December 7, 2008

By John Poirier and Rachelle Younglai

WASHINGTON (Reuters) - U.S. banking regulators swooped in to seize mortgage lender IndyMac Bancorp Inc on Friday after withdrawals by panicked depositors led to the third-largest banking failure in U.S. history.

California-based IndyMac, which specialized in a type of mortgage that often required minimal documents from borrowers, became the fifth U.S. bank to fail this year as a housing bust and credit crunch strain financial institutions. The federal takeover of IndyMac capped a tumultuous day for U.S. markets that saw stocks slide on a surging oil price and renewed fears about the stability of the top two home financing providers, Fannie Mae and Freddie Mac . IndyMac will reopen fully on Monday as IndyMac Federal Bank under Federal Deposit Insurance Corp supervision, but tensions ran high as customers at a branch at its Los Angeles-area headquarters read a notice in the window saying it was closed.

At another branch down the road, a man who said he had more than $200,000 in an account -- twice what is normally FDIC guaranteed -- argued with a security guard who was closing up.

The FDIC, which will seek a buyer for IndyMac, estimated the cost of the bank's failure to its $53 billion insurance fund at between $4 billion and $8 billion.

"IndyMac is a company that was pretty much 100 percent invested in mortgage assets, and we're in a bad mortgage market, and it had no capital. It's not complicated," said Adam Compton, co-head of global financial stock research at RCM in San Francisco, which manages about $150 billion.

IndyMac joins top bank failures headed by the 1984 collapse of Continental Illinois National Bank & Trust Co. The Office of Thrift Supervision (OTS) insisted IndyMac's failure was the second-largest bank failure based on FDIC figures. But the FDIC said its data showed it was third behind the collapse of First RepublicBank Corp in 1988.

RUN ON THE BANK

The OTS, IndyMac's primary regulator, blamed comments by New York Democratic Sen. Charles Schumer for causing a run on deposits at the largest independent publicly traded U.S. mortgage lender. Schumer responded quickly on Friday, blaming the OTS for not doing its job and allowing IndyMac's loose lending practices. "OTS should start doing its job to prevent future IndyMacs," he said in a statement. Schumer questioned IndyMac's ability to survive the housing crisis in late June, and over the next 11 business days, depositors withdrew more than $1.3 billion, the OTS said.

"This institution failed today due to a liquidity crisis," OTS Director John Reich said. "Although this institution was already in distress, I am troubled by any interference in the regulatory process." IndyMac was founded in 1985 by David Loeb and Angelo Mozilo, who also founded Countrywide, another big mortgage lender whose loans helped fuel the housing boom. Countrywide was taken over last week by Bank of America Corp . FDIC spokesman David Barr said agency officials arrived at IndyMac's headquarters in Pasadena at 3 p.m. (2200 GMT).

The successor FDIC-run bank opens for business on Monday. Over the weekend, depositors will have access to their funds by ATM, other debit card transactions, or by writing checks, but no access via online banking and phone services until Monday.

Yet many customers were in the dark as branches shut on Friday. "I'm pissed. They should have let me know," said Elizabeth Ortega, a 29-year-old hairdresser who has a checking account with IndyMac.

IndyMac had said earlier in the week it was unable to raise new capital, would slash staff by 60 percent and had stopped making home loans. Its stock then tumbled, last trading at 28 cents on the New York Stock Exchange, down 95 percent in 2008.

The FDIC insures up to $100,000 per deposit and up to $250,000 per retirement account at insured banks. At the time of closing, IndyMac had about $1 billion of potentially uninsured deposits held by about 10,000 depositors.

The FDIC said it would pay those depositors an advance dividend equal to 50 percent of the uninsured amount.
The OTS told a conference call with reporters that it did not expect significant market impact from IndyMac's closure as the firm is not a systemic institution and does not have numerous counterparties. Reich also said he did not expect a larger thrift to fail.

MORE FAILURES SEEN

Four small banks have already been closed this year and the FDIC is hiring more staff in preparation for more failures. The agency has boosted its list of troubled banks to 90 and has said an increasing number of banks face high exposure to deteriorating conditions in commercial real estate and construction lending. Last year, just three banks failed.

"IndyMac's takeover by the FDIC is one of many to come," predicted Daniel Alpert, an investment banker at Westwood Capital in New York.

Former FDIC official Ann Graham said it was not unprecedented for the FDIC to start running a bank after it fails. "It happens when they need to move more swiftly with the closing than they can move with a potential sale," said Graham, a law professor at Texas Tech University.

"They don't have to sell the institution over the weekend," she said. "They have the time to shop around."
Graham said the FDIC has the authority to operate an institution for two years but expected the agency would dispose of it much sooner than that.