

## FEDERAL DEPOSIT INSURANCE CORPORATION

### 12 CFR Part 327

RIN 3064-AD57

#### Assessments

**AGENCY:** Federal Deposit Insurance Corporation.

**ACTION:** Notice of proposed rulemaking and request for comment.

**SUMMARY:** The FDIC proposes to amend our regulations to revise the assessment system applicable to large institutions to better differentiate institutions by taking a more forward-looking view of risk; to better take into account the losses that the FDIC will incur if an institution fails; to revise the initial base assessment rates for all insured depository institutions; and to make technical and other changes to the rules governing the risk-based assessment system.

**DATES:** Comments must be received on or before 60 days after publication.

**ADDRESSES:** You may submit comments, identified by RIN number, by any of the following methods:

- *Agency Web Site:* <http://www.fdic.gov/regulations/laws/federal/propose.html>. Follow instructions for submitting comments on the Agency Web Site.

- *E-mail:* [Comments@FDIC.gov](mailto:Comments@FDIC.gov).

Include the RIN number in the subject line of the message.

- *Mail:* Robert E. Feldman, Executive Secretary, Attention: Comments, Federal Deposit Insurance Corporation, 550 17th Street, NW., Washington, DC 20429

- *Hand Delivery/Courier:* Guard station at the rear of the 550 17th Street Building (located on F Street) on business days between 7 a.m. and 5 p.m.

*Instructions:* All submissions received must include the agency name and RIN for this rulemaking. Comments will be posted only to the extent practicable and, in some instances, the FDIC may post summaries of categories of comments, with the comments themselves available in the FDIC's reading room. Comments will be posted at: <http://www.fdic.gov/regulations/laws/federal/propose.html>, including any personal information provided with the comment.

**FOR FURTHER INFORMATION CONTACT:** Lisa Ryu, Chief, Large Bank Pricing Section, Division of Insurance and Research, (202) 898-3538; Heather L. Etner, Financial Analyst, Banking and Regulatory Policy Section, Division of Insurance and Research, (202) 898-6796; Robert L. Burns, Chief, Exam

Support and Analysis, Division of Supervision and Consumer Protection (704) 333-3132 x4215; Christopher Bellotto, Counsel, Legal Division, (202) 898-3801; Sheikha Kapoor, Senior Attorney, Legal Division, (202) 898-3960.

#### SUPPLEMENTARY INFORMATION:

##### I. Background

###### *The Reform Act*

On February 8, 2006, the President signed the Federal Deposit Insurance Reform Act of 2005 into law; on February 15, 2006, he signed the Federal Deposit Insurance Reform Conforming Amendments of 2005 (collectively, the Reform Act).<sup>1</sup> The Reform Act, among other things, gives the FDIC, through its rulemaking authority, the opportunity to better price deposit insurance for risk.<sup>2</sup>

The Federal Deposit Insurance Act, as amended by the Reform Act, requires that the assessment system be risk-based and allows the FDIC to define risk broadly. It defines a risk-based system as one based on an institution's probability of causing a loss to the Deposit Insurance Fund (the Fund or the DIF) due to the composition and concentration of the institution's assets and liabilities, the likely amount of any such loss, and the revenue needs of the DIF. The Reform Act leaves in place the statutory provision allowing the FDIC to "establish separate risk-based assessment systems for large and small members of the Deposit Insurance Fund."<sup>3</sup> But the Reform Act provides that "[n]o insured depository institution shall be barred from the lowest-risk category solely because of size."<sup>4</sup>

###### *2006 Assessments Rule*

On November 30, 2006, pursuant to the requirements of the Reform Act, the FDIC adopted by regulation (the 2006 assessments rule) an assessment system that placed insured depository institutions into risk categories (Risk Category I, II, III or IV), depending upon supervisory ratings and capital levels.<sup>5</sup> Within Risk Category I, the 2006 assessments rule created different

assessment systems for large and small institutions that combined supervisory ratings with other risk measures to further differentiate risk and determine assessment rates.<sup>6</sup>

To determine assessment rates for large Risk Category I institutions that had a long-term debt issuer rating, the 2006 assessments rule combined the institution's weighted average CAMELS component rating and any current long-term debt issuer rating or ratings assigned by the major U.S. rating agencies (the debt ratings method). For large institutions that did not have a long-term debt issuer rating, the rule set initial assessment rates using a financial ratios method, which combined the weighted average CAMELS component rating and certain financial ratios. (This method was also applied to all small institutions.) The 2006 assessments rule allowed the FDIC to adjust initial assessment rates for large Risk Category I institutions to ensure that the relative levels of risk posed by these institutions were consistently reflected in assessment rates; the adjustment is known as the large bank adjustment.<sup>7</sup> The FDIC provided additional detail on the calculation of the large bank adjustment in its Guidelines for Large Institutions and Insured Foreign Branches in Risk Category I (the large bank guidelines).<sup>8</sup>

###### *2009 Assessments Rule*

Effective April 1, 2009, the FDIC amended its assessments rule (the 2009 assessments rule) to create the current assessment system. Under this assessment system, the initial base assessment rate for a Risk Category I institution is determined by either the financial ratios method applicable to all small institutions or, for institutions with at least one long-term debt rating, by a new large bank method.<sup>9</sup> The new

<sup>6</sup> The 2006 final rule defined a large institution as an institution (other than an insured branch of a foreign bank) with \$10 billion or more in assets as of December 31, 2006 (although an institution with at least \$5 billion in assets could request treatment as a large institution). If, after December 31, 2006, an institution classified as small reports assets of \$10 billion or more in its report of condition for four consecutive quarters, the FDIC will reclassify the institution as large beginning in the following quarter. If, after December 31, 2006, an institution classified as large reports assets of less than \$10 billion in its report of condition for four consecutive quarters, the FDIC will reclassify the institution as small beginning the following quarter. 12 CFR 327.8(g) and (h) (2009) and 327.9(d)(6) (2009).

<sup>7</sup> 71 FR 69282, 69292-69294 (Nov. 30, 2006).

<sup>8</sup> 72 FR 27122 (May 14, 2007).

<sup>9</sup> The financial ratios method also applies to large institutions without at least one long-term debt rating. The 2009 assessments rule added a new measure—the adjusted brokered deposit ratio—to the financial ratios that were considered under the

<sup>1</sup> Federal Deposit Insurance Reform Act of 2005, Public Law 109-171, 120 Stat. 9; Federal Deposit Insurance Conforming Amendments of 2005, Public Law 109-173, 119 Stat. 3601.

<sup>2</sup> Section 2109(a)(5) of the Reform Act. Section 7(b) of the Federal Deposit Insurance Act (12 U.S.C. 1817(b)).

<sup>3</sup> Section 7(b)(1)(D) of the Federal Deposit Insurance Act (12 U.S.C. 1817(b)(1)(D)).

<sup>4</sup> Section 2104(a)(2) of the Reform Act amending Section 7(b)(2)(D) of the Federal Deposit Insurance Act (12 U.S.C. 1817(b)(2)(D)).

<sup>5</sup> 71 FR 69282. (Nov. 30, 2006). The FDIC also adopted several other final rules implementing the Reform Act, including a final rule on operational changes to part 327. 71 FR 69270 (Nov. 30, 2006).

large bank method incorporates a financial ratios score. For a large institution in Risk Category I with a long-term debt issuer rating, the initial base assessment rate combines the institution's weighted average CAMELS

component rating, its average long-term debt issuer ratings, and its financial ratios score, each equally weighted (the large bank method). The 2009 assessments rule also increased the maximum large bank adjustment of the

initial base assessment rate from 0.50 basis points to 1 basis point.<sup>10</sup>

Initial base assessment rates as of April 1, 2009, are set forth in Table 1 below.

TABLE 1—INITIAL BASE ASSESSMENT RATES AS OF APRIL 1, 2009

	Risk category				
	I*		II	III	IV
	Minimum	Maximum			
Annual Rates (in basis points) .....	12	16	22	32	45

\* Rates for institutions that do not pay the minimum or maximum rate will vary between these rates.

The 2009 assessments rule provided for adjustments to the initial base assessment rate for institutions in all risk categories. An institution's total base assessment rate can vary from its initial base assessment rate as the result of an unsecured debt adjustment and a secured liability adjustment. The unsecured debt adjustment lowers an institution's initial base assessment rate

using its ratio of long-term unsecured debt (and, for small institutions, certain amounts of Tier 1 capital) to domestic deposits.<sup>11</sup> The secured liability adjustment increases an institution's initial base assessment rate if the institution's ratio of secured liabilities to domestic deposits is greater than 25 percent (the secured liability adjustment).<sup>12</sup> In addition, institutions

in Risk Categories II, III and IV are subject to an adjustment for large levels of brokered deposits (the brokered deposit adjustment).<sup>13</sup>

After applying all possible adjustments, the minimum and maximum total base assessment rates for each risk category under the 2009 assessments rule are set out in Table 2 below.

TABLE 2—INITIAL AND TOTAL BASE ASSESSMENT RATES

	Risk category I	Risk category II	Risk category III	Risk category IV
Initial base assessment rate .....	12–16	22	32	45
Unsecured debt adjustment .....	–5–0	–5–0	–5–0	–5–0
Secured liability adjustment .....	0–8	0–11	0–16	0–22.5
Brokered deposit adjustment .....	.....	0–10	0–10	0–10
Total Base Assessment Rate .....	7–24bp	17–43bp	27–58bp	40–77.5bp

All amounts for all risk categories are in basis points annually. Total base rates that are not the minimum or maximum rate will vary between these rates.

**II. Overview of the Proposal**

The FDIC proposes to revise the assessment system applicable to large institutions to better capture risk at the time an institution assumes the risk, to better differentiate institutions during periods of good economic and banking conditions based on how they would fare during periods of stress or economic downturns, and to better take into account the losses that the FDIC may incur if an institution fails.

The FDIC has carefully considered the measurements that should be used to assess large banks' risk. The proposal includes quantitative measures that are readily available and statistically significant in predicting an institution's

long-term performance. The FDIC believes that other considerations—such as stress testing, underwriting characteristics, and risk management practices—are also important in the risk assessment of large institutions, and they should be factored into the risk-based assessment system. While the FDIC has already identified some key metrics for these additional considerations, the FDIC is seeking further input in a request for comments included in this proposed rulemaking. The FDIC also anticipates that any final rule issued pursuant to this notice of proposed rulemaking would be followed by discussions with the industry on ways to improve the system adopted, as

well as coordination with other regulators. Ultimately, the FDIC anticipates a further round of rulemaking may be needed to improve the large bank assessment system adopted pursuant to this rulemaking.

The FDIC proposes to eliminate risk categories for large institutions to allow the FDIC to draw finer distinctions among large institutions based upon the risk that they pose. For all large institutions, the FDIC proposes to eliminate use of long-term debt issuer ratings. The FDIC has found that debt issuer ratings, particularly for the largest institutions, do not respond quickly to an institution's changing risk profile. The FDIC proposes to continue to rely

2006 assessments rule. The adjusted brokered deposit ratio measures the extent to which certain brokered deposits are used to fund rapid asset growth. The adjusted brokered deposit ratio excludes deposits that a Risk Category I institution receives through a deposit placement network on a reciprocal basis, such that: (1) For any deposit

received, the institution (as agent for depositors) places the same amount with other insured depository institutions through the network; and (2) each member of the network sets the interest rate to be paid on the entire amount of funds it places with other network members (reciprocal deposits).

<sup>10</sup> 74 FR 9525, 9535–9536 (Mar. 4, 2009).

<sup>11</sup> Unsecured debt excludes debt guaranteed by the FDIC under its Temporary Liquidity Guarantee Program.

<sup>12</sup> The initial base assessment rate cannot increase more than 50 percent as a result of the secured liability adjustment.

<sup>13</sup> 74 FR 9522, 9541 (Mar. 4, 2009).

upon CAMELS ratings and financial measures to determine assessment rates.<sup>14</sup>

The FDIC proposes to combine CAMELS ratings and certain financial measures into two scorecards—one for most large institutions and another for large institutions that are structurally and operationally complex or that pose unique challenges and risks in case of failure (Highly Complex Institutions). Each scorecard would consist of a performance component, which would measure an institution's financial performance and its ability to withstand stress, and a loss severity component, which would correspond to the level of potential losses in case of failure. The data underlying these measures are readily available. Most of the data are publicly available, but some are gathered during the examination process. Under the proposal, the FDIC would have the ability to adjust each component where necessary to produce accurate relative risk rankings.

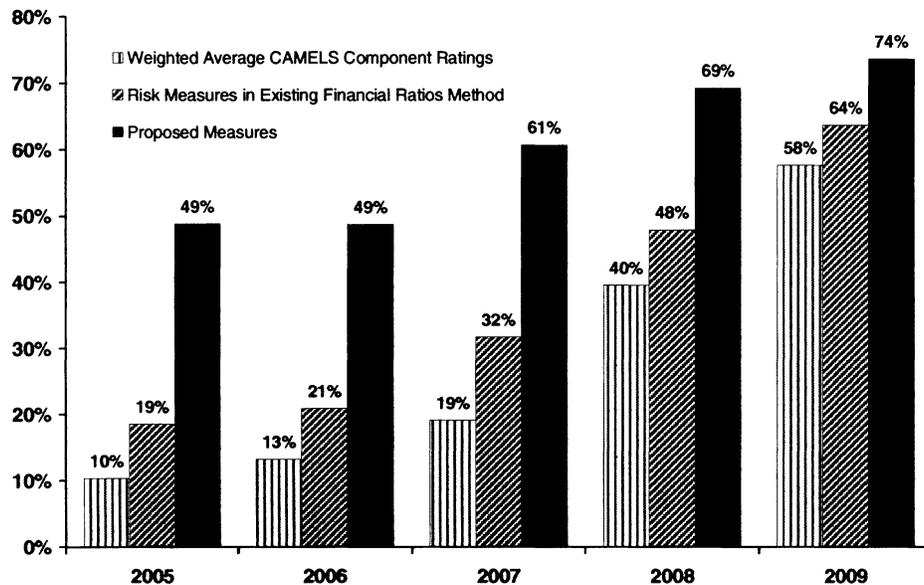
Because some of the financial measures that the FDIC is proposing focus on long-term risk, they should mitigate the pro-cyclicality of the current system. Over the long term, institutions that pose higher long-term risk will pay higher assessments when they assume these risks—usually during economic expansions—rather than facing large assessment increases when conditions deteriorate. In so doing, they should provide incentives for institutions to avoid excessive risk during economic expansions.

As shown in Chart 1, the proposed measures were useful in predicting long-term performance of large institutions over the 2005 to 2009 period. The chart contrasts the predictive values of the proposed measures with weighted-average CAMELS component ratings and with the existing financial ratios method. (The financial ratios method is based on a statistical model that predicts downgrades of small banks within 12

months, but the method also applies to large Risk Category I banks.) The proposed measures predict the FDIC's view, based on its experience and judgment, of the proper rank ordering of risk for large institutions do significantly better than the other two methods and, thus, better than the current system used for most large Risk Category I institutions, which combines weighted-average CAMELS composite scores, the financial ratios method and long-term debt issuer ratings. (As noted above, debt issuer ratings, particularly for the largest institutions, do not respond quickly to an institution's changing risk profile.) For example, in 2006, the proposed measures would have predicted the FDIC's expert judgment-based risk ranking of large institutions as of year-end 2009 nearly two and one-half times better than the risk measures in the existing financial ratios method, which applies to large banks without debt ratings.

### Various Measures' Ability to Predict Current Expert Judgment Risk Ranking<sup>15</sup>

Percentage Approximated by Factors (Adjusted R-Square)



The FDIC also proposes to alter assessment rates applicable to all insured depository institutions to ensure that the revenue collected under the new assessment system would

approximately equal that under the existing assessment system and also to ensure that the lowest rate applicable to both small and large institutions would be the same. The FDIC would retain its

flexibility to raise assessment rates up to 3 basis points above or below base assessment rates without the necessity of further rulemaking.

<sup>14</sup> The proposed rule clarifies that if the FDIC disagrees with the ratings changes to an institution's risk assignment by its primary federal regulator or, for state-chartered institutions, by the state banking supervisor, the FDIC will notify the institution of its decision and any resulting change

to an institution's risk assignment is effective as of the date of FDIC's transmittal notice.

<sup>15</sup> The expert judgment ranking is a risk ranking of large institutions based on FDIC's current analyses. The ranking is largely based on the information available through the FDIC's Large

Insured Depository Institution (LIDI) program. Large institutions that failed or received significant government support over the period are assigned the worst risk ranking and are included in the statistical analysis. Appendix 1 describes the statistical analysis in detail.

**III. Risk-Based Assessment System for Large Insured Depository Institutions**

A “large institution” would continue to be defined under the proposal as an insured depository institution with \$10 billion or greater in total assets for at least four consecutive quarters. The proposal would apply to all large institutions regardless of whether they are defined as new.<sup>16</sup> Insured branches of foreign banks would not be defined as large institutions.

*A. Scorecard for Large Institutions (Other Than Highly Complex Institutions)*

The scorecard method would use risk measures to derive an assessment rate reflective of the risk that an institution poses to the insurance fund. Each

scorecard would produce two scores: A performance score and a loss severity score. To arrive at a performance score, the scorecard would combine CAMELS ratings and financial measures into a single performance score between 0 and 100. The FDIC would have limited ability to adjust an institution’s performance score based upon quantitative or qualitative measures not adequately captured in the scorecard.

The scorecard would also combine loss severity measures into a single loss severity score between 0 and 100. The loss severity score would then be converted into a loss severity measure. The FDIC would also have limited ability to alter an institution’s loss severity score based upon quantitative or qualitative measures not adequately captured in the scorecard. Multiplying

the performance score by the loss severity measure would produce a combined score, which would then be converted to an initial assessment rate.

In general, a risk measure value reflecting lower risk than the cutoff value that results in a score of 0 would also receive a score of 0, where 0 equals the lowest risk for that measure. A risk measure value reflecting higher risk than the cutoff value that results in a score of 100 would also receive a score of 100, where 100 equals the highest risk for that measure. A risk measure value between the cutoff values would be converted to a score between 0 and 100, which would be rounded to 3 decimal points.

Table 3 shows scorecard measures and the possible range of scores.

**TABLE 3—SCORECARD FOR LARGE INSTITUTIONS**

Components	Scorecard measures	Score	
CAMELS .....	<i>Weighted Average CAMELS</i> .....	<i>25–100</i>	
Ability to Withstand Asset-Related Stress	Tier 1 Common Capital Ratio (Tier 1 Common Capital/Total Average Assets less Disallowed Intangibles).	0–100	
	Concentration Measure ..... Higher Risk Concentrations; or Growth-Adjusted Portfolio Concentrations.	0–100	
	Core Earnings/Average Total Assets .....	0–100	
	Credit Quality Measure ..... Criticized and Classified Items/Tier 1 Capital and Reserves; or Underperforming Assets/Tier 1 Capital and Reserves.	0–100	
	Subtotal .....	0–100	
	Outlier Add-ons		
	Criticized and Classified Items/Tier 1 Capital and Reserves; or Underperforming Assets/Tier 1 Capital and Reserves.	30	
	Higher Risk Concentrations .....	30	
	<i>Total ability to withstand asset-related stress score</i> .....	<i>0–160</i>	
Ability to Withstand Funding-Related Stress.	Core Deposits/Total Liabilities .....	0–100	
	Unfunded Commitments/Total Assets .....	0–100	
	Liquid Assets/Short-term Liabilities (liquidity coverage ratio) .....	0–100	
	<i>Total ability to withstand funding-related stress score</i> .....	<i>0–100</i>	
<i>Total Performance Score</i> .....		<i>0–100</i>	
Potential Loss Severity .....	Potential Losses/Total Domestic Deposits (loss severity measure) .....	0–100	
	Secured Liabilities/Total Domestic Deposits .....	0–100	
	<i>Total loss severity score</i> .....	<i>0–100</i>	

<sup>16</sup>In almost all cases, an institution that has had \$10 billion or greater in total assets for four consecutive quarters will have CAMELS ratings.

However, in the rare event that a large institution has not yet received CAMELS ratings, it would be given a weighted average CAMELS rating of 2 for

assessment purposes until actual CAMELS ratings are assigned.

1. Performance Score

The first component of the scorecard for large institutions would be the performance score. The performance score for large institutions would be the weighted average of three inputs: (1) Weighted average CAMELS rating; (2) ability to withstand asset-related stress measures; and (3) ability to withstand funding-related stress measures. Table 4 shows the weight given to each of these three inputs.

