic Protection Corporation (DEPCO) records.

³³ Letter from Senator John Chafee to Chairman Roger W. Jepsen, March 25, 1991, The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 17, Folder 224, University of Rhode Island Special Collections and University Archives, Kingston, RI.

³⁴ Memo from Anthony Aragona to East Providence Credit Union Employees, April 8, 1991, Governor Bruce Sundlun Papers, Box 120, Folder 67, University of Rhode Island Special Collections and University Archives, Kingston, RI.

³⁵ John Downey spoke on the same panel about the Old Stone plan.

officials to determine further steps. He maintained that the FDIC remained sympathetic to the State and its citizens in their efforts to resolve the crisis.³⁶

In Search of a Partner

From January through late September of 1991, officials attempted to make a deal in which Old Stone Bank (OSB) would acquire closed Rhode Island financial institutions. Governor Sundlun's earliest proposal would have Old Stone purchase the following six closed institutions: Chariho-Exeter Credit Union, East Providence Credit Union, Columbian Credit Union, Providence Teachers Credit Union, Greater Providence Deposit and Trust, and Blackstone Valley Loan and Investment.³⁷ On January 23, 1991, Senator Chafee held a meeting in his office that included members of the Rhode Island Congressional delegation and FDIC Chairman William Seidman. Chafee requested an expedited (seven day) FDIC evaluation of the closed institutions to be acquired in order to move forward with the Sundlun plan. Seidman responded that such exams would take three to four weeks, not the greatly shortened time period. He wanted to avoid the unnecessary risks associated with merging unhealthy institutions with a healthy FDIC-backed bank. Seidman stated that his first obligation was to the FDIC depositors. Nevertheless, he thought that Sundlun handled the Rhode Island situation well.³⁸

On February 7, OTS Director Timothy Ryan notified Governor Sundlun that his agency would not be able to proceed with the Old Stone transaction on an expedited basis.³⁹ He provided alternative proposals that might be considered in this manner. In response to the letter, Governor Sundlun met on February 15 with Deputy Undersecretary of the Treasury John Robson and OTS Deputy Director for Regional Operations John Downey. During that meeting, Sundlun raised concerns about an open-ended guarantee, fees on performing assets,

³⁶ United States Congress, House, Committee on Banking, Finance and Urban Affairs, Rhode Island Banking Crisis: Field Hearings before the Committee on Banking, Finance and Urban Affairs, 102nd Cong, 1st Sess, May 24, 1991.

³⁷ Memo from Pat Rogers to Senator John Chafee regarding Phone Call to Bill Seidman, January 22, 1991, The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 17, Folder 224, University of Rhode Island Special Collections and University Archives, Kingston, RI.

³⁸ Memo from Pat Rogers to David Griswold, Mike Ryan, Christine Ferguson, and Ed Quinlan regarding Seidman Meeting, January 23, 1991, The Senatorial Papers of John H. Chafee, Series: Subject File, Box 41, Folder 427, University of Rhode Island Special Collections and University Archives, Kingston, RI; Memo from Pat Rogers to Senator John Chafee regarding Follow up with the Governor's Office after Meeting w/Seidman, January 24, 1991, The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 17, Folder 231, University of Rhode Island Special Collections and University Archives, Kingston, RI.

³⁹ Letter from Timothy Ryan to Governor Bruce Sundlun, February 7, 1991, Governor Bruce Sundlun Papers, Box 119, Folder 57, University of Rhode Island Special Collections and University Archives, Kingston, RI.

indemnification, and the cost of due diligence. The three came to agreement on how to proceed on these issues.⁴⁰

On February 28, Senator Claiborne Pell (D-RI) hosted a meeting of the Rhode Island Congressional delegation, along with representatives of the six closed financial institutions, to discuss the Old Stone deal. Lawyers from the firm Fried, Frank represented the Governor's office.⁴¹ Edward Maggiacomo, representing both Greater Providence and Old Stone Bank, said that under the proposal, Old Stone would assume the assets and most liabilities of the six institutions, while the State Investment Commission would invest approximately \$50 million and provide limited guarantees or problem assets. According to him, OTS rejected the proposal because of the depositor haircut and because the State would not provide unlimited guarantees.

Much discussion ensued over what the OTS suggested as an alternative. Requirements on the part of the State included:

- (1) investing an amount equal to 10% of the total liabilities assumed by OSB, (2) providing collateral and a note to make up for any differences between assets purchased and liabilities assumed, (3) providing OSB with an amount to cover any cash flow problems which would arise by virtue of OSB assuming nonperforming assets, (4) providing some credit buffer over and above the previously described protections (5) providing OSB with a management fee for administering the purchased assets and (6) providing additional funds to indemnify OSB for any possible claims that might arise from its role in the transaction.

Maggiacomo expressed that possible resolution of the credit unions through DEPCO would be more costly than the alternative OTS proposal. He emphasized that it was not the six institutions that had failed, but rather their insurer. He, along with the other credit union representatives, asked that OTS exercise flexibility in their actions, keeping all six institutions, rather than dropping one or more. Members of the Congressional delegation asked Tom Vartanian of Fried, Frank how they could help the State resolve this situation. Vartanian responded that he could not make a specific request at that time but would work with the Governor's office to develop a new proposal as quickly as possible. Maggiacomo agreed and that he expected the Congressional delegation to assist with the effort.⁴²

⁴⁰ Memo to File from Nicolas P. Retsinas regarding Old Stone Proposal, February 16, 1991, Governor Bruce Sundlun Papers, Box 119, Folder 57, University of Rhode Island Special Collections and University Archives, Kingston, RI.

⁴¹ Although, having just been hired within the previous week, they were to serve as only an observer of the meeting.

⁴² Synopsis of 2/28/91 Meeting with Rhode Island Congressional Delegation and Six Closed Credit Unions, February 28, 1991, Governor Bruce Sundlun Papers, Box 119, Folder 57, University of Rhode Island Special Collections and University Archives, Kingston, RI.

Following its conclusion, Chafee expressed frustration with the meeting. He cited a lack of coordination between the delegation, Governor's office, and the institutions. Chafee also thought that the meeting was premature given that no new plan had been submitted to OTS. He thought that Rhode Island needed to project unity in the process of putting forth a new plan. Pat Rogers, Chafee's legislative assistant, recorded several notable observations near the end of the meeting. He noticed that the representatives of the other institutions (apart from Greater Providence) expressed dissatisfaction with the Old Stone plan. One said that he did not object to the DEPCO plan. Another felt that Greater Providence was driving the proposal, without consideration of the others. Finally, Rogers wrote: "[Congressman] Machtley expressed anger that the Governor was moving too slowly with the Old Stone plan. He pointed out that the Governor was going to make the delegation out to be the 'fall guys.' Said that no significant action has come about since the delegation met with the Governor at the State House nearly 6 weeks ago. He said he wanted to let the depositors know that it was Sundlun, not the delegation, who is dragging his feet on the Old Stone plan."⁴³

On March 6, OTS Director Timothy Ryan notified Governor Sundlun that the agency was rejecting the latest version of the Old Stone proposal. Fried, Frank had submitted a revised proposal the previous day. His concerns included the timeframe for establishing a final price on the closed institutions' assets, depositor burden on institutional losses, and the method for determining asset value. Ryan urged Sundlun to reconsider the proposal outlined by OTS on February 7 in order to give depositors access to their funds in a timely manner.⁴⁴

Two days later, Treasury Secretary Nicholas Brady visited Rhode Island. His visit included meeting with officials at the Chamber of Commerce and appearing on the TV show "Ten News Conference." Following the visit, Chafee implored him to work with Tim Ryan on the Old Stone plan.⁴⁵ On March 13, Chafee was notified that Old Stone Bank President Ted Barnes asked that he make one final attempt to convince OTS to approve the latest version of the Old Stone plan. Barnes suggested that Chafee try to get him to support a plan in which Rhode Island would receive a \$125 million loan— perhaps from the U.S. Treasury— to cover the costs of collateralization against losses associated with the merger transaction.⁴⁶

⁴³ Memo from Pat Rogers to File regarding Meeting Greater Providence Trust Officials and Others, March 1, 1991 [Mis-dated as February 29, 1991], The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 17, Folder 231, University of Rhode Island Special Collections and University Archives, Kingston, RI.