TABLE 4—PERFORMANCE SCORE INPUTS AND WEIGHTS

Performance score inputs	Weight (percent)
CAMELS Rating .....	30
Ability to Withstand Asset-Related Stress .....	50
Ability to Withstand Funding-Related Stress .....	20

a. Weighted Average CAMELS Score

To derive the weighted average CAMELS score, a weighted average of an institution's CAMELS component ratings would first be calculated using the weights that are applied in the current rule as shown in Table 5 below.

TABLE 5—WEIGHTS FOR CAMELS COMPONENT RATINGS

CAMELS component	Weight (percent)
C .....	20
A .....	20
M .....	25
E .....	10
L .....	10
S .....	10

A weighted average CAMELS rating would be converted to a score that ranges from 25 to 100. A weighted average rating of 1 would equal a score of 25 and a weighted average of 3.5 or greater would equal a score of 100. Weighted average CAMELS ratings between 1 and 3.5 would be assigned a score between 25 and 100. The score would increase at an increasing rate as the weighted average CAMELS rating increases.

Weighted average CAMELS ratings between 1 and 3.5 would be assigned a

score between 25 and 100 according to the following equation:

$$S = 25 + [(20/3) * (C^2 - 1)],$$

Where:

S = the weighted average CAMELS score and C = the weighted average CAMELS rating.

This equation normalizes the weighted average CAMELS score to the same range as the other components described below so that it can be added to these components, resulting in a performance score. This conversion from a weighted average CAMELS rating to a score is a non-linear conversion. Other conversions used in this proposal would be linear. The non-linear conversion recognizes that the difference between higher CAMELS ratings (e.g., a CAMELS 3 versus a CAMELS 4) represents a greater difference in risk than the difference between lower CAMELS ratings (e.g., a CAMELS 1 versus a CAMELS 2).

b. Ability To Withstand Asset-Related Stress Component

The ability to withstand asset-related stress component would contain measures that are most relevant to assessing a large institution's ability to withstand such stress. These measures would be the following:

- Tier 1 common capital ratio;
- Concentration measure (the higher of the higher-risk concentrations measure or growth-adjusted portfolio concentrations measures);
- Core earnings/average total assets; and
- Credit quality measure (the higher of the criticized and classified items/Tier 1 capital and reserves or underperforming assets/Tier 1 capital and reserves).

In general, these measures proved to be the most statistically significant measures of an institution's ability to withstand asset-related stress, as described in Appendix 1. Appendix B describes these measures in detail and gives the source of the data used to determine them.

Each risk measure within the ability to withstand asset-related stress portion of the scorecard would be converted linearly to a score between 0 and 100 where 100 equals the highest risk and 0 equals the lowest risk for that measure.<sup>17</sup> For each risk measure, a value reflecting lower risk than the cutoff value that results in a score of 0 will also receive a score of 0, where 0

equals the lowest risk for that measure. A value reflecting higher risk than the cutoff value that results in a score of 100 will also receive a score of 100, where 100 equals the highest risk for that measure. A risk measure value between the minimum and maximum cutoff values is converted linearly to a score between 0 and 100. For the Concentration Measure and Credit Quality Measures, a lower ratio implies lower risk and a higher ratio implies higher risk. For these measures, a value between the minimum and maximum cutoff values will be converted linearly to a score between 0 and 100, according to the following formula:

$$S = (V - Min) * 100 / (Max - Min),$$

where S is score (rounded to three decimal points), V is the value of the measure, Min is the minimum cutoff value and Max is the maximum cutoff value.

For the Tier 1 Common Capital Ratio and Core Earnings to Average Total Assets Ratio, a lower value represents higher risk and a higher value represents lower risk. For these measures, a value between the minimum and maximum cutoff values is converted linearly to a score between 0 and 100, according to the following formula:

$$S = (Max - V) * 100 / (Max - Min),$$

where S is score (rounded to three decimal points), V is the value of the measure, Min is the minimum cutoff value and Max is the maximum cutoff value.

The concentration measure score would equal the higher of the two scores that make up the concentration measure score, as would the credit quality score.<sup>18</sup> The credit quality score would be based upon the higher of the criticized and classified items ratio score or the underperforming assets ratio score.<sup>19</sup> Table 6 shows each of the measures, gives the cutoff values for each measure and shows the weight assigned to the measure to derive a score for an institution's ability to withstand asset-related stress. Most of the minimum and maximum cutoff values for each risk measure equal the 10th and 90th percentile values of the particular measure among large institutions based upon data from the period between the first quarter of 2000 and the fourth quarter of 2009.<sup>20 21</sup>

on the higher-risk concentration measure are available consistently since second quarter 2008, and criticized and classified assets are only available consistently since first quarter 2007. For the higher-risk concentration measure, the 85th percentile value is used as a maximum cutoff value. The maximum cutoff value for the criticized and classified asset ratio is close to but does not equal the 90th percentile value. These alternative cutoff values are partly based on recent experience.

<sup>17</sup> This process, in effect, normalizes all the ratios to the same range of values and allows the numbers to be added together.

<sup>18</sup> The higher-risk concentration measure gauges concentrations that are currently deemed to be high risk. The growth-adjusted portfolio concentration measure does not solely consider high-risk portfolios, but considers all portfolio concentrations.

<sup>19</sup> The criticized and classified items ratio measures commercial credit quality while the underperforming assets ratio is often a better indicator for consumer portfolios.

<sup>20</sup> Cutoff values are rounded to one decimal point.

<sup>21</sup> The measures in which the 10th and 90th percentiles would not be used would be the higher-risk concentration measure and the criticized and classified asset ratio due to data availability. Data

TABLE 6—CUTOFF VALUES AND WEIGHTS FOR ABILITY TO WITHSTAND ASSET-RELATED STRESS MEASURES

Scorecard measures	Cutoff values		Weight (percent)
	Minimum	Maximum	
Tier 1 Common Capital Ratio .....	5.8	12.9	15
Concentration Measure .....			35
Higher Risk Concentrations; or .....	0.0	3.2	
Growth-Adjusted Portfolio Concentrations .....	7.6	154.7	
Core Earnings/Average Total Assets .....	0.0	2.3	15
Credit Quality Measure .....			35
Criticized and Classified Items/Tier 1 Capital and Reserves; or .....	6.5	100.0	
Underperforming Assets/Tier 1 Capital and Reserves .....	2.3	35.1	

Each score would be multiplied by a respective weight and the resulting weighted score for each measure would be summed to arrive at an ability to withstand asset-related stress score, which could range from 0 to 100. The FDIC recognizes that extreme values for some measures should have an additional effect on the final scorecard total. For extreme values of certain measures reflecting particularly high risk, this score could increase through

an outlier add-on. Specifically, if an institution's ratio of criticized and classified items to Tier 1 capital and reserves exceeded 100 percent or its ratio of underperforming assets to Tier 1 capital and reserves exceeded 50.2 percent, the ability to withstand asset-related stress component score would be increased by 30 points. Additionally, if the higher risk concentration measure exceeded 4.8, the ability to withstand asset-related stress component score

would be increased by 30 points. These increases (outlier add-ons) would be determined separately and could increase the ability to withstand asset-related stress score by up to 60 points; thus, the ability to withstand asset-related stress component score could be as high as 160 points.<sup>22</sup>

Table 7 illustrates how the ability to withstand asset-related stress score would be calculated for a hypothetical bank, Bank A.

TABLE 7—ABILITY TO WITHSTAND ASSET-RELATED STRESS COMPONENT FOR BANK A

Scorecard measures	Value	Score	Weight (percent)	Weighted score
Tier 1 Common Capital Ratio .....	7.62	74.37	15	11.15
Concentration Measure .....		78.13	35	27.35
Higher Risk Concentrations; or .....	2.50	78.13		
Growth-Adjusted Portfolio Concentrations .....	45.00	25.42		
Core Earnings/Average Total Assets .....	0.50	78.26	15	11.74
Credit Quality Measure .....		100.00	35	35.00
Criticized and Classified Items/Tier 1 Capital and Reserves; or .....	104.32	100.00		
Underperforming Assets/Tier 1 Capital and Reserves .....	33.76	95.91		
Subtotal .....				85.24
Outlier Add-ons:				
Criticized and Classified Items/Tier 1 Capital and Reserves; or .....	104.32			30.00
Underperforming Assets/Tier 1 Capital and Reserves .....	33.76	30.00		
Higher Risk Concentrations .....	2.50	0.00		
Total ability to withstand asset-related stress score .....				115.24

Bank A's higher risk concentrations score (78.13) is higher than its growth-adjusted portfolio concentration score (25.42). Thus, the higher risk concentration score is multiplied by the 35 percent weight to get a weighted score of 27.35 and the growth-adjusted portfolio concentration score would be

ignored. Similarly, Bank A's criticized and classified items to Tier 1 capital and reserves ratio score (100) is higher than its underperforming assets to Tier 1 capital and reserves ratio score (95.91). Therefore, the criticized and classified items to Tier 1 capital and reserves ratio score would be multiplied by the 35

percent weight to get a weighted score of 35.00 and the underperforming assets to Tier 1 capital and reserves ratio score would be ignored. These weighted scores, along with the weighted scores for the Tier 1 common capital ratio (11.15) and core earnings to average total assets ratio (11.74), would be

<sup>22</sup> That is, the statistical analysis shows that a significant amount of criticized and classified items or underperforming assets, or concentrations in high risk portfolios are the most significant (having coefficients with the largest absolute value) measures that help differentiate the risk profiles of large institutions and predict an institution's long-term performance. In addition, recent experience suggests that a small number of institutions with

very high levels of criticized and classified items or underperforming assets, or high risk portfolio concentrations are particularly vulnerable to unexpected asset-related stress. The value that triggers the outlier add-on for the criticized and classified items to Tier 1 capital and reserves was determined using FDIC's judgment. The value that triggers the outlier add-on for the underperforming assets to Tier 1 capital and reserves is the 95th

percentile value for the distribution of values of that measure for large institutions from 2000 to 2009. The value that triggers the outlier add-on for the higher risk concentration measure is the 90th percentile value for the distribution of values of that measure for large institutions from second quarter 2008 to fourth quarter 2009. A lower value was chosen for this measure due to a short history of available data.

added together, resulting in the subtotal of 85.24. Because Bank A's criticized and classified items to Tier 1 capital and reserves ratio score is greater than 100, the criticized and classified items to Tier 1 capital and reserves ratio outlier add-on would be triggered, and an additional 30 points would be added to Bank A's score. Bank A's higher risk concentrations measure score does not exceed 4.8; therefore, the second outlier add-on would not be triggered. Thus, only the outlier add-on for the criticized and classified items to Tier 1 capital and reserves ratio would be added to the subtotal to arrive at the asset vulnerability component score of 115.24 for Bank A.

c. Ability To Withstand Funding-Related Stress

The ability to withstand funding-related stress component would contain three measures that are most relevant to assessing a large institution's ability to withstand such stress—a core deposits to total liabilities ratio, an unfunded commitments to total assets ratio, and a liquid assets to short-term liabilities

(liquidity coverage) ratio. These ratios are significant in predicting a large institution's long-term performance in the statistical test described in Appendix 1. Appendix B describes these ratios in detail and gives the source of the data used to determine them.

Each risk measure would be converted to a score between 0 and 100 where 100 equals the highest risk and 0 equals the lowest risk for that measure. A risk measure value reflecting lower risk than the cutoff value that results in a score of 0, will also receive a score of 0, where 0 equals the lowest risk for that measure. A risk measure value reflecting higher risk than the cutoff value that results in a score of 100, will also receive a score of 100, where 100 equals the highest risk for that measure. For the Core Deposits/Liabilities measure and the Liquidity Coverage Ratio, a lower ratio implies higher risk and a higher ratio implies lower risk. For these measures, a value between the minimum and maximum cutoff values will be converted linearly to a score

between 0 and 100, according to the following formula:

$$S = (Max - V) * 100 / (Max - Min)$$

Where S is score (rounded to three decimal points), V is the value of the measure, Min is the minimum cutoff value and Max is the maximum cutoff value.

For the Unfunded Commitments/Assets measure, a lower value represents lower risk and a higher value represents higher risk. For these measures, a value between the minimum and maximum cutoff values is converted linearly to a score between 0 and 100, according to the following formula:

$$S = (V - Min) * 100 / (Max - Min)$$

Where S is score (rounded to three decimal points), V is the value of the measure, Min is the minimum cutoff value and Max is the maximum cutoff value.

The ability to withstand funding-related stress component score would be the weighted average of the three measure scores. Table 8 shows the cutoff values and weights for these measures.

TABLE 8—CUTOFF VALUES AND WEIGHTS FOR ABILITY TO WITHSTAND FUNDING-RELATED STRESS MEASURES

Scorecard measures	Cutoff values		Weight (percent)
	Minimum	Maximum	
Core Deposits/Total Liabilities .....	3.2	79.1	40
Unfunded Commitments/Total Assets .....	0.3	42.2	40
Liquid Assets/Short-term Liabilities (liquidity coverage ratio) .....	5.6	170.9	20

d. Calculation of Performance Score

The weighted average CAMELS score, the ability to withstand asset-related stress score, and the ability to withstand

funding-related stress score would then be multiplied by their weights and the results would be summed to arrive at the performance score. This score would

not be less than 0 or more than 100 under the proposal. In the example in Table 9, Bank A's performance score would be 81.70.

TABLE 9—PERFORMANCE SCORE FOR BANK A

Performance score components	Weight (percent)	Score	Weighted score
Weighted Average CAMELS Score .....	30	65.15	19.54
Ability to Withstand Asset-Related Stress Score .....	50	115.24	57.62
Ability to Withstand Funding-Related Stress Score .....	20	22.69	4.54
Total Performance Score .....	.....	.....	81.70

The performance score could be adjusted, up or down, by a maximum of 15 points, based upon significant risk factors that are not adequately captured in the scorecard. The resulting score, however, could not be less than 0 or more than 100. The FDIC would use a process similar to the current large bank adjustment to determine the amount of the adjustment to the performance

score.<sup>23</sup> This discretionary adjustment is discussed in more detail below.

2. Loss Severity Score

The loss severity score would measure the relative magnitude of potential losses to the FDIC in the event of an institution's failure. The loss severity score would be based on two measures that are most relevant to

assessing an institution's potential loss severity. The loss severity measure is the ratio of possible losses to the FDIC in the event of an institution's failure to total domestic deposits, averaged over three quarters. A standardized set of assumptions—based on recent failures—regarding liability runoffs and the recovery value of asset categories are applied to calculate possible losses to the FDIC. (Appendix D to the NPR describes the calculation of the measure

<sup>23</sup> 12 CFR 327.9(d)(4) (2009).

in detail.) A loss severity measure is used as part of the current large bank adjustment. The second measure is the ratio of secured liabilities to total domestic deposits. (The greater an institution's secured liabilities relative to domestic deposits, the greater the FDIC's potential rate of loss in the event of failure, since secured liabilities have priority in payment over deposits at failure.) These measures are quantitative measures that are derived from readily available data. Appendix B defines these measures and gives the source of the data used to calculate them.

Each risk measure would be converted to a score between 0 and 100 where 100 equals the highest risk and 0 equals the lowest risk for that measure. A risk measure value reflecting lower risk than the minimum cutoff value results in a score of 0, where 0 equals the lowest risk for that measure. A risk measure value reflecting higher risk than the maximum cutoff value results in a score of 100, where 100 equals the highest risk for that measure. A risk measure value between the minimum and maximum cutoff values is converted linearly to a score between 0

and 100, according to the following formula:

$$S = (V - Min) * 100 / (Max - Min),$$

Where S is score (rounded to three decimal points), V is the value of the measure, Min is the minimum cutoff value and Max is the maximum cutoff value.

The loss severity score would be the weighted average of these scores. Table 10 shows cutoff values and weights for these measures. The loss severity score would not be less than 0 or more than 100 under the proposal.

TABLE 10—CUTOFF VALUES AND WEIGHTS FOR LOSS SEVERITY SCORE MEASURES

Scorecard measures	Cutoff values		Weight (percent)
	Minimum	Maximum	
Potential Losses/Total Domestic Deposits (Loss Severity Measure) .....	0.0	30.1	50
Secured Liabilities/Total Domestic Deposits .....	0.0	75.7	50

In the example in Table 11, Bank A's loss severity score would be 36.04.

TABLE 11—LOSS SEVERITY SCORE FOR BANK A

Scorecard measures	Ratio	Score	Weight (percent)	Weighted score
Potential Losses/Total Domestic Deposits (Loss severity measure) .....	15.20	50.50	50	25.25
Secured Liabilities/Total Domestic Deposits .....	16.34	21.59	50	10.79
Total Loss Severity Score .....	.....	.....	.....	36.04

Similar to the performance score, the loss severity score could be adjusted, up or down, by a maximum of 15 points, based on significant risk factors specific to the institution that are not adequately captured in the scorecard. The resulting score, however, could not be less than 0 or more than 100. The FDIC would use a process similar to the current large bank adjustment to determine the amount of the adjustment to the loss severity score.<sup>24</sup> This discretionary adjustment is discussed in more detail below.

3. Initial Base Assessment Rate

Under the proposal, once the performance and loss severity scores are calculated, and potentially adjusted, these scores would be converted to an initial base assessment rate using the following method:

First, the loss severity score would be converted into a loss severity measure that ranges from 0.8 (score of 5 or lower)

to 1.2 (score of 85 or higher). Scores that fall at or below the minimum cutoff of 5 would receive a loss severity measure of 0.8 and scores that fall at or above the maximum cutoff of 85 would receive a loss severity score of 1.2. Again, a linear interpolation would be used to convert loss severity scores between the cutoffs into a loss severity measure. The conversion would be made using the following formula:

$$\text{Loss Severity Measure} = 0.8 + [(\text{Loss Severity Score} - 5) \times 0.005]$$

For example, if Bank A's loss severity score is 36.04, its loss severity measure would be 0.96, calculated as follows:  $0.8 + [(36.04 - 5) * 0.005] = 0.96$ .

Next, the performance score would be multiplied by the loss severity measure to produce a total score (total score = performance score \* loss severity measure). Since the loss severity measure ranges from 0.8 to 1.2, the total score could be up to 20 percent higher

or lower than the performance score. The total score would be capped at 100 under the proposal and would be rounded to two decimal places. For example, if Bank A's performance score is 81.70 and its loss severity measure is 0.96, its total score would be 78.43, calculated as follows:

$$81.70 * 0.96 = 78.43$$

A large institution with a total score of 30 or lower would pay the minimum initial base assessment rate and an institution with a total score of 90 or greater would pay the maximum initial base assessment rate.<sup>25</sup> For total scores between 30 and 90, initial base assessment rates would rise at an increasing rate as the total score increased. The initial base assessment rate (in basis points) would be calculated according to the following formula (assuming that the maximum initial base assessment rate was 40 basis points higher than the minimum rate):<sup>26</sup>

<sup>24</sup> 12 CFR 327.9(d)(4) (2009).

<sup>25</sup> The score of 30 and 90 equals about the 20th and about the 97th percentile values, respectively,

based on scorecard results as of first quarter 2005 through fourth quarter 2006.

<sup>26</sup> The rate of increase in the initial base assessment rate is based on a statistical analysis of failure probabilities as described in Appendix 2.

$$Rate = \text{Minimum Rate} - 0.165289 + \left( 68.02027 \times \left( \frac{Score}{100} \right)^5 \right)$$

For example, if Bank A's total score were 78.43, and the minimum and maximum initial base assessment rates

were 10 basis points and 50 basis points, respectively, its initial base

assessment rate would be 30.02 basis points, calculated as follows:

$$(10 \text{ bps} - 0.165289) + \left( 68.02027 \times \left( \frac{78.43}{100} \right)^5 \right) = 30.02 \text{ basis points}^{27}$$

This calculation of an initial assessment rate is based on an approximated statistical relationship between an institution's total score and

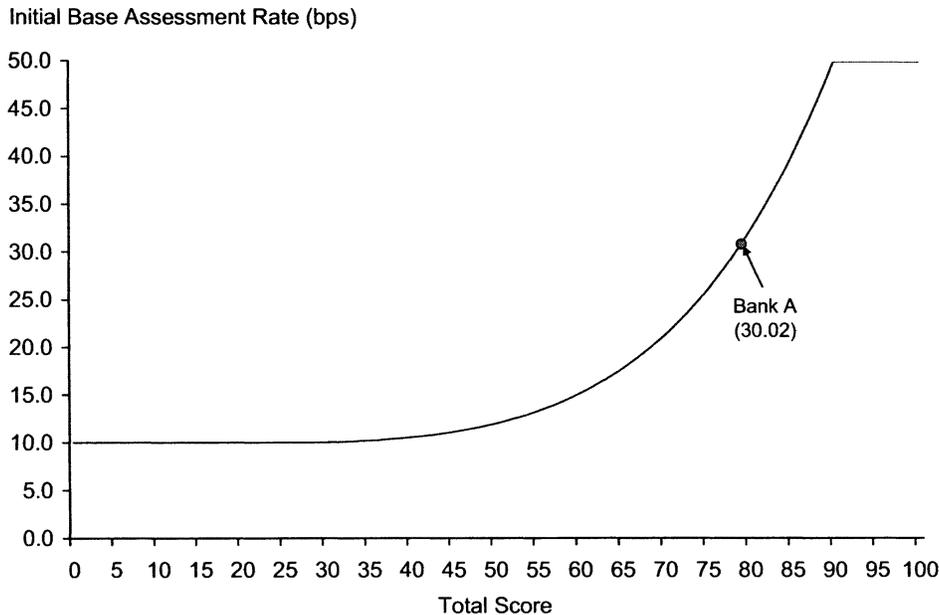
its estimated three-year cumulative failure probability.