⁴⁴ Letter from Timothy Ryan to Governor Bruce Sundlun, March 6, 1991, Governor Bruce Sundlun Papers, Box 119, Folder 57, University of Rhode Island Special Collections and University Archives, Kingston, RI.

⁴⁵ Letter from Senator John Chafee to Secretary Nicholas F. Brady, March 13, 1991, The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 17, Folder 231, University of Rhode Island Special Collections and University Archives, Kingston, RI.

⁴⁶ Memo from Pat Rogers to Senator John Chafee regarding Phone Call to OTS Director, Tim Ryan, March 13, 1991, The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 17, Folder 231, University of Rhode Island Special Collections and University Archives, Kingston, RI.

On April 17, the House Subcommittee on General Oversight and Investigations for the Committee on Banking, Finance and Urban Affairs held a hearing on the Rhode Island credit union crisis. One of the issues discussed was the Old Stone proposal. Individuals who provided testimony specifically about the plan included Governor Sundlun and OTS Deputy Director for Regional Operations John Downey. Sundlun testified that the OTS and other federal regulatory agencies were “unreasonably inflexible.” This, despite the State’s offering to invest \$60 million equity on OSB, pay about \$20,000 per day for federal auditors and develop a \$150 million bond issue to assist with the acquisition. He claimed that OTS wanted a 100% guarantee against downside risk, plus \$100 million cash within five weeks. Speaking about the crisis in general, Sundlun stated, “I knew Rhode Island was the smallest of the 50 states, but it was not until I dealt with the federal regulators that I found out that Rhode Island was too small to survive.”

John Downey presented his agency’s perspective on the situation. He noted that the chairman of OSB first contacted the OTS Boston office on January 4 to express interest in acquiring closed institutions. The initial plan called for OSB to acquire 16 institutions with \$1.4 billion in assets, while the State would invest up to \$120 million in state pension funds. Downey recounted the various interactions among bank and agency officials, including the use of OTS and FDIC examiners. OTS and FDIC examiners found that losses ranged up to \$230 million. Downey further stated that on January 6, Governor Sundlun opposed OTS proposals. He expressed that the State’s proposals exposed Old Stone to undue risk. Furthermore, he doubted that DEPCO could provide adequate protection. It should be the State, not federal taxpayers, that should bear the risk of any loss, according to OTS.⁴⁷

Further discussion of the Old Stone plan took place on May 3 during a meeting of the Federal Reserve in Boston. Mark Hurley and Dwight Smith of OTS were in attendance, along with officials from the State and the Congressional delegation. One issue raised in the meeting was whether the State could constitutionally borrow amounts of money in excess of \$50,000. Later that month the Rhode Island Supreme Court was set to issue a ruling. Another issue concerned the dispatching of OTS examiners to the four institutions that were set to merge with Old Stone. OTS did not want to provoke undue assurance among depositors that the plan had been approved. The Governor and Congressional delegation understood that there were no guarantees and welcomed the work of examiners even on a preliminary basis.⁴⁸

⁴⁷ United States Congress, House, Committee on Banking, Finance and Urban Affairs, Subcommittee on General Oversight and Investigations, Closure of 45 Privately Insured Financial Institutions in Rhode Island, 102nd Cong, 1st Sess, April 17, 1991. The Governor’s submitted written testimony contained a summary of each iteration of the Old Stone proposals, his office called one through six from January to April.

⁴⁸ Memo from Pat Rogers to Senator John Chafee regarding Follow-up to Friday’s Meeting at the Federal Reserve, May 6, 1991, The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 17, Folder 231, University of Rhode Island Special Collections and University Archives, Kingston, RI.

A follow-up hearing before the House Committee on Banking, Finance and Urban Affairs took place in Rhode Island on May 24, 1991. By this point, the Old Stone plan was in its seventh iteration, according to the Governor. Under this proposal, Old Stone would acquire eight institutions. The State Investment Commission would make a \$50 million equity investment in Old Stone, depositors would invest \$50 million from their frozen deposits, and DEPCO would contribute \$50 million in cash.