Chart 2 illustrates the initial base assessment rate based on a range of total

scores and Bank A's assessment rate is indicated on the curve.

Chart 2

Proposed Initial Base Assessment Rates



The initial base assessment rate could be adjusted as a result of the unsecured debt adjustment, secured liability adjustment and brokered deposit adjustment (discussed below).

*B. Scorecard for Highly Complex Institutions*

As mentioned above, those institutions that are structurally and operationally complex or that pose

unique challenges and risks in case of failure (highly complex institutions) would have a different scorecard under the proposal. A "highly complex institution" would be defined as: (1) An insured depository institution (excluding a credit card bank) with greater than \$50 billion in total assets that is wholly owned by a parent company with more than \$500 billion in total assets, or wholly owned by one or

more intermediate parent companies that are wholly owned by a holding company with more than \$500 billion in assets, or (2) a processing bank and trust company with greater than \$10 billion in total assets, provided that the information required to calculate assessment rates as a highly complex institution is readily available to the FDIC.<sup>28</sup> Under the proposal, highly complex institutions would have a

<sup>27</sup> The initial base assessment rate would be rounded to two decimal points.

<sup>28</sup> A parent company would be defined as a bank holding company under the Bank Holding Company Act of 1956 or a savings and loan holding

company under the Home Owners' Loan Act. A credit card bank would be defined as a bank for which credit card plus securitized receivables exceed 50 percent of assets plus securitized receivables. A processing bank and trust company

would be defined as an institution whose last 3 years' non-lending interest income plus fiduciary revenues plus investment banking fees exceed 50 percent of total revenues (and last 3 years' fiduciary revenues are non-zero).

scorecard with measures tailored to the risks posed by these institutions, but the methodology involved would be the same for both scorecards.

The scorecard for highly complex institutions has four additional measures that do not appear in the scorecard for other large institutions (the senior bond spread, the institution's parent company's tangible common equity (TCE) ratio, the 10-day 99 percent Value at Risk (VaR), and the short-term funding to total assets ratio). These

measures were designed to measure vulnerability to changes in the market and would be incorporated into the calculation of a highly complex institution's initial base assessment rate because of the institution's greater involvement in market activities.

Appendix B describes these measures in detail and gives the source of the data used to calculate the measures.

The scorecard for highly complex institutions, like the scorecard for other large institutions, would contain a

performance component and a loss severity component. However, the performance score for highly complex institutions would contain an additional component—the market indicators component. Table 12 shows the scorecard measures and the possible range of scores that would be used for these institutions. Table 13 gives the weights associated with the four components of the performance scorecard for highly complex institutions.

TABLE 12—SCORECARD FOR HIGHLY COMPLEX INSTITUTIONS

Components	Scorecard measures	Score
CAMELS .....	<i>Weighted Average CAMELS</i> .....	25–100
Market Indicator .....	Senior Bond Spread .....	0–100
	Outlier Add-ons	
	Parent Company Tangible Common Equity (TCE) Ratio .....	30
	<i>Total Market Indicator score</i> .....	0–130
Ability to Withstand Asset-Related Stress	Tier 1 Common Capital Ratio (Tier 1 Common Capital/Total Average Assets less Disallowed Intangibles).	0–100
	Concentration Measure .....	0–100
	Higher Risk Concentrations; or Growth-Adjusted Portfolio Concentrations	
	Core Earnings/Average Total Assets .....	0–100
	Credit Quality Measure .....	0–100
	Criticized and Classified Items/Tier 1 Capital and Reserves Underperforming Assets/Tier 1 Capital and Reserves	
	10-day 99% VaR/Tier 1 Capital .....	0–100
	Subtotal .....	0–100
	Outlier Add-ons	
	Criticized and Classified Items/Tier 1 Capital and Reserves; or Underperforming Assets/Tier 1 Capital and Reserves	30
Higher Risk Concentrations Measure .....	30	
<i>Total ability to withstand asset-related stress score</i> .....	0–160	
Ability to Withstand Funding-Related Stress.	Core Deposits/Total Liabilities .....	0–100
	Unfunded Commitments/Total Assets .....	0–100
	Liquid Assets/Short-term Liabilities (liquidity coverage ratio) .....	0–100
	Short-term Funding/Total Assets .....	0–100
	Subtotal .....	0–100
	Outlier Add-ons	
	Short-term funding/Total Assets .....	30
<i>Total ability to withstand funding-related stress score</i> .....	0–130	
<i>Total Performance Score</i> .....	0–100	
Potential Loss Severity .....	Potential Losses/Total Domestic Deposits (loss severity measure) .....	0–100

TABLE 12—SCORECARD FOR HIGHLY COMPLEX INSTITUTIONS—Continued

Components	Scorecard measures	Score
	Secured Liabilities/Total Domestic Deposits .....	0–100
	Total loss severity score .....	0–100

TABLE 13—PERFORMANCE SCORE COMPONENTS AND WEIGHTS

Performance score components	Weight (percent)
CAMELS Rating .....	20
Market Indicators .....	10
Ability to Withstand Asset-Related Stress .....	50
Ability to Withstand Funding-Related Stress .....	20

The additional component, the market indicator component, would be added to the performance scorecard for highly complex institutions. The market indicator component contains only one measure, the senior bond spread score, and one outlier add-on. The FDIC would use the senior bond spread because this measure can be compared consistently across institutions. The senior bond spread would be converted linearly to a score between 0 and 100. The minimum and maximum cutoff values for the

market indicator measure are shown in Table 14. The market indicator component score would be adjusted by up to 30 points if the institution’s parent company’s tangible common equity (TCE) ratio fell below 4 percent since the market generally perceives a parent company to be vulnerable if its TCE is less than 4 percent. Including the outlier add-on, the market indicator component score could be as high as 130 points.

TABLE 14—CUTOFF VALUES AND WEIGHT FOR MARKET INDICATOR MEASURE

Scorecard measures	Cutoff values		Weight (percent)
	Minimum	Maximum	
Senior Bond Spread .....	0.6	3.8	100

The scorecard for highly complex institutions adds one additional factor to the ability to withstand asset-related stress component—the 10-day 99 percent Value at Risk (VaR)/Tier 1

capital—and one additional factor to the ability to withstand funding-related stress component—the short-term funding to total assets ratio. Table 15 and Table 16 show cutoff values and

weights for ability to withstand asset-related stress measures and ability to withstand funding-related stress measures, respectively.

TABLE 15—CUTOFF VALUES AND WEIGHTS FOR ABILITY TO WITHSTAND ASSET-RELATED STRESS MEASURES

Scorecard measures	Cutoff values		Weight (percent)
	Minimum	Maximum	
Tier 1 Common Capital Ratio .....	5.8	12.9	10
Concentration Measure:			35
Higher Risk Concentrations; or .....	0.0	3.2	
Growth-Adjusted Portfolio Concentrations .....	7.6	154.7	
Core Earnings/Average Total Assets .....	0.0	2.3	10
Credit Quality Measure:			35
Criticized and Classified Items to Tier 1 Capital and Reserves; or .....	6.5	100.0	
Underperforming Assets/Tier 1 Capital and Reserves .....	2.3	35.1	
10-day 99 VaR/Tier 1 Capital .....	0.1	0.5	10

TABLE 16—CUTOFF VALUES AND WEIGHTS FOR ABILITY TO WITHSTAND FUNDING-RELATED STRESS MEASURES

Scorecard measures	Cutoff values		Weight (percent)
	Minimum	Maximum	
Core Deposits/Total Liabilities .....	3.2	79.1	30
Unfunded Commitments/Total Assets .....	0.3	42.2	30
Liquid Assets/Short-term Liabilities (liquidity coverage ratio) .....	5.6	170.9	20
Short-term Funding/Total Assets .....	0.0	19.1	20

The scorecard for highly complex institutions also adds an additional outlier add-on. The ability to withstand funding-related stress component score

for highly complex institutions would be adjusted by 30 points if the ratio of short-term funding to total assets

exceeded 26.9 percent.<sup>29</sup> The use of

<sup>29</sup> Historical analysis shows that a significant amount of short-term funding can increase the risk profile of an institution. External funding sources

short-term funding has proved to be highly unstable and the FDIC has found an increased vulnerability, particularly for institutions that are active participants, when there is a heavy reliance on this type of funding. Including the outlier add-on, the ability to withstand funding-related stress component score for highly complex institutions could be as high as 130 points.

To calculate the performance score for highly complex institutions, the weighted average CAMELS score, the market indicators score, the ability to withstand asset-related stress score, and the ability to withstand funding-related stress score would be multiplied by their weights and the results would be summed to arrive at the performance score. The score would be capped at 100 under the proposal. The loss severity score for highly complex institutions would be calculated the same way as the loss severity score for other large institutions.

As is the case for other large institutions, the performance score and the loss severity score for highly complex institutions could be adjusted, up or down, by maximum of 15 points each, based upon significant risk factors that are not adequately captured in the scorecard. The resulting scores, however, could not be less than 0 or more than 100. The FDIC would use a process similar to the current large bank adjustment to determine the amount of any adjustments.<sup>30</sup> This discretionary adjustment is discussed in more detail below.

The initial base assessment rate for highly complex institutions would be calculated from the total score in the same manner as for other large institutions as described above. As in the case of other large institutions, the initial base assessment rate could also be adjusted as a result of the unsecured debt adjustment, the secured liability adjustment, and the brokered deposit adjustment (discussed below).

### C. Large Bank Adjustment to the Performance Score and Loss Severity Score

Under current rules, large institutions and insured branches of foreign banks

can be a critical source of liquidity but short-term funding exposes an institution to near-term price risk and rollover risk. These risks increase for an institution during periods of market disruption or when the institution itself is experiencing financial distress. The add-on is triggered when the level of short-term funding to total assets ratio exceeds 26.9%. This is the 95th percentile of this measure among large institutions based upon data from the period between the third quarter of 1999 and the second quarter of 2009.

<sup>30</sup> 12 CFR 327.9(d)(4)(2009).

within Category 1 are subject to an assessment rate adjustment (the large bank adjustment). The large bank adjustment was designed to preserve consistency in the relative risk rankings of large institutions as indicated by assessment rates, to ensure fairness among all large institutions, and to ensure that assessment rates take into account all available information that is relevant to the FDIC's risk-based assessment decision. The FDIC proposes that a large bank adjustment be retained that would be imposed in the same manner (and subject to the same notice requirements) as under the current rule.<sup>31</sup>

As proposed, the FDIC could adjust the performance score and/or the loss severity score for all large institutions and highly complex institutions, up or down, by a maximum of 15 points each, based upon significant risk factors that are not adequately captured in the scorecard. In determining whether to make a large bank adjustment, the FDIC may consider such information as financial performance and condition information and other market or supervisory information. The FDIC would also consult with an institution's primary Federal regulator and, for state chartered institutions, state banking supervisor. Appendix E lists some, but not all, criteria that could be considered in determining whether or not a discretionary adjustment is necessary.

In general, the proposed adjustments to the performance and loss severity scores would have a proportionally greater effect on the assessment rate of those institutions with a higher total score. The effect of an upward adjustment to a score on the institution's assessment rate would be calculated as

$$A_u = 68.02027 \times \left[ \left( \frac{P+C}{100} \right)^5 - \left( \frac{P}{100} \right)^5 \right]$$

and the effect of a downward adjustment to a score on the institution's assessment rate would be

$$A_d = 68.02027 \times \left[ \left( \frac{P}{100} \right)^5 - \left( \frac{P-C}{100} \right)^5 \right],$$

where  $A_u$  is an increase in the assessment rate,  $A_d$  is a decrease in the assessment rate,  $C$  is the amount of upward adjustment to score, and  $P$  is pre-adjustment score.

Notifications involving an upward adjustment to an institution's assessment rate would be made in advance of implementing such an adjustment so that the institution has an

opportunity to respond to or address the FDIC's rationale for proposing an upward adjustment. Adjustments would be implemented after considering the institution's response to this notification along with any subsequent changes either to the inputs or other risk factors that relate to the FDIC's decision.

The FDIC acknowledges the need to clarify and make technical changes to its adjustment guidelines for large institutions to ensure consistency with this rulemaking.<sup>32</sup>

### D. Liability-Based Adjustments

The proposed rule would continue to allow for adjustments to an institution's initial base assessment rate as a result of certain long-term unsecured debt, secured liabilities and brokered deposits. These adjustments are currently provided for in the 2009 assessments rule, except that the brokered deposit adjustment currently applies only to institutions in Risk Categories II, III and IV. The proposed rule would extend the brokered deposit adjustment to all large institutions since the adjusted brokered deposit ratio (which took brokered deposits and growth into account for large Risk Category I institutions) would no longer apply. The unsecured debt adjustment, secured liability adjustment and brokered deposit adjustment would be applicable to both large institutions and highly complex institutions under the proposal.

### E. Calculation of Total Assessment Rate

After making the adjustments just described, the resulting assessment rate would be the total assessment rate. Under the proposal, unlike the current rule for both large and small institutions, a large institution's total assessment rate could not be more than 50 percent lower than its initial base assessment rate. This change ensures that all institutions would pay assessments even if the minimum initial base assessment rate is set at 5 basis points or less.

### F. Updating Scorecard

The FDIC proposes that it have the flexibility to update the minimum and maximum cutoff values and weights used in each scorecard annually, without notice-and-comment rulemaking. In particular, the FDIC could add new data from each year to its analysis and could, from time to time, exclude some earlier years from its analysis. Updating the minimum and maximum cutoff values and weights would allow the FDIC to use the most

<sup>31</sup> 12 CFR 327.9(d)(4) (2009).

<sup>32</sup> 72 FR 27122 (May 14, 2007).

recent data, thereby improving the accuracy of the scorecard method.

On the other hand, if, as a result of its review and analysis, the FDIC concludes that *additional* or *alternative* measures should be used to determine risk-based assessments or that a new method should be used to differentiate risk among large institutions and highly complex institutions, such changes would be made through notice-and-comment rulemaking.

Financial ratios for any given quarter would continue to be calculated from the report of condition filed by each institution or data collected through the FDIC's LIDI program as of the last day of the quarter.<sup>33</sup> CAMELS component rating changes would continue to be effective as of the date that the rating

change is transmitted to the institution for purposes of determining assessment rates.<sup>34</sup>

**IV. Assessment Rates**

As discussed above, the FDIC proposes a wider range of assessment rates than under the current assessment system. To maintain approximately the same total revenue under the proposed rule as under the current system, the FDIC proposes that the Board adopt new initial and total base assessment rate schedules set out in Tables 17 and 18, effective January 1, 2011.

Under the proposed rule, the range of initial base assessment rates for small institutions and insured branches of foreign banks in Risk Category I would be uniformly 2 basis points lower than under the current assessment system;

the initial base assessment rate for institutions in Risk Category II would be unchanged; while the proposed initial base assessment rate for small institutions and insured branches in Risk categories III and IV would be somewhat higher. For large and highly complex institutions the minimum rate in the proposed range of rates would be 2 basis points lower than the current Risk Category I minimum assessment rate and the maximum rate in the range would be slightly higher than current maximum Risk Category IV assessment rates.<sup>35</sup>

Actual total assessment rates will be set uniformly 3 basis points higher than the proposed rates in accordance with the Amended Restoration Plan that the FDIC adopted on September 29, 2009.<sup>36</sup>

**TABLE 17—PROPOSED INITIAL AND TOTAL BASE ASSESSMENT RATES FOR SMALL INSTITUTIONS AND INSURED BRANCHES OF FOREIGN BANKS**

	Risk category I	Risk category II	Risk category III	Risk category IV
Initial base assessment rate .....	10–14	22	34	50
Unsecured debt adjustment .....	– 5–0	– 5–0	– 5–0	– 5–0
Secured liability adjustment .....	0–7	0–11	0–17	0–25
Brokered deposit adjustment .....	.....	0–10	0–10	0–10
<b>Total Base Assessment Rate .....</b>	<b>5–21</b>	<b>17–43</b>	<b>29–61</b>	<b>45–85</b>

All amounts for all risk categories are in basis points annually. Total base rates that are not the minimum or maximum rate will vary between these rates. All rates shown would increase 3 basis points on January 1, 2011, pursuant to the FDIC Amended Restoration Plan adopted on September 29, 2009. 74 FR 51062 (Oct. 2, 2009).

**TABLE 18—PROPOSED INITIAL AND TOTAL BASE ASSESSMENT RATES FOR LARGE INSTITUTIONS**

	Large institutions
Initial base assessment rate .....	10–50
Unsecured debt adjustment .....	– 5–0
Secured liability adjustment .....	0–25
Brokered deposit adjustment .....	0–10
<b>Total Base Assessment Rate .....</b>	<b>5–85</b>

All amounts are in basis points annually. Total base rates that are not the minimum or maximum rate will vary between these rates. All rates shown would increase 3 basis points on January 1, 2011, pursuant to the FDIC Amended Restoration Plan adopted on September 29, 2009. 74 FR 51062 (Oct. 2, 2009).

Based upon the analysis and projections below, the FDIC has concluded that the proposed assessment rate structure (including the previously announced 3 basis point uniform increase in assessment rates beginning January 1, 2011) should satisfy the FDIC's revenue and liquidity needs.

Under the proposal, for the fourth quarter 2009 assessment period, total base assessment rates would have been lower for about 52 percent of large institutions and 76 percent of small institutions.<sup>37</sup> The rates would have been higher for about 48 percent of large institutions and 9 percent of small

institutions. The rates would have remained the same for 15 percent of small institutions.

*Fund Balance and Reserve Ratio Projections*

In September 2009, the FDIC projected that both the Fund balance

<sup>33</sup> Reports of condition include Reports of Income and Condition and Thrift Financial Reports.

<sup>34</sup> Pursuant to existing supervisory practice, the FDIC does not assign a different component rating from that assigned by an institution's primary federal regulator, even if the FDIC disagrees with a CAMELS component assigned by an institution's primary federal regulator, unless: (1) The disagreement over the component rating also involves a disagreement over a CAMELS composite rating; and (2) the disagreement over the CAMELS

composite rating is not a disagreement over whether the CAMELS composite rating should be a 1 or a 2. The FDIC has no plans to alter this practice.

<sup>35</sup> 12 U.S.C. 1817(b)(2)(D) provides that "No insured depository institution shall be barred from the lowest risk category solely because of size."

<sup>36</sup> 74 FR 51062 (Oct. 2, 2009). Under current rules, the FDIC has discretion to increase or decrease assessment rates in effect up to 3 basis points above or below total base assessment rates

without the need for additional rulemaking. The proposed rule would not affect this provision.

<sup>37</sup> For the purpose of this analysis, large institutions are those with total assets of \$10 billion or greater as of December 31, 2009. The estimates in the text regarding the effect of the proposal on assessment rates, the effect on industry capital and earnings discussed later in the text and the Regulatory Flexibility Act analysis discussed later in the text, are based in part on approximations of a few risk measures.

and the reserve ratio as of September 30, 2009, would be negative, owing, in part, to an increase in provisioning for anticipated failures. The FDIC also projected the Fund balance and reserve ratio for each quarter over the next several years using the then most recently available information on expected failures and loss rates and statistical analyses of trends in CAMELS downgrades, failure rates and loss rates. The FDIC projected that, over the period 2009 through 2013, the Fund could incur approximately \$100 billion in failure costs; the FDIC projected that most of these costs would occur in 2009 and 2010.

Partly as a result of these projections, the FDIC increased risk-based assessment rates uniformly by 3 basis points effective January 1, 2011. Despite this increase, the FDIC projected that the Fund balance would become significantly negative in 2010 and would remain negative until first quarter 2013. According to these projections, the reserve ratio would return to the statutorily mandated minimum reserve ratio of 1.15 percent in the first quarter of 2017.

As projected, the Fund balance and reserve ratio as of September 30, 2009, and December 31, 2009, were negative. (The Fund balance on December 31, 2009 was negative \$20.9 billion; the reserve ratio was -0.39 percent.) In February 2010, the FDIC reexamined its projections using the most recently available information on expected failures and loss rates, and statistical analyses of trends in CAMELS downgrades, failure rates and loss rates. This reexamination resulted in no material changes to the FDIC's projections. However, these projections are subject to considerable uncertainty. Losses could be less than or exceed projected amounts, for example, if conditions affecting the national or regional economies, prove less or more severe than is currently anticipated.

#### *Effect on Industry Capital and Earnings*

The proposed changes involve increases in premiums for some institutions and reductions in premiums for other institutions. Because overall revenue remains almost constant, the effect on aggregate earnings and capital is small. Projections show that imposition of the new premiums will increase aggregate capital by 2 one-hundredths of one percent (0.02 percent) over one year. For 6,042 institutions, assessment rates would decrease and earnings and capital would increase; for 771 institutions, assessment rates would increase and earnings and capital would decline. For

institutions whose initial earnings are positive, the change in premiums will increase earnings by an average of 0.87 percent (on an asset weighted basis). For institutions whose initial earnings are negative, the change in premiums will increase losses by an average of 0.85 percent (on an asset weighted basis).<sup>38</sup>

Imposition of the proposed assessment rates would make a critical difference for two institutions, whose tier 1 capital ratio would fall below 2 percent over a one-year horizon (assuming the proposed rule were adopted for 2010). No institution's equity-to-capital ratio would fall below 4 percent over a one-year horizon.<sup>39</sup>

#### **V. Effective Date**

January 1, 2011.

#### **VI. Request for Comments**

The FDIC seeks comment on every aspect of this proposed rule. In particular, the FDIC seeks comment on the questions set out below. The FDIC asks that commenters include reasons for their positions.<sup>40</sup> The FDIC specifically requests comment on the following:

##### *A. Questions for Future Rulemakings*

As mentioned above, the FDIC seeks input on additional measures that could

<sup>38</sup> The proposed changes to assessment rates would not take effect until January 1, 2011. For two reasons, the analysis in the text examines the effect on earnings and capital had proposed rates been in effect on January 1, 2010. First, it is difficult to project 2011 institution income so far in advance. Second, as discussed in the text, because overall assessment revenue under the proposed system would remain approximately the same as the current system, the effect on earnings and capital is small for almost all institutions. This conclusion holds true for 2011, as well, because both current and proposed assessment rates will increase uniformly by three basis points beginning January 1, 2011. (A detailed analysis of the projected effects of the payment of proposed assessment on the capital and earnings of insured institutions is contained in Appendix 3.)

<sup>39</sup> In setting assessment rates, the FDIC's Board of Directors of the FDIC is authorized to set assessments for insured depository institutions in such amounts as the Board of Directors may determine to be necessary. 12 U.S.C. 1817(b)(2)(A). In so doing, the Board shall consider: (1) The estimated operating expenses of the DIF; (2) the estimated case resolution expenses and income of the DIF; (3) the projected effects of the payment on the capital and earnings of insured depository institutions; (4) the risk factors and other factors taken into account pursuant to 12 U.S.C. 1817(b) (1) under the risk-based assessment system, including the requirement under such paragraph to maintain a risk-based system; and (5) any other factors the Board of Directors may determine to be appropriate. 12 U.S.C. 1817(b)(2)(B). As reflected in the text, in making its projections of the Fund balance and liquidity needs, and in making its recommendations regarding assessment rates, the Board has taken into account these statutory factors.

<sup>40</sup> The FDIC may not address all of the questions posed in the current rulemaking, but may consider the information gathered in future actions.

be incorporated into the assessment system in future rulemakings.

a. The FDIC would like to factor into the scorecard credit, liquidity, market, and interest rate stress tests. How should these stress tests be factored into the scorecard? What methodology and assumptions should be used?

b. Underwriting is a key determinant of credit quality. The FDIC would like to develop metrics to measure underwriting quality. How could underwriting quality best be measured?

c. A high level of counterparty risk can significantly increase an institution's ability to withstand stress. How could counterparty risk best be measured?

d. A high level of market risk can significantly increase an institution's ability to withstand stress. How could market risk best be measured?

e. How could liquidity risk best be measured?

f. How should the exposure of individual banks to systemic risk be measured? What activities and behavior constitute exposure to systemic risk?

g. How is the capability of risk management best assessed?

h. Should the FDIC review the assessment system applicable to small institutions to determine whether improvements, including improvements analogous to those being proposed for the large institution assessment system, should be made to the assessment system used for small institutions?

##### *B. Questions About the Proposal*

###### *1. Deposit Insurance Pricing System:*

(a) Should the risk categories be eliminated as proposed?

(b) Should the two scorecards be combined?

(c) Should highly complex institutions be defined as proposed?

(d) Should the risk measures, particularly the components of the high risk concentrations measure, be defined as proposed?

(e) Should the performance score and loss severity score be combined as proposed?

(f) Should the initial base assessment rate be calculated as proposed?

###### *2. Performance Scorecard:*

(a) Are the proposed weights assigned to performance score components and measures appropriate?

(b) Are the cut-off values for the risk measures and the outlier add-ons appropriate?

(c) Should any other measures be added? Should any measures be removed or replaced?

(d) For the growth-adjusted portfolio concentration measure, are the risk weights assigned to each portfolio as described in Appendix C appropriate?

(e) For the higher-risk concentration measure, should concentrations in other portfolios be considered?

(f) Should purchased impaired loans under SOP 03-3 be excluded from the definition of criticized and classified items or underperforming assets?

(g) Should the liquidity coverage ratio be computed as proposed?

(h) Are the outlier add-ons appropriate measures? Is the score addition for add-ons appropriate?

(i) Is the size of the discretionary adjustment to the performance score appropriate?

### 3. Loss Severity Scorecard:

(a) Are asset haircuts, runoff, and secured liability assumptions for the loss severity measure as described in Appendix D appropriate?

(b) Are asset adjustments due to liability runoff and capital reductions as described in Appendix D applied appropriately?

(c) Are the proposed weights assigned to loss severity measures appropriate?

(d) Are cut-off values for risk measures and outlier add-ons appropriate?

(e) Should any other measures be added? Should any measures be removed or replaced?

(f) Is the size of the discretionary adjustment to the loss severity score appropriate?

### 4. Assessment Rate Schedule:

(a) Should the entire proposed assessment rate schedule be adjusted to make it revenue neutral overall?

(b) Is the basis point range for assessments appropriate?

### 5. Regulatory Matters:

(a) What is the extent of regulatory burden with implementation of the proposed deposit insurance pricing system?

(b) Are the requirements in the proposed regulation clearly stated? If not, how could the regulation be more clearly stated?

(c) Does the proposed regulation contain language or jargon that is not clear? If so, which language requires clarification?

## VII. Regulatory Analysis and Procedure

### A. Solicitation of Comments on Use of Plain Language

Section 722 of the Gramm-Leach-Bliley Act, Public Law 106-102, 113 Stat. 1338, 1471 (Nov. 12, 1999), requires the Federal banking agencies to use plain language in all proposed and final rules published after January 1,

2000. The FDIC invites your comments on how to make this proposal easier to understand. For example:

- Has the FDIC organized the material to suit your needs? If not, how could this material be better organized?

- Are the requirements in the proposed regulation clearly stated? If not, how could the regulation be more clearly stated?

- Does the proposed regulation contain language or jargon that is not clear? If so, which language requires clarification?

- Would a different format (grouping and order of sections, use of headings, paragraphing) make the regulation easier to understand? If so, what changes to the format would make the regulation easier to understand?

- What else could the FDIC do to make the regulation easier to understand?

### B. Regulatory Flexibility Act

The Regulatory Flexibility Act (RFA) requires that each Federal agency either certify that a proposed rule would not, if adopted in final form, have a significant economic impact on a substantial number of small entities or prepare an initial regulatory flexibility analysis of the rule and publish the analysis for comment.<sup>41</sup> Certain types of rules, such as rules of particular applicability relating to rates or corporate or financial structures, or practices relating to such rates or structures, are expressly excluded from the definition of “rule” for purposes of the RFA.<sup>42</sup> The proposed rule relates directly to the rates imposed on insured depository institutions for deposit insurance, and to the risk-based assessment system components that measure risk and weigh that risk in determining each institution’s assessment rate, and includes technical and other changes to the FDIC’s assessment regulations. Nonetheless, the FDIC is voluntarily undertaking an initial regulatory flexibility analysis of the proposed rule for publication.

As of December 31, 2009, of the 8,012 insured commercial banks and savings associations, there were 4,427 small insured depository institutions as that term is defined for purposes of the RFA (*i.e.*, those with \$175 million or less in assets).

For purposes of this analysis, whether the FDIC were to collect needed

assessments under the existing rule or under the proposed rule, the total amount of assessments collected would be the same. The FDIC’s total assessment needs are driven by statutory requirements and by the FDIC’s aggregate insurance losses, expenses, investment income, and insured deposit growth, among other factors. Given the FDIC’s total assessment needs, the proposed rule would merely alter the distribution of assessments among insured institutions. Using data as of December 31, 2009, the FDIC calculated the total assessments that would be collected under the base rate schedule in the proposed rule.

The economic impact of the final rule on each small institution for RFA purposes (*i.e.*, institutions with assets of \$175 million or less) was then calculated as the difference in basis points and annual assessments under the proposed rule compared to the existing rule, assuming the same total assessments collected by the FDIC from the banking industry.<sup>43 44</sup>

Based on the December 2009 data, under the proposed rule, the change in the assessment system would result in lower assessments for the majority of small institutions. Small institutions would experience an average drop of 1.39 basis points in their assessment rates under the proposed rule. More than 86 percent of these institutions would face a lower assessment rate, with 76 percent of them being charged 1 to 2 basis points lower than the current pricing rule. Of the total 4,427 small institutions, only 13 percent would experience an increase and only 173 institutions would experience an assessment rate increase of more than 2 basis points. These figures indicate that the proposed rule will have a positive economic impact for a substantial number of small insured institutions. Table 19 below sets forth the results of the analysis in more detail.

<sup>43</sup> Throughout this regulatory flexibility analysis (unlike the rest of the final rule), a “small institution” refers to an institution with assets of \$175 million or less.

<sup>44</sup> The proposed rule would not go into effect until January 1, 2011. Under the existing assessment system and under the proposed rule, assessment rates would increase uniformly by three basis points beginning on that date. Because the increase is uniform in both cases, the analysis in the text, which compares current assessment rates with proposed base assessment rates, should apply equally to 2011.

<sup>41</sup> See 5 U.S.C. 603, 604 and 605.

<sup>42</sup> 5 U.S.C. 601.

TABLE 19—CHANGE IN BASIS POINT ASSESSMENTS UNDER THE PROPOSED RULE

Change in basis point assessments	Number of institutions	Percent of institutions
More than -2 basis points lower .....	114	2.58
-2 to -1 basis points lower .....	3,377	76.28
-1 to 0 basis points lower .....	356	8.04
0 to 1 basis points higher .....	243	5.49
1 to 2 basis points higher .....	164	3.70
More than 2 basis points higher .....	173	3.91
Total .....	4,427	100.00

The FDIC performed a similar analysis to determine the impact on profits for small institutions. Based on

December 2009 data, under the final rule, 96 percent of the 3,039 small institutions with reported profits would

experience a positive change in their annual profits. Table 20 sets forth the results of the analysis in more detail.

TABLE 20—CHANGE IN ASSESSMENTS UNDER THE PROPOSAL AS A PERCENTAGE OF PROFIT \*

Change in assessments as a percentage of profit	Number of institutions	Percent of institutions
More than .2 percent lower .....	18	0.59
.1 to .2 percent lower .....	18	0.59
.05 to .1 percent lower .....	41	1.35
0 to .05 percent lower .....	2,841	93.48
0 to 1 percent higher .....	121	3.98
Total .....	3,039	100.00

\* Institutions with negative or no profit were excluded. These institutions are shown separately in the next table.

Of those small institutions with reported profits, less than 4 percent would have experienced a decrease in their profits under the proposed rule. More than 96 percent of these small institutions would have an increase in their profits. Again, these figures indicate a positive economic impact on

profits for the majority of small insured institutions.

Table 21 excludes small institutions that either show no profit or show a loss, because a percentage cannot be calculated. The FDIC analyzed the effect of the proposed rule on these institutions by determining the annual assessment change that would result.

Table 21 below shows that only 2.81 percent (39) of the 1,388 small insured institutions in this category would experience an increase in annual assessments of \$10,000 or more. More than 10 percent of these institutions would experience a decrease of \$5,000 or more.

TABLE 21—CHANGE IN ASSESSMENTS UNDER THE PROPOSED RULE FOR INSTITUTIONS WITH NEGATIVE OR NO REPORTED PROFIT

Change in assessments	Number of institutions	Percent of institutions
\$5,000–\$10,000 decrease .....	147	10.59
\$1,000–\$5,000 decrease .....	468	33.72
\$0–\$1,000 decrease .....	334	24.06
\$0–\$1,000 increase .....	151	10.88
\$1,000–\$10,000 increase .....	249	17.94
\$10,000 increase or more .....	39	2.81
Total .....	1,388	100.00

The proposed rule does not directly impose any “reporting” or “recordkeeping” requirements within the meaning of the Paperwork Reduction Act. The compliance requirements for the proposed rule would not exceed existing compliance requirements for the present system of FDIC deposit insurance assessments, which, in any event, are governed by separate regulations.

The FDIC is unaware of any duplicative, overlapping or conflicting Federal rules.

The initial regulatory flexibility analysis set forth above demonstrates that the proposed rule would not have a significant economic impact on a substantial number of small institutions

within the meaning of those terms as used in the RFA.<sup>45</sup>

#### C. Paperwork Reduction Act

No collections of information pursuant to the Paperwork Reduction Act (44 U.S.C. 3501 *et seq.*) are contained in the proposed rule.

<sup>45</sup> 5 U.S.C. 605.

D. The Treasury and General Government Appropriations Act, 1999—Assessment of Federal Regulations and Policies on Families

The FDIC has determined that the proposed rule will not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, enacted as part of the Omnibus Consolidated and Emergency Supplemental Appropriations Act of 1999 (Pub. L. 105–277, 112 Stat. 2681).

List of Subjects in 12 CFR Part 327

Bank deposit insurance, Banks, Banking, Savings associations.

For the reasons set forth in the preamble, the FDIC proposes to amend chapter III of title 12 of the Code of Federal Regulations as follows:

PART 327—ASSESSMENTS

1. The authority citation for part 327 continues to read as follows:

Authority: 12 U.S.C. 1441, 1813, 1815, 1817–1819, 1821; Sec. 2101–2109, Pub. L. 109–171, 120 Stat. 9–21, and Sec. 3, Public Law 109–173, 119 Stat. 3605.

2. In § 327.4, revise paragraphs (c) and (f) to read as follows:

§ 327.4 Assessment rates.

\* \* \* \* \*

(c) Requests for review. An institution that believes any assessment risk assignment provided by the Corporation pursuant to paragraph (a) of this section is incorrect and seeks to change it must submit a written request for review of that risk assignment. An institution cannot request review through this process of the CAMELS ratings assigned by its primary Federal regulator or challenge the appropriateness of any such rating; each Federal regulator has established procedures for that purpose. An institution may also request review of a determination by the FDIC to assess the institution as a large or a small institution (12 CFR 327.9(d)(9)) or a determination by the FDIC that the institution is a new institution (12 CFR 327.9(d)(10)). Any request for review must be submitted within 90 days from the date the assessment risk assignment being challenged pursuant to paragraph (a) of this section appears on the institution's quarterly certified statement invoice. The request shall be submitted to the Corporation's Director of the Division of Insurance and Research in Washington, DC, and shall include documentation sufficient to support the change sought by the institution. If additional information is requested by the Corporation, such information shall be provided by the

institution within 21 days of the date of the request for additional information. Any institution submitting a timely request for review will receive written notice from the Corporation regarding the outcome of its request. Upon completion of a review, the Director of the Division of Insurance and Research (or designee) or the Director of the Division of Supervision and Consumer Protection (or designee), as appropriate, shall promptly notify the institution in writing of his or her determination of whether a change is warranted. If the institution requesting review disagrees with that determination, it may appeal to the FDIC's Assessment Appeals Committee. Notice of the procedures applicable to appeals will be included with the written determination.

\* \* \* \* \*

(f) Effective date for changes to risk assignment. Changes to an insured institution's risk assignment resulting from a supervisory ratings change become effective as of the date of written notification to the institution by its primary Federal regulator or state authority of its supervisory rating (even when the CAMELS component ratings have not been disclosed to the institution), if the FDIC, after taking into account other information that could affect the rating, agrees with the rating. If the FDIC does not agree, the FDIC will notify the institution of the FDIC's supervisory rating; resulting changes to an insured institution's risk assignment become effective as of the date of written notification to the institution by the FDIC.

\* \* \* \* \*

3. In § 327.8, revise paragraphs (g), (h), (i), (m), (n), (o), (p), (q), and (r), and add paragraphs (t), (u) and (v) to read as follows:

§ 327.8 Definitions.

\* \* \* \* \*

(g) Small Institution. An insured depository institution with assets of less than \$10 billion as of December 31, 2006, and an insured branch of a foreign institution, shall be classified as a small institution. If, after December 31, 2006, an institution classified as large under paragraph (h) of this section (other than an institution classified as large for purposes of § 327.9(d)(8)) reports assets of less than \$10 billion in its quarterly reports of condition for four consecutive quarters, the FDIC will reclassify the institution as small beginning the following quarter.

(h) Large Institution. An institution classified as large for purposes of § 327.9(d)(9) or an insured depository institution with assets of \$10 billion or

more as of December 31, 2006 (other than an insured branch of a foreign bank or a highly complex institution) shall be classified as a large institution. If, after December 31, 2006, an institution classified as small under paragraph (g) of this section reports assets of \$10 billion or more in its quarterly reports of condition for four consecutive quarters, the FDIC will reclassify the institution as large beginning the following quarter.

(i) Highly Complex Institution. A highly complex institution is an insured depository institution with greater than \$50 billion in total assets that is not a credit card bank and is wholly owned by a parent company with more than \$500 billion in total assets, or wholly owned by one or more intermediate parent companies that are wholly owned by a holding company with more than \$500 billion in assets, or a processing bank and trust company with greater than \$10 billion in total assets, provided that the information required to calculate assessment rates as a highly complex institution is readily available to the FDIC. If, after December 31, 2010, an institution classified as highly complex falls below \$50 billion in total assets in its quarterly reports of condition for four consecutive quarters, or its parent company or companies fall below \$500 billion in total assets for four consecutive quarters, or a processing bank and trust company falls below \$10 billion in total assets in its quarterly reports of condition for four consecutive quarters, the FDIC will reclassify the institution beginning the following quarter.

\* \* \* \* \*

(m) Established depository institution. An established insured depository institution is a bank or savings association that has been federally insured for at least five years as of the last day of any quarter for which it is being assessed.

(1) Merger or consolidation involving new and established institution(s). Subject to paragraphs (m)(2), (3), (4), and (5) of this section and § 327.9(d)(10)(iii), (iv), when an established institution merges into or consolidates with a new institution, the resulting institution is a new institution unless:

(i) The assets of the established institution, as reported in its report of condition for the quarter ending immediately before the merger, exceeded the assets of the new institution, as reported in its report of condition for the quarter ending immediately before the merger; and

(ii) Substantially all of the management of the established

institution continued as management of the resulting or surviving institution.

(2) *Consolidation involving established institutions.* When established institutions consolidate, the resulting institution is an established institution.

(3) *Grandfather exception.* If a new institution merges into an established institution, and the merger agreement was entered into on or before July 11, 2006, the resulting institution shall be deemed to be an established institution for purposes of this part.