John Downey of OTS once again testified on the issue. He continued to proclaim the proposal unacceptable. He did note, however, that the FDIC and OTS had dispatched examiners to one of the credit unions involved in the proposal: East Providence. Information from the examination would be used to develop an estimate of asset losses in the closed institutions, and help the Governor decide on the next course of action. After questioning by Representative Gerald Kleczka (D-WI), Downey noted that no application had been submitted to OTS by Old Stone regarding any of the closed institutions. In addition, he stated that the number of institutions included in the deal and conditions of the transaction continuously changed, leading to much confusion.⁴⁹ The FDIC and OTS completed their examination of East Providence on May 31. Later that day, Governor Sundlun announced a new transaction involving East Providence Credit Union, reportedly without first consulting federal regulators.⁵⁰

By June, things were looking up for the latest iteration of the Old Stone plan. According to Downey, OTS was prepared to approve OSB's June 6 application to acquire the assets and liability of EPCU, provided that the articulated conditions were fulfilled either prior to or at the time of the transaction. These included transaction costs, guarantee on the assets, indemnification, legal opinions from the RI Supreme Court and Attorney General, and line of liquidity.⁵¹ Press releases extolled this breakthrough development. The FDIC was expected to approve the transaction once the terms and conditions were met. Governor Sundlun announced that the deal would put over \$100 million back into the hands of 30,000 depositors. Furthermore, this acquisition was thought to potentially serve as a model for the acquisition of other closed credit unions.⁵² Senator Chafee urged FDIC Chairman Seidman to consider the

⁴⁹ United States Congress, House, Committee on Banking, Finance and Urban Affairs, Rhode Island Banking Crisis: Field Hearings before the Committee on Banking, Finance and Urban Affairs, 102nd Cong, 1st Sess, May 24, 1991.

⁵⁰ Letter from Timothy Ryan to Senator John Chafee, June 5, 1991, The Senatorial Papers of John H. Chafee, Series: Press Releases/Subject File (1977-1999), Box 10, Folder 129, University of Rhode Island Special Collections and University Archives, Kingston, RI.

⁵¹ Letter from John F. Downey to Theodore Barnes, June 11, 1991, Governor Bruce Sundlun Papers, Box 115, Folder 30, University of Rhode Island Special Collections and University Archives, Kingston, RI.

acquisition application in an expedited fashion.⁵³ Governor Sundlun requested that Downey move expeditiously to have the FDIC examine Columbian, Providence Teachers and Greater Providence Trust with the goal of creating new parallel agreements.⁵⁴ OTS Director Timothy Ryan informed Governor Sundlun on June 20 that the OTS and FDIC would begin exams for Providence Teachers and Columbian the following week. He also expressed gratitude for the work of the State's Congressional delegation.⁵⁵

On August 15, officials from the State, DEPCO, and Old Stone bank met with federal regulators at the OTS office in Boston. Regulators announced about 20 changes, conditions, or objections to the documents. The most important issues included environmental liability, tax effects, asset valuation, and liability valuation.⁵⁶ On September 11, officials representing the State, Old Stone Bank, DeLoitte Touche, and the IRS gathered in Washington, DC for an IRS pre-submission ruling conference. The IRS wanted to discuss issues in person, since this ruling was set to be the first of its kind. This was viewed as a cooperative and constructive meeting. A follow-up meeting was scheduled for September 23 to settle any remaining concerns.⁵⁷

⁵² Old Stone Corporation Press Release- "Old Stone Receives Regulatory Approval to Acquire East Providence Credit Union," June 11, 1991, The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 17, Folder 233, University of Rhode Island Special Collections and University Archives, Kingston, RI; Governor's Office Press Release- "Governor Bruce Sundlun's Statement on the Proposed Transaction between East Providence Credit Union and Old Stone Bank," June 19, 1991, The Senatorial Papers of John H. Chafee, Series: Press Releases/Subject File (1977-1999), Box 10, Folder 129, University of Rhode Island Special Collections and University Archives, Kingston, RI.; Senator John Chafee Press Release- "Chafee Welcomes Support of Old Stone Plan, Urges Prompt Review by FDIC," June 19, 1991, The Senatorial Papers of John H. Chafee, Series: Press Releases/Subject File (1977-1999), Box 10, Folder 129, University of Rhode Island Special Collections and University Archives, Kingston, RI.; See also, Letter from Congressman Ron Machtley to Governor Bruce Sundlun, June 11, 1991, Governor Bruce Sundlun Papers, Box 115, Folder 30, University of Rhode Island Special Collections and University Archives, Kingston, RI.