(4) *Subsidiary exception.* Subject to paragraph (m)(5) of this section, a new institution will be considered established if it is a wholly owned subsidiary of:

(i) A company that is a bank holding company under the Bank Holding Company Act of 1956 or a savings and loan holding company under the Home Owners' Loan Act, and:

(A) At least one eligible depository institution (as defined in 12 CFR 303.2(r)) that is owned by the holding company has been chartered as a bank or savings association for at least five years as of the date that the otherwise new institution was established; and

(B) The holding company has a composite rating of at least "2" for bank holding companies or an above average or "A" rating for savings and loan holding companies and at least 75 percent of its insured depository institution assets are assets of eligible depository institutions, as defined in 12 CFR 303.2(r); or

(ii) An eligible depository institution, as defined in 12 CFR 303.2(r), that has been chartered as a bank or savings association for at least five years as of the date that the otherwise new institution was established.

(5) *Effect of credit union conversion.* In determining whether an insured depository institution is new or established, the FDIC will include any period of time that the institution was a federally insured credit union.

(n) *Risk assignment.* For all small institutions and insured branched of foreign banks, risk assignment includes assignment to Risk Category I, II, III, or IV, and, within Risk Category I, assignment to an assessment rate or rates. For all large institutions and highly complex institutions, risk assignment includes assignment to an assessment rate or rates.

(o) *Unsecured debt.* For purposes of the unsecured debt adjustment as set forth in § 327.9(d)(6), unsecured debt shall include senior unsecured liabilities and subordinated debt.

(p) *Senior unsecured liability.* For purposes of the unsecured debt

adjustment as set forth in § 327.9(d)(6), senior unsecured liabilities shall be the unsecured portion of other borrowed money as defined in the quarterly report of condition for the reporting period as defined in paragraph (b) of this section, but shall not include any senior unsecured debt that the FDIC has guaranteed under the Temporary Liquidity Guarantee Program, 12 CFR Part 370.

(q) *Subordinated debt.* For purposes of the unsecured debt adjustment as set forth in § 327.9(d)(6), subordinated debt shall be as defined in the quarterly report of condition for the reporting period; however, subordinated debt shall also include limited-life preferred stock as defined in the quarterly report of condition for the reporting period.

(r) *Long-term unsecured debt.* For purposes of the unsecured debt adjustment as set forth in § 327.9(d)(6), long-term unsecured debt shall be unsecured debt with at least one year remaining until maturity.

\* \* \* \* \*

(t) *Processing bank and trust company.* A processing bank and trust company is an institution whose last 3 years' non-lending interest income plus fiduciary revenues plus investment banking fees exceed 50 percent of total revenues (and its last 3 years' fiduciary revenues are non-zero).

(u) *Parent company.* A parent company is a bank holding company under the Bank Holding Company Act of 1956 or a savings and loan holding company under the Home Owners' Loan Act.

(v) *Credit Card Bank.* A credit card bank is a bank for which credit card plus securitized receivables exceed 50 percent of assets plus securitized receivables.

4. Revise § 327.9 to read as follows:

**§ 327.9 Assessment risk categories and pricing methods.**

(a) *Risk Categories.* Each small insured depository institution and each insured branch of a foreign bank shall be assigned to one of the following four Risk Categories based upon the institution's capital evaluation and supervisory evaluation as defined in this section.

(1) *Risk Category I.* Institutions in Supervisory Group A that are Well Capitalized;

(2) *Risk Category II.* Institutions in Supervisory Group A that are Adequately Capitalized, and institutions in Supervisory Group B that are either Well Capitalized or Adequately Capitalized;

(3) *Risk Category III.* Institutions in Supervisory Groups A and B that are

Undercapitalized, and institutions in Supervisory Group C that are Well Capitalized or Adequately Capitalized; and

(4) *Risk Category IV.* Institutions in Supervisory Group C that are Undercapitalized.

(b) *Capital evaluations.* Each small institution and each insured branch of a foreign bank will receive one of the following three capital evaluations on the basis of data reported in the institution's Consolidated Reports of Condition and Income, Report of Assets and Liabilities of U.S. Branches and Agencies of Foreign Banks, or Thrift Financial Report dated as of March 31 for the assessment period beginning the preceding January 1; dated as of June 30 for the assessment period beginning the preceding April 1; dated as of September 30 for the assessment period beginning the preceding July 1; and dated as of December 31 for the assessment period beginning the preceding October 1.

(1) *Well Capitalized.* (i) Except as provided in paragraph (b)(1)(ii) of this section, a Well Capitalized institution is one that satisfies each of the following capital ratio standards: Total risk-based ratio, 10.0 percent or greater; Tier 1 risk-based ratio, 6.0 percent or greater; and Tier 1 leverage ratio, 5.0 percent or greater.

(ii) For purposes of this section, an insured branch of a foreign bank will be deemed to be Well Capitalized if the insured branch:

(A) Maintains the pledge of assets required under § 347.209 of this chapter; and

(B) Maintains the eligible assets prescribed under § 347.210 of this chapter at 108 percent or more of the average book value of the insured branch's third-party liabilities for the quarter ending on the report date specified in paragraph (b) of this section.

(2) *Adequately Capitalized.* (i) Except as provided in paragraph (b)(2)(ii) of this section, an Adequately Capitalized institution is one that does not satisfy the standards of Well Capitalized under this paragraph but satisfies each of the following capital ratio standards: Total risk-based ratio, 8.0 percent or greater; Tier 1 risk-based ratio, 4.0 percent or greater; and Tier 1 leverage ratio, 4.0 percent or greater.

(ii) For purposes of this section, an insured branch of a foreign bank will be deemed to be Adequately Capitalized if the insured branch:

(A) Maintains the pledge of assets required under § 347.209 of this chapter; and

(B) Maintains the eligible assets prescribed under § 347.210 of this chapter at 106 percent or more of the average book value of the insured branch's third-party liabilities for the quarter ending on the report date specified in paragraph (b) of this section; and

(C) Does not meet the definition of a Well Capitalized insured branch of a foreign bank.

(3) *Undercapitalized.* An undercapitalized institution is one that does not qualify as either Well Capitalized or Adequately Capitalized under paragraphs (b)(1) and (b)(2) of this section.

(c) *Supervisory evaluations.* Each small institution and each insured branch of a foreign bank will be assigned to one of three Supervisory Groups based on the Corporation's consideration of supervisory evaluations provided by the institution's primary Federal regulator. The supervisory evaluations include the results of examination findings by the primary Federal regulator, as well as other information that the primary Federal regulator determines to be relevant. In addition, the Corporation will take into consideration such other information (such as state examination findings, as appropriate) as it determines to be relevant to the institution's financial condition and the risk posed to the Deposit Insurance Fund. The three Supervisory Groups are:

(1) *Supervisory Group "A."* This Supervisory Group consists of financially sound institutions with only a few minor weaknesses;

(2) *Supervisory Group "B."* This Supervisory Group consists of

institutions that demonstrate weaknesses which, if not corrected, could result in significant deterioration of the institution and increased risk of loss to the Deposit Insurance Fund; and

(3) *Supervisory Group "C."* This Supervisory Group consists of institutions that pose a substantial probability of loss to the Deposit Insurance Fund unless effective corrective action is taken.

(d) *Determining Assessment Rates for Insured Depository Institutions.* A small insured depository institution in Risk Category I shall have its initial base assessment rate determined using the financial ratios method set forth in paragraph (d)(1) of this section. An insured branch of a foreign bank in Risk Category I shall have its assessment rate determined using the weighted average ROCA component rating method set forth in paragraph (d)(2) of this section. A large insured depository institution shall have its initial base assessment rate determined using the large institution method set forth in paragraph (d)(3) of this section. A highly complex insured depository institution shall have its initial base assessment rate determined using the highly complex institution method set forth at paragraph (d)(4) of this section.

(1) *Financial ratios method.* Under the financial ratios method for small Risk Category I institutions, each of six financial ratios and a weighted average of CAMELS component ratings will be multiplied by a corresponding pricing multiplier. The sum of these products will be added to or subtracted from a uniform amount. The resulting sum shall equal the institution's initial base assessment rate; provided, however, that

no institution's initial base assessment rate shall be less than the minimum initial base assessment rate in effect for Risk Category I institutions for that quarter nor greater than the maximum initial base assessment rate in effect for Risk Category I institutions for that quarter. An institution's initial base assessment rate, subject to adjustment pursuant to paragraphs (d)(6) and (7) of this section, as appropriate (resulting in the institution's total base assessment rate, which in no case can be lower than 50 percent of the institution's initial base assessment rate), and adjusted for the actual assessment rates set by the Board under § 327.10(c), will equal an institution's assessment rate. The six financial ratios are: Tier 1 Leverage Ratio; Loans past due 30–89 days/gross assets; Nonperforming assets/gross assets; Net loan charge-offs/gross assets; Net income before taxes/risk-weighted assets; and the Adjusted brokered deposit ratio. The ratios are defined in Table A.1 of Appendix A to this subpart. The ratios will be determined for an assessment period based upon information contained in an institution's report of condition filed as of the last day of the assessment period as set out in § 327.9(b). The weighted average of CAMELS component ratings is created by multiplying each component by the following percentages and adding the products: Capital adequacy—25%, Asset quality—20%, Management—25%, Earnings—10%, Liquidity—10%, and Sensitivity to market risk—10%. The following table sets forth the initial values of the pricing multipliers:

Risk measures *	Pricing multipliers **
Tier 1 Leverage Ratio .....	(0.056)
Loans Past Due 30–89 Days/Gross Assets .....	0.575
Nonperforming Assets/Gross Assets .....	1.074
Net Loan Charge-Offs/Gross Assets .....	1.210
Net Income before Taxes/Risk-Weighted Assets .....	(0.764)
Adjusted brokered deposit ratio .....	0.065
Weighted Average CAMELS Component Rating .....	1.095

\* Ratios are expressed as percentages.

\*\* Multipliers are rounded to three decimal places.

The six financial ratios and the weighted average CAMELS component rating will be multiplied by the respective pricing multiplier, and the products will be summed. To this result will be added the uniform amount of 9.861. The resulting sum shall equal the institution's initial base assessment rate; provided, however, that no institution's initial base assessment rate shall be less than the minimum initial base

assessment rate in effect for Risk Category I institutions for that quarter nor greater than the maximum initial base assessment rate in effect for Risk Category I institutions for that quarter. Appendix A to this subpart describes the derivation of the pricing multipliers and uniform amount and explains how they will be periodically updated.

(i) *Publication and uniform amount and pricing multipliers.* The FDIC will

publish notice in the **Federal Register** whenever a change is made to the uniform amount or the pricing multipliers for the financial ratios method.

(ii) *Implementation of CAMELS rating changes—(A) Changes between risk categories.* If, during a quarter, a CAMELS composite rating change occurs that results in an institution whose Risk Category I assessment rate is

determined using the financial ratios method moving from Risk Category I to Risk Category II, III or IV, the institution's initial base assessment rate for the portion of the quarter that it was in Risk Category I shall be determined using the supervisory ratings in effect before the change and the financial ratios as of the end of the quarter, subject to adjustment pursuant to paragraphs (d)(6) and (7) of this section, as appropriate, and adjusted for the actual assessment rates set by the Board under § 327.10(c). For the portion of the quarter that the institution was not in Risk Category I, the institution's initial base assessment rate, which shall be subject to adjustment pursuant to paragraphs (d)(6), (7) and (8) of this section, shall be determined under the assessment schedule for the appropriate Risk Category. If, during a quarter, a CAMELS composite rating change occurs that results in an institution moving from Risk Category II, III or IV to Risk Category I, and its initial base assessment rate would be determined using the financial ratios method, then that method shall apply for the portion of the quarter that it was in Risk Category I, subject to adjustment pursuant to paragraphs (d)(6) and (7) of this section, as appropriate, and adjusted for the actual assessment rates set by the Board under § 327.10(c). For the portion of the quarter that the institution was not in Risk Category I, the institution's initial base assessment rate, which shall be subject to adjustment pursuant to paragraphs (d)(6), (7) and (8) of this section, shall be determined under the assessment schedule for the appropriate Risk Category.

(B) *Changes within Risk Category I.* If, during a quarter, an institution's CAMELS component ratings change in a way that would change the institution's initial base assessment rate within Risk Category I, the initial base assessment rate for the period before the change shall be determined under the financial

ratios method using the CAMELS component ratings in effect before the change, subject to adjustment pursuant to paragraphs (d)(6) and (7) of this section, as appropriate. Beginning on the date of the CAMELS component ratings change, the initial base assessment rate for the remainder of the quarter shall be determined using the CAMELS component ratings in effect after the change, again subject to adjustment pursuant to paragraphs (d)(6) and (7) of this section, as appropriate.

(2) *Assessment rate for insured branches of foreign banks—(i) Insured branches of foreign banks in Risk Category I.* Insured branches of foreign banks in Risk Category I shall be assessed using the weighted average ROCA component rating.

(ii) *Weighted average ROCA component rating.* The weighted average ROCA component rating shall equal the sum of the products that result from multiplying ROCA component ratings by the following percentages: Risk Management—35%, Operational Controls—25%, Compliance—25%, and Asset Quality—15%. The weighted average ROCA rating will be multiplied by 5.076 (which shall be the pricing multiplier). To this result will be added 1.873 (which shall be a uniform amount for all insured branches of foreign banks). The resulting sum—the initial base assessment rate—will equal an institution's total base assessment rate; provided, however, that no institution's total base assessment rate will be less than the minimum total base assessment rate in effect for Risk Category I institutions for that quarter nor greater than the maximum total base assessment rate in effect for Risk Category I institutions for that quarter.

(iii) No insured branch of a foreign bank in any risk category shall be subject to the unsecured debt adjustment, the secured liability adjustment, the brokered deposit adjustment, or the adjustment in paragraph (d)(5) of this section.

(iv) *Implementation of changes between Risk Categories for insured branches of foreign banks.* If, during a quarter, a ROCA rating change occurs that results in an insured branch of a foreign bank moving from Risk Category I to Risk Category II, III or IV, the institution's initial base assessment rate for the portion of the quarter that it was in Risk Category I shall be determined using the weighted average ROCA component rating. For the portion of the quarter that the institution was not in Risk Category I, the institution's initial base assessment rate shall be determined under the assessment schedule for the appropriate Risk Category. If, during a quarter, a ROCA rating change occurs that results in an insured branch of a foreign bank moving from Risk Category II, III or IV to Risk Category I, the institution's assessment rate for the portion of the quarter that it was in Risk Category I shall equal the rate determined as provided using the weighted average ROCA component rating. For the portion of the quarter that the institution was not in Risk Category I, the institution's initial base assessment rate shall be determined under the assessment schedule for the appropriate Risk Category.

(v) *Implementation of changes within Risk Category I for insured branches of foreign banks.* If, during a quarter, an insured branch of a foreign bank remains in Risk Category I, but a ROCA component rating changes that would affect the institution's initial base assessment rate, separate assessment rates for the portion(s) of the quarter before and after the change(s) shall be determined under paragraph (d)(2) of this section.

(3) *Assessment scorecard for large institutions (other than highly complex institutions).* All large institutions other than highly complex institutions shall have their quarterly assessments determined using the scorecard for large institutions.

SCORECARD FOR LARGE INSTITUTIONS

Components	Scorecard measures	Score
CAMELS .....	<i>Weighted Average CAMELS</i> .....	25–100
Ability to Withstand Asset-Related Stress	Tier 1 Common Capital Ratio (Tier 1 Common Capital/Total Average Assets less Disallowed Intangibles).	0–100
	Concentration Measure .....	0–100
	Higher Risk Concentrations; or Growth-Adjusted Portfolio Concentrations.	
	Core Earnings/Average Total Assets .....	0–100
	Credit Quality Measure .....	0–100
	Criticized and Classified Items/Tier 1 Capital and Reserves; or	

SCORECARD FOR LARGE INSTITUTIONS—Continued

Components	Scorecard measures	Score
	Underperforming Assets/Tier 1 Capital and Reserves.	
	Subtotal .....	0–100
	Outlier Add-ons	
	Criticized and Classified Items/Tier 1 Capital and Reserves; or .....	30
	Underperforming Assets/Tier 1 Capital and Reserves Higher Risk Concentrations .....	30
	<i>Total ability to withstand asset-related stress score</i> .....	0–160
Ability to Withstand Funding-Related Stress.	Core Deposits/Total Liabilities .....	0–100
	Unfunded Commitments/Total Assets .....	0–100
	Liquid Assets/Short-Term Liabilities (liquidity coverage ratio) .....	0–100
	<i>Total ability to withstand funding-related stress score</i> .....	0–100
	<i>Total Performance Score</i> .....	0–100
Potential Loss Severity .....	Potential Losses/Total Domestic Deposits (loss severity measure) .....	0–100
	Secured Liabilities/Total Domestic Deposits .....	0–100
	<i>Total loss severity score</i> .....	0–100

**Note:** The large institution scorecard produces two scores: Performance and loss severity.

(i) *Performance score.* The performance score for large institutions is the weighted average of three inputs: Weighted average CAMELS rating (30%); ability to withstand asset-related stress measures (50%); and ability to withstand funding-related stress measures (20%).

(A) *Weighted Average CAMELS score.* To derive the weighted average CAMELS score, a weighted average of an institution’s CAMELS component ratings is calculated using the following weights:

CAMELS component	Weight (percent)
C .....	25
A .....	20
M .....	25
E .....	10
L .....	10
S .....	10

A weighted average CAMELS rating is converted to a score that ranges from 25 to 100. A weighted average rating of 1 equals a score of 25 and a weighted average of 3.5 or greater equals a score of 100. Weighted average CAMELS ratings between 1 and 3.5 are assigned a score between 25 and 100 according to the following equation:

$$S = 25 + [(20/3) * (C^2 - 1)],$$

Where:

S = the weighted average CAMELS score and  
C = the weighted average CAMELS rating.

(B) *Ability to Withstand Asset-Related Stress.* The ability to withstand asset-related stress component contains four measures: Tier 1 common ratio; Concentration measure (the higher of the higher-risk concentrations measure or growth-adjusted portfolio concentrations measures); Core earnings to average assets; and Credit quality

measure (the higher of the criticized and classified assets to Tier 1 capital and reserves or underperforming assets to Tier 1 capital and reserves). Appendices B and C define these measures in detail and give the source of the data used to determine them.

The concentration measure score is the higher of the scores of the two measures that make up the concentration measure score (higher risk concentrations or growth adjusted portfolio concentrations). The credit quality score is the higher of the criticized and classified items ratio score or the underperforming assets ratio score. Each asset related stress measure is assigned the following cutoff values and weight to derive a score for an institution’s ability to withstand asset-related stress:

CUTOFF VALUES AND WEIGHTS FOR ABILITY TO WITHSTAND ASSET-RELATED STRESS MEASURES

Scorecard measures	Cutoff values		Weight (percent)
	Minimum	Maximum	
Tier 1 Common Capital Ratio .....	5.8	12.9	15
Concentration Measure: .....			35
Higher Risk Concentrations; or .....	0.0	3.2	
Growth-Adjusted Portfolio Concentrations .....	7.6	154.7	
Core Earnings/Average Total Assets .....	0.0	2.3	15
Credit Quality Measure: .....			35
Criticized and Classified Items/Tier 1 Capital and Reserves; or .....	6.5	100.0	

CUTOFF VALUES AND WEIGHTS FOR ABILITY TO WITHSTAND ASSET-RELATED STRESS MEASURES—Continued

Scorecard measures	Cutoff values		Weight (percent)
	Minimum	Maximum	
Underperforming Assets/Tier 1 Capital and Reserves .....	2.3	35.1	.....

For each of the risk measures within the ability to withstand asset-related stress portion of the scorecard, a value reflecting lower risk than the cutoff value that results in a score of 0 will also receive a score of 0, where 0 equals the lowest risk for that measure. A value reflecting higher risk than the cutoff value that results in a score of 100 will also receive a score of 100, where 100 equals the highest risk for that measure. A risk measure value between the minimum and maximum cutoff values is converted linearly to a score between 0 and 100. For the Concentration Measure and Credit Quality Measures, a lower ratio implies lower risk and a higher ratio implies higher risk. For these measures, a value between the minimum and maximum cutoff values will be converted linearly to a score between 0 and 100, according to the following formula:

$$S = (V - Min) * 100 / (Max - Min),$$

Where S is score (rounded to three decimal points), V is the value of the measure, Min is the minimum cutoff value and Max is the maximum cutoff value.

For the Tier 1 Common Capital Ratio and Core Earnings to Average Total Assets Ratio, a lower value represents higher risk and a higher value represents lower risk. For these measures, a value between the minimum and maximum cutoff values is converted linearly to a score between 0 and 100, according to the following formula:

$$S = (Max - V) * 100 / (Max - Min),$$

Where S is score (rounded to three decimal points), V is the value of the measure, Min is the minimum cutoff value and Max is the maximum cutoff value.

Each score is multiplied by a respective weight and the resulting weighted score for each measure is summed to arrive at an ability to withstand asset-related stress score, which ranges from 0 to 100.

For extreme values of certain measures reflecting particularly high risk, this score can increase through an outlier add-on. If an institution's ratio of criticized and classified items to Tier 1 capital and reserves exceeds 100 percent or its ratio of underperforming assets to Tier 1 capital and reserves exceeds 50.2

percent, the ability to withstand asset-related stress component score is increased by 30 points. Additionally, if the higher risk concentration measure exceeds 4.8, the ability to withstand asset-related stress component score is increased by 30 points. These increases (outlier add-ons) are determined separately and can increase the ability to withstand asset-related score by up to 60 points; thus, the ability to withstand asset-related component score can be as high as 160 points.

(C) *Ability to Withstand Funding-Related Stress.* The ability to withstand funding-related stress component contains three risk measures: A core deposits to liabilities ratio, an unfunded commitments to total assets ratio, and a liquidity coverage ratio. Appendix B describes these ratios in detail and gives the source of the data used to determine them. The ability to withstand funding-related stress component score is the weighted average of the three measure scores. Each measure is assigned the following cutoff values and weights to derive a score for an institution's ability to withstand funding-related stress:

CUTOFF VALUES AND WEIGHTS FOR ABILITY TO WITHSTAND FUNDING-RELATED STRESS MEASURES

Scorecard measures	Cutoff values		Weight (percent)
	Minimum	Maximum	
Core Deposits/Total Liabilities .....	3.2	79.1	40
Unfunded Commitments/Total Assets .....	0.3	42.2	40
Liquid Assets/Short-term Liabilities (Liquidity Coverage Ratio) .....	5.6	170.9	20

A risk measure value reflecting lower risk than the cutoff value that results in a score of 0, will also receive a score of 0, where 0 equals the lowest risk for that measure. A risk measure value reflecting higher risk than the cutoff value that results in a score of 100, will also receive a score of 100, where 100 equals the highest risk for that measure. For the Core Deposits/Liabilities measure and the Liquidity Coverage Ratio, a lower ratio implies higher risk and a higher ratio implies lower risk. For these measures, a value between the minimum and maximum cutoff values will be converted linearly to a score between 0 and 100, according to the following formula:

$$S = (Max - V) * 100 / (Max - Min)$$

Where S is score (rounded to three decimal points), V is the value of the measure, Min is the minimum cutoff value and Max is the maximum cutoff value.

For the Unfunded Commitments/Assets measure, a lower value represents lower risk and a higher value represents higher risk. For these measures, a value between the minimum and maximum cutoff values is converted linearly to a score between 0 and 100, according to the following formula:

$$S = (V - Min) * 100 / (Max - Min)$$

Where S is score (rounded to three decimal points), V is the value of the measure, Min is the minimum cutoff value and Max is the maximum cutoff value.

(D) *Calculation of Performance Score.* The weighted average CAMELS score, the ability to withstand asset-related stress score, and the ability to withstand funding-related stress score are multiplied by their weights and the results are summed to arrive at the performance score. The performance score cannot exceed 100. The performance score is subject to adjustment, up or down, by a maximum of 15 points, as set forth in section (d)(5). The resulting score cannot be less than 0 or more than 100.

(ii) *Loss severity score.* The loss severity score is based on two measures: Loss severity measure and secured liabilities to total domestic deposits ratio. Appendices B and D describe

these measures in detail. The loss severity score is the weighted average of these scores. Each measure is assigned the following cutoff values and weight to derive a score for an institution's loss severity score:

CUTOFF VALUES AND WEIGHTS FOR LOSS SEVERITY SCORE MEASURES

Scorecard measures	Cutoff values		Weight (percent)
	Minimum	Maximum	
Potential Losses/Total Domestic Deposits (loss severity measure) .....	0.0	30.1	50
Secured Liabilities/Total Domestic Deposits .....	0.0	75.7	50

A risk measure value reflecting lower risk than the minimum cutoff value results in a score of 0, where 0 equals the lowest risk for that measure. A risk measure value reflecting higher risk than the maximum cutoff value results in a score of 100, where 100 equals the highest risk for that measure. A risk measure value between the minimum and maximum cutoff values is converted linearly to a score between 0 and 100, according to the following formula:

$$S = (V - Min) * 100 / (Max - Min)$$

Where S is score (rounded to three decimal points), V is the value of the measure, Min is the minimum cutoff value and Max is the maximum cutoff value.

The loss severity score is subject to adjustment, up or down, by a maximum of 15 points, as set forth in section (d)(5). The resulting score cannot be less than 0 or more than 100.

(iii) *Initial base assessment rate.* The performance and loss severity scores, with any adjustments under paragraph (d)(5) of this section, are converted to an initial base assessment rate. The loss severity score is converted into a loss severity measure that ranges from 0.8 (score of 5 or lower) and 1.2 (score of 85 or higher). Scores that fall at or below the minimum cutoff of 5 receive a loss severity measure of 0.8 and scores that falls at or above the maximum cutoff of 85 receive a loss severity score of 1.2. The following linear interpolation

converts loss severity scores between the cutoffs into a loss severity measure: (Loss Severity Measure = 0.8 + [(Loss Severity Score - 5) x 0.005]. The performance score is multiplied by the loss severity measure to produce a total score (total score = performance score \* loss severity measure). The total score cannot exceed 100. A large institution with a total score of 30 or lower pays the minimum initial base assessment rate and an institution with a total score of 90 or greater pays the maximum initial base assessment rate. For total scores between 30 and 90, initial base assessment rates rise at an increasing rate as the total score increases, calculated according to the following formula:

$$Rate = Minimum Rate - 0.165289 + \left( 68.02027 \times \left( \frac{Score}{100} \right)^5 \right)$$

Where Rate is the initial base assessment rate and Minimum Rate is the minimum initial base assessment rate then in effect. Initial base assessment rates are subject to adjustment pursuant to sections (d)(6), (d)(7), and (d)(8),

resulting in the institution's total base assessment rate, which in no case can be lower than 50 percent of the institution's initial base assessment rate.

(4) *Assessment scorecard for highly complex institutions.* All highly

complex institutions shall have their quarterly assessments determined using the scorecard for highly complex institutions.

SCORECARD FOR HIGHLY COMPLEX INSTITUTIONS

Components	Scorecard measures	Score
CAMELS .....	Weighted Average CAMELS .....	25-100
Market Indicator .....	Senior Bond Spread .....	0-100
	Outlier Add-ons	
Ability to Withstand Asset-Related Stress	Parent Company Tangible Common Equity (TCE) Ratio .....	30
	Total Market Indicator score .....	0-130
	Tier 1 Common Capital Ratio (Tier 1 Common Capital/Total Average Assets less Disallowed Intangibles).	0-100
Ability to Withstand Asset-Related Stress	Concentration Measure ..... Higher Risk Concentrations; or Growth-Adjusted Portfolio Concentrations.	0-100
	Core Earnings/Average Total Assets .....	0-100
	Credit Quality Measure ..... Criticized and Classified Items/Tier 1 Capital and Reserves.	0-100

SCORECARD FOR HIGHLY COMPLEX INSTITUTIONS—Continued

Components	Scorecard measures	Score
	Underperforming Assets/Tier 1 Capital and Reserves.	
	10-day 99% VaR/Tier 1 Capital .....	0–100
	Subtotal .....	0–100
	Outlier Add-ons	
	Criticized and Classified Items/Tier 1 Capital and Reserves; or Underperforming Assets/Tier 1 Capital and Reserves	30
	Higher Risk Concentrations Measure .....	30
	<i>Total ability to withstand asset-related stress score</i> .....	0–160
Ability to Withstand Funding-Related Stress.	Core Deposits/Total Liabilities .....	0–100
	Unfunded Commitments/Total Assets .....	0–100
	Liquid Assets/Short-term Liabilities (liquidity coverage ratio) .....	0–100
	Short-term Funding/Total Assets .....	0–100
	Subtotal .....	0–100
	Outlier Add-ons	
	Short-term funding/Total Assets .....	30
	<i>Total ability to withstand funding-related stress score</i> .....	0–130
	<i>Total Performance Score</i> .....	0–100
Potential Loss Severity .....	Potential Losses/Total Domestic Deposits (loss severity measure) .....	0–100
	Secured Liabilities/Total Domestic Deposits .....	0–100
	<i>Total loss severity score</i> .....	0–100

The scorecard for highly complex institutions contains the performance components and the loss severity components of the large bank scorecard and employs the same methodology. The assessment process set forth in section (d)(3) for the large bank scorecard applies to highly complex institutions, modified as follows. The scorecard for highly-complex institutions contains an additional component—market indicator—in the performance score; an additional component—10-day 99 percent Value at Risk (VaR)/Tier 1 capital—in the ability to withstand asset-related stress; and an additional component—short-term

funding to total assets ratio—in the ability to withstand funding-related stress.

(i) *Performance score for highly complex institutions.* The performance score for highly complex institutions is the weighted average of four inputs: Weighted average CAMELS rating (20%); market indicator score (10%); ability to withstand asset-related stress score (50%); and ability to withstand funding-related stress score (20%). To calculate the performance score for highly complex institutions, the weighted average CAMELS score, the market indicator score, the ability to withstand asset-related stress score, and

ability to withstand funding-related stress score are multiplied by their weights and the results are summed to arrive at the performance score. The resulting score cannot exceed 100.

(A) *Market indicator.* The market indicator component contains one component—the senior bond spread score, and one outlier add-on—the Parent Tangible Common Equity (TCE) ratio. The senior bond spread is converted to a score according to the linear interpolation method used for the large bank scorecard. The minimum and maximum cutoff values for the market indicator measure are:

CUTOFF VALUES AND WEIGHTS FOR MARKET INDICATOR MEASURE

Scorecard measures	Cutoff values		Weight (percent)
	Minimum	Maximum	
Senior Bond Spread .....	0.6	3.8	100

A risk measure value reflecting lower risk than the minimum cutoff value results in a score of 0, where 0 equals the lowest risk for that measure. A risk measure value reflecting higher risk than the maximum cutoff value results in a score of 100, where 100 equals the highest risk for that measure. A value between the minimum and maximum cutoff values will be converted linearly

to a score between 0 and 100, according to the following formula:  

$$S = (V - Min) * 100 / (Max - Min)$$

The market indicator component score can be adjusted by up to 30 points if the outlier add-on—institution's parent company's TCE ratio—falls below 4 percent. Including the outlier add-on, the market indicator component score can be as high as 130 points.

(B) *Ability to withstand asset-related stress.* The scorecard for highly complex institutions adds one additional factor to the ability to withstand asset-related stress component—the 10-day 99 percent Value at Risk (VaR)/Tier 1 capital. The cutoff values and weights for ability to withstand asset-related stress measures are set forth below.

CUTOFF VALUES AND WEIGHTS FOR ABILITY TO WITHSTAND ASSET-RELATED STRESS MEASURES

Scorecard measures	Cutoff values		Weight (percent)
	Minimum	Maximum	
Tier 1 Common Ratio .....	5.8	12.9	10
Concentration Measure .....			35
Higher Risk Concentrations; or .....	0.0	3.2	
Growth-Adjusted Portfolio Concentrations .....	7.6	154.7	
Core Earnings/Average Total Assets .....	0.0	2.3	10
Credit Quality Measure .....			35
Criticized and Classified Items/Tier 1 Capital and Reserves; or .....	6.5	100.0	
Underperforming Assets/Tier 1 Capital and Reserves .....	2.3	35.1	
10-day 99% VaR/Tier 1 Capital .....	0.1	0.5	10

Appendix B describes these measures in detail and gives the source of the data used to calculate the measures.

(C) *Ability to withstand funding related stress.* The scorecard for highly

complex institutions adds one additional factor to the ability to withstand funding-related stress component—the short-term funding to

total assets ratio. The cutoff values and weights for ability to withstand funding-related stress measures for highly complex institutions are set forth below.

CUTOFF VALUES AND WEIGHTS FOR ABILITY TO WITHSTAND FUNDING-RELATED STRESS MEASURES

Scorecard measures	Cutoff values		Weight (percent)
	Minimum	Maximum	
Core Deposits/Total Liabilities .....	3.2	79.1	30
Unfunded Commitments/Total Assets .....	0.3	42.2	30
Liquid Assets/Short-term Liabilities (liquidity coverage ratio) .....	5.6	170.9	20
Short-term Funding/Total Assets .....	0.0	19.1	20

Appendix B describes these measures in detail and gives the source of the data used to calculate the measures.

The scorecard for highly complex institutions adds an additional outlier add-on to the scorecard for large institutions. The ability to withstand funding-related stress component score for highly complex institutions is adjusted by 30 points if the ratio of short term funding to total assets exceeds 26.9 percent. The maximum ability to withstand funding-related stress component score for highly complex institutions, including the outlier add-on, is 130 points.

(ii) *Loss severity score for highly complex institutions.* The loss severity score for highly complex institutions is calculated as provided for the loss severity score for large institutions in section (d)(3)(ii).

(iii) The performance score and the loss severity score for highly complex

institutions can be adjusted, up or down, by maximum of 15 points each, as set forth in section (d)(5), resulting in the institution's initial base assessment rate.

(iv) The initial base assessment rate for highly complex institutions is calculated from the total score in the same manner as for large institutions as set forth in section (d)(3). Initial base assessment rates are subject to adjustment pursuant to sections (d)(6), (d)(7), and (d)(8), resulting in the institution's total base assessment rate, which in no case can be lower than 50 percent of the institution's initial base assessment rate.

(5) *Adjustment to performance score and/or loss severity score for large institutions and highly complex institutions.* The performance score and the loss severity score for large institutions and highly complex institutions are subject to adjustment

under paragraph (d)(5) of this section, up or down, by a maximum of 15 points each, based upon significant risk factors that are not adequately captured in the appropriate scorecard. In making such adjustments, the FDIC may consider such information as financial performance and condition information and other market or supervisory information. Appendix E lists some, but not all, criteria that the FDIC may consider in determining whether to make such adjustments.

(i) *Prior notice of adjustments—(A) Prior notice of upward adjustment.* Prior to making any upward adjustment to an institution's performance score and/or loss severity score because of considerations of additional risk information, the FDIC will formally notify the institution and its primary Federal regulator and provide an opportunity to respond. This notification will include the reasons for

the adjustment(s) and when the adjustment(s) will take effect.

(B) *Prior notice of downward adjustment.* Prior to making any downward adjustment to an institution's performance score and/or loss severity score because of considerations of additional risk information, the FDIC will formally notify the institution's primary Federal regulator and provide an opportunity to respond.

(ii) *Determination whether to adjust upward; effective period of adjustment.* After considering an institution's and the primary Federal regulator's responses to the notice, the FDIC will determine whether the adjustment to an institution's performance score and/or loss severity score is warranted, taking into account any revisions to scorecard measures, as well as any actions taken by the institution to address the FDIC's concerns described in the notice. The FDIC will evaluate the need for the adjustment each subsequent assessment period. The amount of adjustment will in no event be larger than that contained in the initial notice without further notice to, and consideration of, responses from the primary Federal regulator and the institution.

(iii) *Determination whether to adjust downward; effective period of adjustment.* After considering the primary Federal regulator's responses to the notice, the FDIC will determine whether the adjustment to performance score and/or loss severity score is warranted, taking into account any revisions to scorecard measures, as well as any actions taken by the institution to address the FDIC's concerns described in the notice. Any downward adjustment in an institution's performance score and/or loss severity score will remain in effect for subsequent assessment periods until the FDIC determines that an adjustment is no longer warranted. Downward adjustments will be made without notification to the institution. However, the FDIC will provide advance notice to an institution and its primary Federal regulator and give them an opportunity to respond before removing a downward adjustment.

(iv) *Adjustment without notice.* Notwithstanding the notice provisions set forth above, the FDIC may change an institution's performance score and/or loss severity score without advance notice under this paragraph, if the institution's supervisory ratings or the scorecard measures deteriorate.

(6) *Unsecured debt adjustment to initial base assessment rate for all institutions.* All small, large, and highly complex institutions, except new small

institutions as provided under paragraph (d)(10)(i) of this section, are subject to downward adjustment of assessment rates for unsecured debt, based on the ratio of long-term unsecured debt (and, for small institutions as defined in paragraph (d)(6)(ii) of this section, specified amounts of Tier 1 capital) to domestic deposits. Any unsecured debt adjustment shall be made after any adjustment under paragraph (d)(5) of this section. Insured branches of foreign banks are not subject to the unsecured debt adjustment as provided in paragraph (d)(2)(iii).

(i) *Large institutions and highly complex institutions.* The unsecured debt adjustment for large institutions and highly complex institutions shall be determined by multiplying the institution's ratio of long-term unsecured debt to domestic deposits by 40 basis points.

(ii) *Small institutions.*—The unsecured debt adjustment for small institutions will factor in an amount of Tier 1 capital (qualified Tier 1 capital) in addition to any long-term unsecured debt; the amount of qualified Tier 1 capital will be the sum of the amounts set forth below:

Range of Tier 1 capital to adjusted average assets	Amount of Tier 1 capital within range which is qualified (percent)
≤ 5% .....	0
> 5% and ≤ 6% .....	10
> 6% and ≤ 7% .....	20
> 7% and ≤ 8% .....	30
> 8% and ≤ 9% .....	40
> 9% and ≤ 10% .....	50
> 10% and ≤ 11% .....	60
> 11% and ≤ 12% .....	70
> 12% and ≤ 13% .....	80
> 13% and ≤ 14% .....	90
> 14% .....	100

For institutions that file Thrift Financial Reports, adjusted total assets will be used in place of adjusted average assets in the preceding table. The sum of qualified Tier 1 capital and long-term unsecured debt as a percentage of domestic deposits will be multiplied by 40 basis points to produce the unsecured debt adjustment for small institutions.

(iii) *Limitation.*—No unsecured debt adjustment for any institution shall exceed 5 basis points. No unsecured debt adjustment for any institution shall result in a total base assessment rate that is less than 50 percent of the institution's initial base assessment rate.

(iv) *Applicable quarterly reports of condition.*—Ratios for any given quarter shall be calculated from quarterly

reports of condition (Call Reports and Thrift Financial Reports) filed by each institution as of the last day of the quarter.

(7) *Secured liability adjustment for all institutions.* All institutions, except insured branches of foreign banks as provided under paragraph (d)(2)(iii) of this section, are subject to upward adjustment of their assessment rate based upon the ratio of their secured liabilities to domestic deposits. Any such adjustment shall be made after any applicable adjustment under paragraph (d)(5) or (d)(6) of this section.

(i) *Secured liabilities for banks.*—Secured liabilities for banks include Federal Home Loan Bank advances, securities sold under repurchase agreements, secured Federal funds purchased and other borrowings that are secured as reported in banks' quarterly Call Reports.

(ii) *Secured liabilities for savings associations.*—Secured liabilities for savings associations include Federal Home Loan Bank advances as reported in quarterly Thrift Financial Reports ("TFRs"). Secured liabilities for savings associations also include securities sold under repurchase agreements, secured Federal funds purchased or other borrowings that are secured.

(iii) *Calculation.*—An institution's ratio of secured liabilities to domestic deposits will, if greater than 25 percent, increase its assessment rate, but any such increase shall not exceed 50 percent of its assessment rate before the secured liabilities adjustment. For an institution that has a ratio of secured liabilities (as defined in paragraph (ii) above) to domestic deposits of greater than 25 percent, the institution's assessment rate (after taking into account any adjustment under paragraphs (d)(5) or (6) of this section) will be multiplied by the following amount: the ratio of the institution's secured liabilities to domestic deposits minus 0.25. Ratios of secured liabilities to domestic deposits shall be calculated from the report of condition, or similar report, filed by each institution.

(8) *Brokered Deposit Adjustment.* All small institutions in Risk Categories II, III, and IV, all large institutions, and all highly complex institutions shall be subject to an assessment rate adjustment for brokered deposits. Any such brokered deposit adjustment shall be made after any adjustment under paragraph (d)(5), (d)(6) or (d)(7) of this section. The brokered deposit adjustment includes all brokered deposits as defined in Section 29 of the Federal Deposit Insurance Act (12 U.S.C. 1831f), and 12 CFR 337.6, including reciprocal deposits as defined

in § 327.8(r), and brokered deposits that consist of balances swept into an insured institution by another institution. The adjustment under this paragraph is limited to those institutions whose ratio of brokered deposits to domestic deposits is greater than 10 percent; asset growth rates do not affect the adjustment. The adjustment is determined by multiplying by 25 basis points the difference between an institution's ratio of brokered deposits to domestic deposits and 0.10. The maximum brokered deposit adjustment will be 10 basis points. Brokered deposit ratios for any given quarter are calculated from the quarterly reports of condition filed by each institution as of the last day of the quarter. Insured branches of foreign banks are not subject to the brokered deposit adjustment as provided in section (d)(2)(iii).