⁵³ Letter from Senator John Chafee to Chairman L. William Seidman, June 14, 1991, The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 17, Folder 233, University of Rhode Island Special Collections and University Archives, Kingston, RI.

⁵⁴ Letter from Governor Bruce Sundlun to John F. Downey, June 17, 1991, Governor Bruce Sundlun Papers, Box 115, Folder 30, University of Rhode Island Special Collections and University Archives, Kingston, RI.

⁵⁵ Letter from Timothy Ryan to Governor Bruce Sundlun, June 20, 1991, The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 17, Folder 233, University of Rhode Island Special Collections and University Archives, Kingston, RI.

⁵⁶ August 15, 1991 OTS Meeting, August 15, 1991, The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 17, Folder 233, University of Rhode Island Special Collections and University Archives, Kingston, RI.

On September 26, 1991, Old Stone Bank announced that it was suspending its efforts to acquire closed Rhode Island institutions. This included the previously-announced East Providence transaction.⁵⁸ One day later, Old Stone Corporation (the Bank's parent company) announced that it was selling approximately 50% of Old Stone Credit Corporation, its consumer finance subsidiary.⁵⁹ In a local news interview, Downey of OTS said that given the information learned through the examinations, in conjunction with the situation concerning Old Stone's own portfolios, the situation was not optimal for pursuing the deal.⁶⁰ Downey was optimistic that Northeast Savings Bank would be able to step into the fold, using all the groundwork that had been completed in the preceding months.⁶¹ In his press release, Governor Sundlun announced that upon the withdrawal of Old Stone, State officials commenced meetings with Northeast Chairman and CEO George Rutland about pursuing a transaction.⁶²

Building off Failure: The Northeast Savings Bank Acquisition Plan

Immediately following the collapse of the Old Stone deal, parties worked to put into motion a new plan involving Northeast Savings. As John Downey of OTS stated in the aforementioned interview, "... everybody's been working very hard to try to get this done under a lot of

⁵⁷ Overview IRS Meeting- Washington, DC, September 11, 1991, The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 17, Folder 233, University of Rhode Island Special Collections and University Archives, Kingston, RI; Memo from Governor Bruce Sundlun to the Rhode Island Congressional Delegation regarding IRS Meeting in Washington- September 11, 1991, September 16, 1991, The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 17, Folder 233, University of Rhode Island Special Collections and University Archives, Kingston, RI.

⁵⁸ Old Stone Corporation Press Release- "Old Stone Bank Suspends Efforts to Acquire Credit Unions," September 26, 1991, The Senatorial Papers of John H. Chafee, Series: Press Releases/Subject File (1977-1999), Box 3, Folder 37, University of Rhode Island Special Collections and University Archives, Kingston, RI.

⁵⁹ Old Stone Corporation Press Release- "Old Stone Signs Definitive Agreement on Partial Sale of Old Stone Credit Corporation; Nears Completion of Annual Regulatory Exam," September 27, 1991, The Senatorial Papers of John H. Chafee, Series: Press Releases/Subject File (1977-1999), Box 3, Folder 37, University of Rhode Island Special Collections and University Archives, Kingston, RI.

⁶⁰ It turned out that Old Stone was itself on shaky financial footing. On January 29, 1993, federal regulators took over the institution. By that point, it had been overcome by bad loans and was barely solvent. See "Federal Regulators Seize Old Stone Bank Branches to Stay Open under their Supervision," *Providence Journal*, January 30, 1993, A1.

⁶¹ Statement by John Downey, September 27, 1991, The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 17, Folder 233, University of Rhode Island Special Collections and University Archives, Kingston, RI.