(9) *Request to be treated as a large institution*—(i) *Procedure*. Any institution in Risk Category I with assets of between \$5 billion and \$10 billion may request that the FDIC determine its assessment rate as a large institution. The FDIC will grant such a request if it determines that it has sufficient information to do so. Any such request must be made to the FDIC's Division of Insurance and Research. Any approved change will become effective within one year from the date of the request. If an institution whose request has been granted subsequently reports assets of less than \$5 billion in its report of condition for four consecutive quarters, the FDIC will consider such institution to be a small institution subject to the financial ratios method.

(ii) *Time limit on subsequent request for alternate method*. An institution whose request to be assessed as a large institution is granted by the FDIC shall not be eligible to request that it be assessed as a small institution for a period of three years from the first quarter in which its approved request to be assessed as a large bank became effective. Any request to be assessed as a small institution must be made to the

FDIC's Division of Insurance and Research.

(iii) An institution that disagrees with the FDIC's determination that it is a large or small institution may request review of that determination pursuant to § 327.4(c).

(10) *New and established institutions and exceptions*—(i) *New small institutions*. A new small institution that is well capitalized shall be assessed the Risk Category I maximum initial base assessment rate for the relevant assessment period, except as provided in § 327.8(m)(1), (2), (3), (4), (5) and paragraphs (d)(10)(ii) and (iii) of this section. No new small institution in any risk category shall be subject to the unsecured debt adjustment as determined under paragraph (d)(6) of this section. All new small institutions in any Risk Category shall be subject to the secured liability adjustment as determined under paragraph (d)(7) of this section. All new small institutions in Risk Categories II, III, and IV shall be subject to the brokered deposit adjustment as determined under paragraph (d)(8) of this section.

(ii) *New large institutions and new highly complex institutions*. All new large institutions and all new highly complex institutions shall be assessed under the appropriate method provided at paragraph (d)(3) or (d)(4) of this section and subject to the adjustments provided at paragraphs (d)(5), (d)(7), and (d)(8) of this section. No new Highly Complex or large institutions are entitled to adjustment under paragraph (d)(6) of this section. If a large or highly complex institution has not yet received CAMELS ratings, it will be given a weighted CAMELS rating of 2 for assessment purposes until actual CAMELS ratings are assigned.

(iii) *CAMELS ratings for the surviving institution in a merger or consolidation*. When an established institution merges with or consolidates into a new institution, if the FDIC determines the resulting institution to be an established institution under § 327.8(m)(1), its CAMELS ratings for assessment purposes will be based upon the

established institution's ratings prior to the merger or consolidation until new ratings become available.

(iv) *Rate applicable to institutions subject to subsidiary or credit union exception*. If a small institution is considered established under § 327.8(m)(4) and (5), but does not have CAMELS component ratings, it shall be assessed at two basis points above the minimum initial base assessment rate applicable to Risk Category I institutions until it receives CAMELS component ratings. Thereafter, the assessment rate will be determined by annualizing, where appropriate, financial ratios obtained from all quarterly reports of condition that have been filed, until the institution files four quarterly reports of condition. If a large or highly complex institution is considered established under § 327.8(m)(4) and (5), but does not have CAMELS component ratings, it will be given a weighted CAMELS rating of 2 for assessment purposes until actual CAMELS ratings are assigned.

(v) *Request for review*. An institution that disagrees with the FDIC's determination that it is a new institution may request review of that determination pursuant to § 327.4(c).

(11) *Assessment rates for bridge depository institutions and conservatorships*. Institutions that are bridge depository institutions under 12 U.S.C. 1821(n) and institutions for which the Corporation has been appointed or serves as conservator shall, in all cases, be assessed at the Risk Category I minimum initial base assessment rate, which shall not be subject to adjustment under paragraphs (d)(5), (6), (7) or (8) of this section.

5. Revise § 327.10 to read as follows:

**§ 327.10 Assessment rate schedules.**

(a) *Initial and Total Base Assessment Rate Schedule for Small Institutions and Insured Branches of Foreign Banks*. The initial and total base assessment rate for a small insured depository institution or an insured branch of a foreign bank shall be the rate prescribed in the following schedule:

	Risk category I	Risk category II	Risk category III	Risk category IV
Initial base assessment rate .....	10–14	22	34	50
Unsecured debt adjustment .....	–5–0	–5–0	–5–0	–5–0
Secured liability adjustment .....	0–7	0–11	0–17	0–25
Brokered deposit adjustment .....		0–10	0–10	0–10
<b>TOTAL BASE ASSESSMENT RATE .....</b>	<b>5–21</b>	<b>17–43</b>	<b>29–61</b>	<b>45–85</b>

All amounts for all risk categories are in basis points annually. Total base rates that are not the minimum or maximum rate will vary between these rates. All rates shown will increase 3 basis points on January 1, 2011, pursuant to the FDIC Restoration Plan adopted on September 29, 2009 (74 FR 51062 (Oct. 2, 2009)).

(1) *Risk Category I Initial Base Assessment Rate Schedule.* The annual initial base assessment rates for all institutions in Risk Category I shall range from 10 to 14 basis points.

(2) *Risk Category II, III, and IV Initial Base Assessment Rate Schedule.* The annual initial base assessment rates for Risk Categories II, III, and IV shall be 22, 34, and 50 basis points, respectively.

(3) *Risk Category I Total Base Assessment Rate Schedule after Adjustments.* The annual total base assessment rates after adjustments for all institutions in Risk Category I shall range from 5 to 21 basis points.

(4) *Risk Category II Total Base Assessment Rate Schedule after Adjustments.* The annual total base assessment rates after adjustments for all institutions in Risk Category II shall range from 17 to 43 basis points.

(5) *Risk Category III Total Base Assessment Rate Schedule after Adjustments.* The annual total base assessment rates after adjustments for all institutions in Risk Category III shall range from 29 to 61 basis points.

(6) *Risk Category IV Total Base Assessment Rate Schedule after Adjustments.* The annual total base assessment rates after adjustments for

all institutions in Risk Category IV shall range from 45 to 85 basis points.

(7) All institutions in any one risk category, other than Risk Category I, will be charged the same initial base assessment rate, subject to adjustment as appropriate.

(b) *Initial and Total Base Assessment Rate Schedule for Large Institutions and Highly Complex Institutions.* The annual initial base assessment rate and total base assessment rate for a large insured depository institution or a highly complex insured depository institution shall be the rate prescribed in the following schedule:

	Large institutions
Initial base assessment rate .....	10–50
Unsecured debt adjustment .....	–5–0
Secured liability adjustment .....	0–25
Brokered deposit adjustment .....	0–10
<b>TOTAL BASE ASSESSMENT RATE .....</b>	<b>5–85</b>

All amounts are in basis points annually. Total base rates that are not the minimum or maximum rate will vary between these rates. All rates shown will increase 3 basis points on January 1, 2011, pursuant to the FDIC Restoration Plan adopted on September 29, 2009 (74 FR 51062 (Oct. 2, 2009)).

(1) *Initial Base Assessment Rate Schedule for Large Institutions and Highly Complex Institutions.* The annual initial base assessment rates for all large institutions and highly complex institutions shall range from 10 to 50 basis points.

(2) *Total Base Assessment Rate Schedule for Large Institutions and Highly Complex Institutions.* The annual total base assessment rates for all large institutions and highly complex institutions shall range from 5 to 85 basis points.

(c) *Total Base Assessment Rate Schedule adjustments and procedures—*

(1) *Board Rate Adjustments.* The Board may increase or decrease the total base assessment rate schedule for all insured depository institutions up to a maximum increase of 3 basis points or a fraction thereof or a maximum decrease of 3 basis points or a fraction thereof (after aggregating increases and decreases), as the Board deems necessary. Any such adjustment shall apply uniformly to each rate in the total base assessment rate schedule. In no case may such Board rate adjustments result in a total base assessment rate that is mathematically less than zero or in a total base assessment rate schedule that, at any time, is more than 3 basis points above or below the total base assessment schedule for the Deposit Insurance Fund, nor may any one such Board adjustment constitute an increase or decrease of more than 3 basis points.

(2) *Amount of revenue.* In setting assessment rates, the Board shall take into consideration the following:

- (i) Estimated operating expenses of the Deposit Insurance Fund;
- (ii) Case resolution expenditures and income of the Deposit Insurance Fund;
- (iii) The projected effects of assessments on the capital and earnings of the institutions paying assessments to the Deposit Insurance Fund;
- (iv) The risk factors and other factors taken into account pursuant to 12 U.S.C. 1817(b)(1); and
- (v) Any other factors the Board may deem appropriate.

(3) *Adjustment procedure.* Any adjustment adopted by the Board pursuant to this paragraph will be adopted by rulemaking, except that the Corporation may set assessment rates as necessary to manage the reserve ratio, within set parameters not exceeding cumulatively 3 basis points, pursuant to paragraph (c)(1) of this section, without further rulemaking.

(4) *Announcement.* The Board shall announce the assessment schedules and the amount and basis for any adjustment thereto not later than 30 days before the quarterly certified statement invoice date specified in § 327.3(b) of this part for the first assessment period for which the adjustment shall be effective. Once set, rates will remain in effect until changed by the Board.

6. Revise Appendix A to Subpart A of Part 327 to read as follows:

**Appendix A to Subpart A**

**Method To Derive Pricing Multipliers and Uniform Amount**

**I. Introduction**

The uniform amount and pricing multipliers are derived from:

- A model (the Statistical Model) that estimates the probability that a Risk Category I institution will be downgraded to a composite CAMELS rating of 3 or worse within one year;
- Minimum and maximum downgrade probability cutoff values, based on data from June 30, 2008, that will determine which small institutions will be charged the minimum and maximum initial base assessment rates applicable to Risk Category I; and
- The maximum initial base assessment rate for Risk Category I, which is four basis points higher than the minimum rate.

**II. The Statistical Model**

The Statistical Model is defined in equations 1 and 3 below:

*Equation 1*

$$\text{Downgrade } (0,1)_{i,t} = \beta_0 + \beta_1 (\text{Tier 1 Leverage Ratio}_T) + \beta_2 (\text{Loans past due 30 to 89 days ratio}_{i,t}) + \beta_3 (\text{Nonperforming asset ratio}_{i,t}) + \beta_4 (\text{Net loan charge-off ratio}_{i,t}) + \beta_5 (\text{Net income before taxes ratio}_{i,t}) + \beta_6 (\text{Adjusted brokered deposit ratio}_{i,t}) + \beta_7 (\text{Weighted average CAMELS component rating}_{i,t})$$

Where Downgrade(01)<sub>i,t</sub> (the dependent variable—the event being explained) is the incidence of downgrade from a composite rating of 1 or 2 to a rating of 3 or worse during an on-site examination for an institution i between 3 and 12 months after time t. Time t is the end of

a year within the multi-year period over which the model was estimated (as explained below). The dependent variable takes a value of 1 if a downgrade occurs and 0 if it does not.

The explanatory variables (regressors) in the model are six financial ratios and a weighted average of the “C,” “A,” “M,” “E” and “L” component ratings. The six financial ratios included in the model are:

- Tier 1 leverage ratio
- Loans past due 30–89 days/Gross assets
- Nonperforming assets/Gross assets
- Net loan charge-offs/Gross assets

- Net income before taxes/Risk-weighted assets
- Brokered deposits/domestic deposits above the 10 percent threshold, adjusted for the asset growth rate factor

Table A.1 defines these six ratios along with the weighted average of CAMELS component ratings. The adjusted brokered deposit ratio ( $B_{i,T}$ ) is calculated by multiplying the ratio of brokered deposits to domestic deposits above the 10 percent threshold by an asset growth rate factor that ranges from 0 to 1 as shown in Equation 2 below. The asset growth rate factor ( $A_{i,T}$ ) is

calculated by subtracting 0.4 from the four-year cumulative gross asset growth rate (expressed as a number rather than as a percentage), adjusted for mergers and acquisitions, and multiplying the remainder by  $3^{1/3}$ . The factor cannot be less than 0 or greater than 1.

Equation 2

$$B_{i,T} = \left( \frac{\text{Brokered Deposits}_{i,T}}{\text{Domestic Deposits}_{i,T}} - 0.10 \right) * A_{i,T}$$

Where

$$A_{i,T} = \left[ \left( \frac{\text{GrossAssets}_{i,T} - \text{GrossAssets}_{i,T-4}}{\text{GrossAssets}_{i,T-4}} - 0.4 \right) * \frac{10}{3} \right],$$

subject to

$$0 \leq A_{i,T} \leq 1 \text{ and } B_{i,T} \geq 0.$$

The component rating for sensitivity to market risk (the “S” rating) is not available for years prior to 1997. As a result, and as described in Table A.1, the Statistical Model is estimated using a weighted average of five component ratings excluding the “S”

component. Delinquency and non-accrual data on government guaranteed loans are not available before 1993 for Call Report filers and before the third quarter of 2005 for TFR filers. As a result, and as also described in Table A.1, the Statistical Model is estimated without deducting delinquent or past-due government guaranteed loans from either the loans past due 30–89 days to gross assets

ratio or the nonperforming assets to gross assets ratio. Reciprocal deposits are not presently reported in the Call Report or TFR. As a result, and as also described in Table A.1, the Statistical Model is estimated without deducting reciprocal deposits from brokered deposits in determining the adjusted brokered deposit ratio.

TABLE A.1—DEFINITIONS OF REGRESSORS

Regressor	Description
Tier 1 Leverage Ratio (%) .....	Tier 1 capital for Prompt Corrective Action (PCA) divided by adjusted average assets based on the definition for prompt corrective action.
Loans Past Due 30–89 Days/Gross Assets (%) .....	Total loans and lease financing receivables past due 30 through 89 days and still accruing interest divided by gross assets (gross assets equal total assets plus allowance for loan and lease financing receivable losses and allocated transfer risk).
Nonperforming Assets/Gross Assets (%) .....	Sum of total loans and lease financing receivables past due 90 or more days and still accruing interest, total nonaccrual loans and lease financing receivables, and other real estate owned divided by gross assets.
Net Loan Charge-Offs/Gross Assets (%) .....	Total charged-off loans and lease financing receivables debited to the allowance for loan and lease losses less total recoveries credited to the allowance to loan and lease losses for the most recent twelve months divided by gross assets.
Net Income before Taxes/Risk-Weighted Assets (%) .....	Income before income taxes and extraordinary items and other adjustments for the most recent twelve months divided by risk-weighted assets.
Adjusted brokered deposit ratio (%) .....	Brokered deposits divided by domestic deposits less 0.10 multiplied by the asset growth rate factor (which is the term $A_{i,T}$ as defined in equation 2 above) that ranges between 0 and 1.
Weighted Average of C, A, M, E and L Component Ratings.	The weighted sum of the “C,” “A,” “M,” “E” and “L” CAMELS components, with weights of 28 percent each for the “C” and “M” components, 22 percent for the “A” component, and 11 percent for the “E” and “L” components. (For the regression, the “S” component is omitted.)

7. Revise Appendix B to Subpart A of Part 327 to read as follows:

**Appendix B to Subpart A**

**Description of Scorecard Measures**

(1) *Scorecard Measures Applied to All Large Banks*

Quantitative measures (Data Source)	Description
Tier 1 Common Capital Ratio (Call/TFR Reports).	The ratio is calculated as Tier 1 capital less perpetual preferred stock and related surplus divided by average total assets less disallowed intangibles.
Concentration Measure .....	Concentration score takes a higher score of the following two:
(1) Higher-Risk Concentrations Measure (LIDI).	The measure is a sum of following ratios squared: construction and development loans (C&D), leveraged loans, nontraditional mortgages, subprime consumer loans, and total exposure (outstanding loan balances and unfunded commitments) to top 20 single-name borrowers, all as a ratio to tier 1 capital and reserves.

Quantitative measures ( <i>Data Source</i> )	Description
(2) Growth-Adjusted Portfolio Concentrations ( <i>Call/TFR Reports</i> ).	<p>The measure is calculated in following steps:</p> <ol style="list-style-type: none"> <li>(1) Concentration levels (as a ratio to total risk-based capital) are calculated for each broad portfolio category (C&amp;D, other commercial real estate loans, residential mortgage (including mortgage-backed securities), commercial and industrial loans, credit card and other consumer loans).</li> <li>(2) Three-year merger-adjusted portfolio growth rates are then scaled to a growth factor of 1 and 1.5. If three years of data are not available, a growth factor of 1 would be assigned.</li> <li>(3) Risk weights are assigned to each category based on relative SCAP loss rates.</li> <li>(4) Concentration levels are multiplied by risk weights and growth factor and the resulting value for each portfolio is squared and summed.</li> </ol> <p>Both concentration measures are described in detail in Appendix C.</p>
Core Earnings/Average Total Assets ( <i>Call/TFR Reports</i> ).	<p>Core earnings are defined as quarterly net income less extraordinary items and realized gains and losses on available-for-sale (AFS) and held-to-maturity (HTM) securities, adjusted for mergers. The ratio takes a four-quarter sum of merger-adjusted core earnings and divides it by a five-quarter average of total assets. If four quarters of data on core earnings are not available, data for quarters that are available would be added and annualized. If five quarters of data on total assets are not available, data for quarters that are available would be averaged.</p>
Credit Quality Measure: ..... a. Criticized and Classified Items/Tier 1 Capital and Reserves ( <i>LIDI</i> ).	<p>Asset quality score takes a higher score of the following two:</p> <p>The sum of criticized and classified items divided by a sum of Tier 1 capital and reserves. Criticized and classified items include items with an internal grade of “Special Mention” or worse and include retail items under Uniform Retail Classification Guidelines, securities that are rated sub-investment grade, and marked-to-market counterparty positions with an internal grade of “Special Mention” or worse, or an external rating of sub-investment grade less credit valuation allowances (CVA). Criticized and classified items exclude loans and securities in trading books, and the maximum amount recoverable from the U.S. government, its agencies, or government-sponsored agencies, under guarantee or insurance provisions.</p>
b. Underperforming Assets/Tier 1 Capital and Reserves ( <i>Call/TFR Reports</i> ).	<p>Sum of loans past due 30–89 days, loans past due 90+ days, nonaccrual loans, restructured loans, restructured 1–4 family loans, and ORE (excluding the maximum amount recoverable from the U.S. government, its agencies, or government-sponsored agencies, under guarantee or insurance provisions) divided by a sum of Tier 1 capital and reserves.</p>
Core Deposits/Total Liabilities ( <i>Call/TFR Reports</i> ).	<p>The core deposit ratio is a sum of demand deposits, NOW accounts, MMDA, other savings deposits, CDs under \$100M less insured brokered deposits under \$100,000 divided by total liabilities.</p>
Unfunded Commitments/Total Assets ( <i>Call/TFR Reports</i> ).	<p>Unfunded commitments are unused portions of commitments to make or purchase extensions of credit in the form of loans or participations in loans, lease financing receivables, or similar transactions and include unused commitments for home equity line of credit, commercial real estate, construction and land development loans either secured or not secured by real estate, securities underwriting and others, excluding unused commitments for credit card lines. Total amount of unfunded commitments is divided by total assets.</p>
Liquid Assets/Short-term Liabilities (Liquidity Coverage Ratio) ( <i>Call/TFR Reports</i> ).	<p>Liquid assets are defined as the sum of cash and balances due from depository institutions, Federal funds sold and securities purchased under agreements to resell, and agency securities (securities issued by the U.S. Treasury, U.S. government agencies, and US government-sponsored enterprises) less securities sold under agreements to repurchase or agency securities, whichever is smaller. “Short-term” liabilities are defined as a sum of large CDs (larger than \$100,000) with a remaining maturity of one year or less, fed funds purchased and repos, unsecured borrowings with a remaining maturity of one year or less, foreign deposits and unused commitments for asset-backed commercial paper with a remaining maturity of one year or less.</p>
Potential Losses/Total Domestic Deposits (Loss Severity Measure) ( <i>Call/TFR Reports</i> ).	<p>The loss severity ratio is a ratio of potential losses to the DIF—as calculated in the FDIC’s loss severity model—to domestic deposits. Appendix D describes the loss severity model in detail.</p>
Secured Liabilities/Total Domestic Deposits ( <i>Call/TFR Reports</i> ).	<p>The secured liability ratio is a sum of secured liabilities (FHLB advances, securities sold under repurchase agreements, secured Federal funds purchased, and other secured borrowings) divided by domestic deposits.</p>

(2) Scorecard Measures Applied to Highly Complex Institutions Only

Quantitative measures	Description
10-day 99% VaR/Tier 1 Capital ( <i>LIDI Reports</i> ).	<p>The ratio is defined as 10-day 99%VaR based on banks’ internal model divided by Tier 1 capital.</p>
Short-term Funding/Total Assets ( <i>Call/TFR Reports</i> ).	<p>The short-term funding ratio is a ratio of a sum of Federal funds purchased and repos to total assets. If more granular maturity data are available, we may want to include non-deposit liabilities with a remaining maturity of three months or less.</p>
Senior Bond Spread ( <i>IDC</i> ) .....	<p>Quarterly average of median weekly spreads for senior bonds with three to ten years remaining to maturity issued by the parent company over comparable-maturity Treasuries.</p>
Parent TCE Ratio (9–Y Reports) ....	<p>The parent TCE ratio is a ratio of a sum of common stock, surplus, undivided profits, accumulated other comprehensive income, and other equity capital components less intangible assets to tangible assets (total assets less intangible assets).</p>

8. Revise Appendix C to Subpart A of Part 327 to read as follows:

## APPENDIX C TO SUBPART A

### Concentration Measures

The concentration measure score is a higher of the two concentration scores: a higher-risk concentration measure and a growth-adjusted portfolio concentration measure.