⁶² Governor's Office Press Release- "Statement by the Governor," September 27, 1991, The Senatorial Papers of John H. Chafee, Series: Press Releases/Subject File (1977-1999), Box 3, Folder 37, University of Rhode Island Special Collections and University Archives, Kingston, RI.

pressure and this last thing that happened may delay it a little bit, but we're committed to get Northeast through this process."⁶³

October meetings between the State and Northeast officials revealed a host of complications, including a cash shortage to complete the deal. Northeast Chairman and CEO George Rutland requested a \$25 million investment from the State in order to attain the required return on the transaction. On October 24, Rutland, along with Director of Administration Harry Baird agreed that the transaction would not be possible.⁶⁴

Officials continued working in an effort to salvage the deal. On December 30, OTS Director Timothy Ryan contacted Governor Sundlun to express concerns over how the latter was handling the crisis. Ryan thought that the State was not playing an active enough role in trying to solve the crisis and that he was told DEPCO might be unwilling to provide a proper guarantee for the acquirer of the closed credit unions on the value of the assets.⁶⁵ That same day, Sundlun responded that there must have been a misunderstanding. He cited the December 13 meeting with OTS staff in Boston, in which there was a question about whether the State of Rhode Island should sign the Northeast acquisition agreement as a separate legal entity from DEPCO. Based on the discussion, the State agreed to sign the transaction. Sundlun stated that DEPCO was providing an open-ended guarantee, and that they were also in agreement regarding the valuation methodology.⁶⁶ The following day, Senator Chafee contacted the Governor regarding an "11th hour communication glitch" between Sundlun's staff and OTS. Chafee stated that Mike Ryan had informed him that he was in touch with DOA Director Harry Baird and David Cruise (Sundlun's Chief of Staff) at the State House and Attorney Stephanie Blucher at OTS in Washington to clear up the confusion.⁶⁷

⁶³ Statement by John Downey, September 27, 1991, The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 17, Folder 233, University of Rhode Island Special Collections and University Archives, Kingston, RI.

⁶⁴ A Statement by George P. Rutland, Chairman and Chief Executive Officer, Northeast Savings, F.A. Regarding Negotiations with the State of Rhode Island to Acquire up to Four Closed Credit Unions, October 25, 1991, The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 13, Folder 168, University of Rhode Island Special Collections and University Archives, Kingston, RI.

⁶⁵ Letter from Timothy Ryan to Governor Bruce Sundlun, December 30, 1991, Governor Bruce Sundlun Papers, Box 115, Folder 31, University of Rhode Island Special Collections and University Archives, Kingston, RI.

⁶⁶ Letter from Governor Bruce Sundlun to Timothy Ryan, December 30, 1991, Governor Bruce Sundlun Papers, Box 115, Folder 31, University of Rhode Island Special Collections and University Archives, Kingston, RI.

⁶⁷ Letter from Senator John Chafee to Governor Bruce Sundlun, December 31, 1991, The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 13, Folder 168, University of Rhode Island Special Collections and University Archives, Kingston, RI.

Roadblocks, Setbacks and the Light on the Horizon

Obstacles to completing the deal continued into 1992. On January 21, more than one year into the crisis, Sundlun pleaded with FDIC Chairman William Taylor to expedite the processing of the Northeast deal to acquire four institutions. Sundlun said he was left to believe, based on their November 14 meeting, that the deal was set for consideration on the FDIC's January 21 agenda. The Governor was greatly disappointed when this turned out not to be the case.⁶⁸ Director of Administration Baird implored Senator Chafee to assist in the matter. Apparently, John Stone of the FDIC thought that the transaction would be on the agency's January 28 agenda, despite the State's efforts to stick to a tight timeline. Baird asked Chafee to help bring the final approval to a conclusion.⁶⁹ The next day, Senator Chafee spoke to Stone, reminding him that the Northeast proposal had already been endorsed by the State of Rhode Island, the Office of Thrift Supervision and the New England Regional Office of the FDIC.⁷⁰

On February 6, Senator Chafee urged officials from the Resolution Trust Corporation (RTC) and the FDIC to approve the Northeast plan. The only major remaining unresolved issue concerned the value of Northeast preferred stock, which was being controlled by the Federal Savings and Loan Insurance Corporation.⁷¹ The following day, Governor Sundlun announced that there were no further issues to resolve in advance of the acquisition. He stated that Northeast and the State agreed to jointly provide an additional \$9 million to the RTC in order to settle the Bank's debt. In addition, the amount of depositor funds that would not be made immediately available for withdrawal increased from \$24 million to \$28 million. The Governor stated that it would be better to move quickly, rather than endure further uncertain negotiations with the RTC.⁷² Chafee stated that he looked forward to continued cooperation between State and Federal officials in order to open the institutions.⁷³ On February 11, Senator Chafee contacted IRS

⁶⁸ Letter from Governor Bruce Sundlun to Chairman William Taylor, January 21, 1992, Governor Bruce Sundlun Papers, Box 70, Folder 106, University of Rhode Island Special Collections and University Archives, Kingston, RI.

⁶⁹ Letter from Harry J. Baird to Senator John Chafee, January 21, 1992, The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 13, Folder 168, University of Rhode Island Special Collections and University Archives, Kingston, RI.

⁷⁰ Letter from Senator John Chafee to John W. Stone, January 23, 1992, The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 13, Folder 168, University of Rhode Island Special Collections and University Archives, Kingston, RI.

⁷¹ Senator John Chafee Press Release- "Chafee Urges Top Federal Regulators to Approve Northeast Transaction," February 6, 1992, The Senatorial Papers of John H. Chafee, Series: Press Releases/Subject File (1977-1999), Box 10, Folder 129, University of Rhode Island Special Collections and University Archives, Kingston, RI.

⁷² Governor's Office Press Release- "Northeast Savings Acquisition Agreement Update," February 7, 1992, The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 13, Folder 168, University of Rhode Island Special Collections and University Archives, Kingston, RI.

Commissioner Shirley Peterson and SEC Chairman Richard Breeden requesting expeditious consideration of the Northeast proposal.⁷⁴

On February 12, 1992 the FDIC Board of Directors formally approved the Northeast Savings proposal to purchase Columbian Credit Union, Greater Providence Deposit Corporation, East Providence Credit Union, and Providence Teachers Union. Each of the offices would become a branch of Northeast Savings.⁷⁵ Northeast officially signed off on the acquisition agreement on April 21, 1992.⁷⁶

Aftermath

Governor Bruce Sundlun won re-election in 1992. Two years later, he was defeated in the Democratic primary.

In February 1992, DEPCO sued Ernst & Young, which had served as RISDIC's auditor. Five years later, the firm settled with the State for \$103 million.⁷⁷

After nearly a year and a half on the run, Joseph Mollicone surrendered to authorities in April 1992. The following year, he was convicted of 26 counts of embezzlement, conspiracy and

⁷³ Senator John Chafee Press Release- "Chafee Pleased that Major Roadblock has been Removed from Northeast Savings Acquisition; Will Now Press FDIC for Final Approval," February 7, 1992, Series: Press Releases/Subject File (1977-1999), Box 10, Folder 129, University of Rhode Island Special Collections and University Archives, Kingston, RI.

⁷⁴ Letter from Senator John Chafee to Commissioner Shirley D. Peterson, February 11, 1992, The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 13, Folder 168, University of Rhode Island Special Collections and University Archives, Kingston, RI; Letter from Senator John Chafee to Chairman Richard C. Breeden, February 11, 1992, The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 13, Folder 168, University of Rhode Island Special Collections and University Archives, Kingston, RI.

⁷⁵ FDIC Press Release- "Statement," February 12, 1992, The Senatorial Papers of John H. Chafee, Series: Banking (1982-2000), Box 13, Folder 168, University of Rhode Island Special Collections and University Archives, Kingston, RI. Account holders with balances under \$9,000 were to have immediate access to 100% of their funds. Those holding accounts over the threshold received 90% in cash, along with a debenture for the remaining balance. See DEPCO Business Plan 1992-1996, November 19, 1992, Governor Bruce Sundlun Papers, Box 116, Folder 33, University of Rhode Island Special Collections and University Archives, Kingston, RI.

⁷⁶ Acquisition Agreement by and among Northeast Savings, F.A. and Maurice Paradis and Edward D. Pare, Jr. and The Rhode Island Depositors Economic Protection Corporation and The State of Rhode Island and Providence Plantations, April 21, 1992, Rhode Island Depositors Economic Protection Corporation (DEPCO) records, Box 77, Folder 13, Rhode Island State Archives, 2002-09, Rhode Island Depositors Economic Protection Corporation (DEPCO) records.

⁷⁷ Katherine Gregg, "DEPCO Reaps \$103 Million Settlement; The Settlement with Ernst & Young will Shave Five Years off the Time Needed for Taxpayers to Pay for the Bailout of Depositors Stranded by the 1991 Banking Crisis," *Providence Journal*, September 18, 1997, A1.

violation of banking laws. Superior Court Judge Dominic F. Cresto sentenced Mollicone to 40 years in prison, with 30 years to serve, plus \$12 million dollars to the state and a \$420,000 fine.⁷⁸

DEPCO completed repayment on the \$125 million U.S. Treasury loan in October, 1993, more than six years ahead of schedule.⁷⁹

In July, 1994, Citizens Savings Bank purchased Old Stone Bank.⁸⁰

On June 20, 1995, Governor Lincoln Almond signed a law requiring all financial institutions in Rhode Island that receive deposits to maintain federal deposit insurance.⁸¹

Shawmut National Corporation purchased Northeast Federal Corporation in June, 1994.⁸² On November 1, 1995, all remaining depositors were mailed the last of their checks. The final debentures had originally been scheduled for payment in May 2012.⁸³

All depositors affected by the crisis got their money back.

DEPCO paid off its \$697 million debt in August 2000, 20 years ahead of schedule.⁸⁴ DEPCO closed for business in December, 2002.⁸⁵

Mollicone was released from prison on July 24, 2002, having served 10 years.⁸⁶ He currently works two jobs and pays the State of Rhode Island \$300 a month in accordance with his

⁷⁸ John Sullivan, "Mollicone Gets 30 Years; Judge Cresto also Orders Mollicone to Pay \$420,000 in Fines and \$12 Million in Restitution," *Providence Journal*, July 28, 1993, A1.

⁷⁹ John Kostrzewa, "DEPCO Repays in a Big Way; A \$125 Million Check Marked the First Retirement of a Chunk of Debt Taken on by the Bailout Agency," *Providence Journal*, October 9, 1993, C1.

⁸⁰ Jeffrey L. Hiday, "Citizens will Take over Old Stone; Citizens Financial Group Solidifies its Standing as Rhode Island's Second Biggest Bank, behind Fleet," *Providence Journal*, July 2, 1994, A1.

⁸¹ Rhode Island (State). Legislature. General Assembly. *An Act Relating to Financial Institutions* (95-S641). June 20, 1995.

⁸² Jeffrey L. Hiday, "Two Big Regional Banks get Bigger; Shawmut Buys the Rest of Northeast Federal," *Providence Journal*, June 14, 1994, D1.

⁸³ Neil Downing, "Money Line: A Long, Painful Chapter in R.I. Banking is Over; The Banking Crisis that Began Nearly Five Years Ago Officially Ends, as the Final Payout Checks are Mailed," *Providence Journal*, November 2, 1995, F1.

⁸⁴ Stacey Higginbotham, "Rhode Island Erases \$697 Million Debt; Successful DEPCO to Close Shop," *The Bond Buyer*, August 16, 2000, 3.

⁸⁵ John Kostrzewa, "The Credit-Union Calamity- An Imperfect Agency Mops up the Mess," *Providence Journal*, December 20, 2002, A1. Although all depositors had been paid off, not all of the agreements with delinquent borrowers had been settled. Upon dissolving, DEPCO transferred its assets to the Rhode Island Division of Taxation, and arranged for a three-member committee to deal with remaining affairs. The final debt settlement took place on February 21, 2005. See Andrea L. Stape, "Panel Picks up where DEPCO Left Off in '02," *Providence Journal*, February 16, 2005, A1; Andrea L. Stape, "State Accepts \$6.5 Million Procaccianti Settlement," *Providence Journal*, February 22, 2005, A1.

⁸⁶ Tom Mooney, "Now Free, Mollicone Must Lecture on His Misdeeds," *Providence Journal*, July 25, 2002.

sentence. Mollicone will remain on parole until 2023.⁸⁷ It will take over 3,000 years for him to pay back the stolen sum.

The crisis cost Rhode Island taxpayers \$290 million.⁸⁸

⁸⁷ Katie Mulvaney, "Where are they Now?- Embezzler Mollicone Working Two Jobs to Pay Back R.I.- Once-Fugitive Banker Owes Nearly \$12 Million, Pays \$300 a Month," *Providence Journal*, December 31, 2017, A6.

⁸⁸ Andrea L. Stape, "Panel Picks up where DEPCO Left Off in '02," *Providence Journal*, February 16, 2005, A1.