#### 1. Higher-Risk Concentration Measure

The higher-risk concentration measure is the sum of the squared value of concentrations in each of five risk areas and is calculated as:

$$H_i = \sum_{k=1}^5 \left( \frac{\text{Amount of exposure}_{i,k}}{\text{Tier 1 Capital}_i} \right)^2$$

Where:

H is institution *i*'s higher-risk concentration measure and

*k* is a risk area.<sup>1</sup> The five risk areas (*k*) are defined as:

- Construction and development loans;
- Leveraged lending;
- Nontraditional mortgages;
- Subprime consumer loans; and
- Total exposure (outstanding loan balances, unfunded commitments and counterparty credit risk) to top 20 single-name borrowers.

Data on higher-risk lending, other than construction and development loans, are obtained through an examination process and defined according to the interagency guidance for a given product. A loan is considered to be leveraged when the obligor's post-financing leverage as measured by debt-to-assets, debt-to-equity, cash flow-to-total debt, or other such standards unique to particular industries significantly exceeds industry norms for leverage.<sup>2</sup> Nontraditional

mortgages are mortgage products that allow borrowers to defer payment of principal and, sometimes, interest. These products include "interest-only" mortgages and "payment option" adjustable-rate mortgages.<sup>3</sup> Subprime loans are consumer loans that are typically made to borrowers with weakened credit histories, including a combination of payment delinquencies, charge-offs, judgments, and bankruptcies who may also display reduced repayment capacity as measured by credit scores, debt-to-income ratios, or other criteria.<sup>4</sup>

#### 2. Growth-adjusted Portfolio Concentration Measure

The growth-adjusted concentration measure is the sum of the squared values of concentrations in each of seven portfolios, each of the squared values being first adjusted for growth and risk weights before summing. The measure is calculated as:

$$N_i = \sum_{k=1}^7 \left[ g_{i,k} \times w_k \times \left( \frac{\text{Amount of exposure}_{i,k}}{\text{Total Capital}_i} \right) \right]^2$$

Where:

N is institution *i*'s growth-adjusted portfolio concentration measure<sup>5</sup>;

*k* is a portfolio;

*g* is a growth factor for institution *i*'s portfolio *k*; and,

*w* is a risk weight for portfolio *k*.

The seven portfolios (*k*) are defined based on the Call Report data and they are:

- First-lien residential mortgages and mortgage-backed securities;
- Closed-end junior liens and home equity lines of credit (HELOCs);
- Construction and development loans;
- Other commercial real estate loans;
- Commercial and industrial loans;
- Credit card loans; and
- Other consumer loans.

The growth factor, *g*, is based on a three-year merger-adjusted growth rate for a given portfolio; *g* ranges from 1 to 1.5 where a 20 percent growth rate equals a factor of 1 and an 80 percent growth rate equals a factor of 1.5.<sup>6</sup> For growth rates less than 20 percent, *g* is 1; for growth rates greater than 80 percent, *g* is 1.5. For growth rates of 20 percent to 80 percent, the growth factor is calculated as:

$$g_{i,k} = 1 + \left[ (G_{i,k} - 0.20) \times \frac{1.5 - 1.0}{0.8 - 0.2} \right] = 1 + \left[ \frac{5}{6} (G_{i,k} - 0.20) \right]$$

Where

$$G_{i,k} = \frac{V_{i,k,t}}{V_{i,k,t-12}} - 1,$$

V is the portfolio amount as reported on the Call Report and *t* is the quarter for which the assessment is being determined.

The risk weight for each portfolio reflects relative loss rates and is based on the mid-

point of two-year cumulative indicative loss rate ranges used in the adverse scenario for the interagency Supervisory Capital Assessment Program (SCAP) in early 2009.<sup>8</sup>

<sup>1</sup> The high-risk concentration measure is rounded to two decimal points.

<sup>2</sup> <http://www.fdic.gov/news/news/press/2001/pr0901a.html>.

<sup>3</sup> <http://www.fdic.gov/regulations/laws/federal/2006/06noticeFINAL.html>.

<sup>4</sup> Generally, subprime borrowers will display a range of credit risk characteristics that may include one or more of the following: (1) Two or more 30-day delinquencies in the last 12 months, or one or more 60-day delinquencies in the last 24 months; (2) judgment, foreclosure, repossession, or charge-off in the prior 24 months; (3) bankruptcy in the last 5 years; (4) relatively high default probability as

evidenced by, for example, a Fair Isaac and Co. risk score (FICO) of 660 or below (depending on the product/collateral), or other bureau or proprietary scores with an equivalent default probability likelihood; and/or (5) debt service-to-income ratio of 50 percent or greater, or otherwise limited ability to cover family living expenses after deducting total monthly debt-service requirements from monthly income. <http://www.fdic.gov/news/news/press/2001/pr0901a.html>.

<sup>5</sup> The growth-adjusted portfolio concentration measure is rounded to two decimal points.

<sup>6</sup> The cut-off values of 0.2 and 0.8 correspond to about 45th percentile and 80th percentile among

the large institutions, respectively, based on the data from 2000 to 2009.

<sup>7</sup> The growth factor is rounded to two decimal points.

<sup>8</sup> Board of Governors of the Federal Reserve System, "The Supervisory Capital Assessment Program: Overview of Results," May 7, 2009. <http://www.federalreserve.gov/newsevents/speech/bcreg20090507a1.pdf>.

<sup>9</sup> The risk weights are based on loss rates for each portfolio relative to the loss rate for C&I loans, which is given a risk weight of 1.

TABLE C.1—TWO-YEAR CUMULATIVE INDICATIVE LOSS RANGE: SCAP ADVERSE SCENARIO

Portfolio	Two-year cumulative loss range			Risk weights
	Minimum	Maximum	Midpoint	
First-Lien Mortgages*	4.3	5.8	5.1	0.8
Second/Junior Lien Mortgages	12.0	16.0	14.0	2.2
Commercial and Industrial (C&I) Loans	5.0	8.0	6.5	1.0
Construction and Development (C&D) Loans	15.0	18.0	16.5	2.5
Commercial Real Estate Loans, excluding C&D**	7.6	9.4	8.5	1.3
Credit Card Loans	18.0	20.0	19.0	2.9
Other Consumer Loans	8.0	12.0	10.0	1.5

\* Assumes that 80 percent of first liens are prime and the remaining 20 percent at Alt-A.

\*\* Assumes that 80 percent of CRE portfolio are nonfarm non-residential and the remaining 20 percent are multifamily. The allocation is based on the aggregate bank data.

9. Add Appendix D to Subpart A of Part 327 to read as follows:

**Appendix D to Subpart A**

**Description of the Loss Severity Model**

The FDIC's loss severity model applies a standardized set of assumptions to an institution's balance sheet for a given quarter to measure possible losses to the FDIC in the event of an institution's failure. To determine an institution's loss severity rate, the size and composition of an institution's liabilities are adjusted to reflect expected changes (due to uninsured deposit and other unsecured liability runoff and growth in insured deposits) as an institution approaches failure. Assets are then reduced to match any reduction in liabilities.<sup>1</sup> The institution's asset values are then further reduced until the Tier 1 leverage ratio reaches 2 percent.<sup>2</sup> Asset adjustments are made pro rata to asset categories to preserve the institution's relative proportion of assets by asset categories. Assumptions regarding asset losses at failure and the extent of secured liabilities are then applied to the estimated balance sheet at failure to determine whether the institution has enough unencumbered assets to cover domestic deposits. Any projected shortfall is divided by current domestic deposits to obtain an end-of-period loss severity ratio, which is then averaged over the three most recent quarters to produce the loss severity measure for the scorecard.

**Runoff and Capital Adjustment Assumptions**

Table D.1 contains run-off assumptions.

TABLE D.1—RUNOFF RATE ASSUMPTIONS

Liability type	Runoff rate* (percent)
Insured Deposits	- 32.0

<sup>1</sup> In most cases, the model would yield reductions in liabilities and assets prior to failure. Exceptions may occur for institutions primarily funded through

TABLE D.1—RUNOFF RATE ASSUMPTIONS—Continued

Liability type	Runoff rate* (percent)
Uninsured Deposits	28.6
Foreign Deposits	80.0
Fed Funds Purchased	40.0
Repurchase Agreements	25.0
Trading Liabilities	50.0
Federal Home Loan Bank Borrowings <= 1 Year	25.0
Federal Home Loan Bank Borrowings > 1 Year	0.0
Other Borrowings <= 1 Year	50.0
Other Borrowings > 1 Year	0.0
Subordinated Debt and Limited Liability Preferred Stock	15.0
Other Liabilities	0.0

\* A negative rate implies growth.

Given the resulting total liabilities after runoff, assets are then reduced pro rata to preserve the relative amount of assets in each of the following asset categories and to achieve a Tier 1 leverage of 2 percent:

- Cash and Interest Bearing Balances;
- Trading Account Assets;
- Fed Funds Sold and Repurchase Agreements;
- Treasury and Agency Securities;
- Municipal Securities;
- Other Securities;
- Construction and Development Loans;
- Nonresidential Real Estate Loans;
- Multifamily Real Estate Loans;
- 1-4 Family Closed-End First Liens;
- 1-4 Family Closed-End Junior Liens;
- Revolving Home Equity Loans; and
- Agricultural Real Estate Loans.

**Recovery Value of Assets at Failure**

Table D.2 shows loss rates applied to each of the asset categories as adjusted above.

insured deposits, which the model assumes to grow prior to failure.

<sup>2</sup> Of course, in reality, runoff and capital declines occur more or less simultaneously as an institution

TABLE D.2—ASSET LOSS RATE ASSUMPTIONS

Asset category	Loss rate (percent)
Cash and Interest Bearing Balances	0.0
Trading Account Assets	0.0
Fed Funds Sold and Repurchase Agreements	0.0
Treasury and Agency Securities	0.0
Municipal Securities	10.0
Other Securities	15.0
Construction and Development Loans	38.2
Nonresidential Real Estate Loans	17.6
Multifamily Real Estate Loans	10.8
1-4 Family Closed-End First Liens	19.4
1-4 Family Closed-End Junior Liens	41.0
Revolving Home Equity Loans	41.0
Agricultural Real Estate Loans	19.7
Agricultural Loans	11.8
Commercial and Industrial Loans	21.5
Credit Card Loans	18.3
Other Consumer Loans	18.3
All Other Loans	51.0
Other Assets	75.0

**Secured Liabilities at Failure**

Table D.3 shows the percentage of each liability category that is assumed to be secured.

TABLE D.3—SECURED LIABILITY ASSUMPTIONS

Liability type	Percentage secured at failure (percent)
Foreign Deposits	100
Repurchase Agreements	100
Federal Home Loan Bank Borrowings <= 1 Year	100

approaches failure. The loss severity measure assumptions simplify this process for ease of modeling.

TABLE D.3—SECURED LIABILITY ASSUMPTIONS—Continued

Liability type	Percentage secured at failure (percent)
Federal Home Loan Bank Borrowings > 1 Year .....	100
Other Borrowings <= 1 Year	50

TABLE D.3—SECURED LIABILITY ASSUMPTIONS—Continued

Liability type	Percentage secured at failure (percent)
Other Borrowings > 1 Year ..	50

**Loss Severity Ratio Calculation**

The FDIC's loss given failure (LGD) is calculated as:

$$LGD = \frac{InsuredDeposits_{Failure}}{DomesticDeposits_{Failure}} \times (DomesticDeposits_{Failure} - RecoveryValueofAssets_{Failure} + SecuredLiabilities_{Failure})$$

An end-of-quarter loss severity ratio is LGD divided by total domestic deposits at quarter-end and the loss severity measure for the

scorecard is an average of end-of-period loss severity ratio for three most recent quarters.

9. Add Appendix E to Subpart A of Part 327 to read as follows:

**Appendix E to Subpart A**

**Additional Risk Considerations for Large Institutions**

Information Source	Examples of Associated Risk Indicators or Information
Additional Performance Indicators	<p><i>Adequacy of Capital to Withstand Stress (Level and Trend)</i></p> <ul style="list-style-type: none"> <li>Regulatory capital ratios</li> <li>Capital composition</li> <li>Unrealized losses on securities</li> <li>Dividend payout ratios</li> <li>Internal capital growth rates relative to asset growth</li> <li>Robustness of internal stress testing models and reserve methodology</li> </ul> <p><i>Adequacy and Stability of Earnings to Withstand Stress (Level and Trend)</i></p> <ul style="list-style-type: none"> <li>Return on assets and return on risk-adjusted assets</li> <li>Concentration of revenue sources</li> <li>Earning composition including noncash earnings e.g., mortgage servicing rights (MSR), income from interest reserves) relative to core income</li> <li>Net interest margins, funding costs and volumes, earning asset yields and volumes</li> <li>Loan loss provisions relative to problem loans</li> <li>Historical volatility of various earnings sources</li> </ul> <p><i>Ability to Withstand Credit-Related Stress (Level and Trend)</i></p> <ul style="list-style-type: none"> <li>Loan and securities portfolio composition and volume of higher risk lending activities or securities</li> <li>Loan performance measures (past due, nonaccrual, classified and criticized, and renegotiated loans)</li> <li>Portfolio characteristics such as internal loan rating and credit score distributions, internal estimates of default, internal estimates of loss given default, and internal estimates of exposures in the event of default</li> <li>Portfolio underwriting characteristics and trends (including portfolio growth)</li> <li>Robustness of credit administration and credit risk monitoring (e.g., internal loan classification)</li> <li>Off-balance sheet credit exposure measures (unfunded loan commitments, securitization activities, counterparty derivatives exposures) and hedging activities</li> </ul> <p><i>Ability to Withstand Liquidity-Related Stress (Level and Trend)</i></p> <ul style="list-style-type: none"> <li>Composition of deposit and non-deposit funding sources</li> <li>Liquid resources relative to short-term obligations, undisbursed credit lines, and contingent liabilities</li> <li>Reliance on securitization as a funding source</li> <li>Level of contingent liabilities</li> <li>Robustness of contingency or emergency funding strategies and analyses</li> </ul> <p><i>Ability to Withstand Interest Rate Shocks</i></p> <ul style="list-style-type: none"> <li>Maturity and repricing information on assets and liabilities, interest rate risk analyses</li> <li>Robustness of internal interest rate models</li> </ul> <p><i>Ability to Withstand Trading Stress (Level and Trend)</i></p> <ul style="list-style-type: none"> <li>Assessment of trading desk composition and revenue dependency (prop trading compared to customer flow, liquid products compared to illiquid products)</li> <li>Assessment of VaR framework, stress testing framework and results</li> <li>Appropriateness of desk limits.</li> </ul> <p><i>Ability to Withstand Stress to Counterparties (Level and Trend)</i></p> <ul style="list-style-type: none"> <li>Gross current exposure (Top 5 and Total by Client Types and Ratings) to capital</li> <li>Current net exposure (Top 5 and Total by Client Types and Ratings) to capital</li> <li>Peak potential exposure (Top 5 and Total by Client Types and Ratings) to capital</li> <li>Exposure aggregation reporting</li> <li>Margining policies, netting enforceability and hedging capabilities.</li> </ul> <p><i>Market indicator of the institution's ability to withstand stress (Level and Trend)</i></p>

Information Source	Examples of Associated Risk Indicators or Information
Additional Loss Severity Indicators .....	<ul style="list-style-type: none"> <li>• Subordinated debt spreads</li> <li>• Credit default swap spreads</li> <li>• Parent's equity price volatility</li> <li>• Market-based measures of default probabilities</li> <li>• Rating agency watch lists</li> <li>• Market analyst reports</li> </ul> <ul style="list-style-type: none"> <li>• Ability to identify and describe discreet business units within the banking legal entity</li> <li>• Funding structure considerations relating to the order of claims in the event of liquidation (including the extent of subordinated claims and priority claims).</li> <li>• Volumes of brokered deposits, potentially more volatile deposits such as Internet or money desk or high-cost deposits.</li> <li>• Potential for significant ring-fencing of foreign assets.</li> <li>• Volume of hard-to-value assets (Level 3 assets)</li> </ul>

**Note:** The following Appendices will not appear in the Code of Federal Regulations.

**Appendix 1**

**Statistical Analysis of Measures**

The risk measures included in the scorecard and the weights assigned to those measures are generally based on the results of an ordinary least square (OLS) model, and in some cases, a logistic regression model.

The OLS model estimates how well a set of risk measures in 2005 through 2009 can predict the FDIC's view, based on its experience and judgment, of the proper rank ordering of risk (the expert judgment ranking) for large institutions as of year-end 2009.

The OLS model is specified as:

$$Ranking_{i,2009} = \beta_0 + \sum_{k=1}^n \beta_k \times Score_{i,k,t}$$

Where:

*k* is a risk measure;

*n* is the number of risk measures; and

*t* is the quarter that is being assessed

The logistic regression model estimates how well the same set of risk measures in

2005 through 2008 can predict whether a large bank fails and it is specified as:

$$Fail(0,1)_i = \beta_0 + \sum_{k=1}^n \beta_k \times Score_{i,k,t}$$

Where:

*Fail* is whether an institution *i* failed on or prior to year-end 2009 or not.<sup>1</sup>

**Selecting Risk Measures<sup>2</sup>**

To select the risk measures for the scorecard, the FDIC first selected a set of financial measures that were deemed to be most relevant to assessing large institutions' ability to withstand stress. Those measures were converted to a score between 0 and 100

and then regressed against the expert judgment ranking. A stepwise selection method was used to select risk measures for each year that were statistically significant at a 15 percent confidence level or better.

Table 1.1 shows the risk measures that were considered and descriptive statistics of scores for those measures for large institutions based on data from 2005–2009. Most of these measures, other than concentration and credit quality measures, are based on report

of condition and income data and defined in Appendix 1. The concentration measure is described in detail in Appendix 2. A distance-to-default measure is calculated as a sum of Tier 1 capital and 12-quarter average core earnings—both divided by total assets—divided by the 12-quarter standard deviation in core earnings. The three-year merger-adjusted asset growth rate (AG) is calculated as:

$$AG = \frac{Asset_t}{Asset_{t-12}}$$

Where *t* is the quarter for which the assessment is being determined.

<sup>1</sup> For the purpose of regression analysis, large institutions that received significant government support or merged with another entity with government support.

<sup>2</sup> The FDIC has conducted a number of robustness tests with alternative ratios for capital and earnings, a log transformation of several variables—the

liquidity coverage ratio, the brokered deposit ratio and the growth-adjusted concentration ratio—and alternative dependent variables—CAMELS and the FDIC's internal risk ratings. These robustness tests show that the same set of variables are generally statistically significant in most models; that converting to a score from a raw ratio generally

resolves any potential concern related to a nonlinear relationship between the dependent variable and several explanatory variables; and, finally, that alternative ratios for capital and earnings are not better in predicting expert judgment ranking or failure.

TABLE 1.1—DESCRIPTIVE STATISTICS OF RISK MEASURE SCORES

Risk measure	Average score	Median score	Standard deviation of scores
Weighted average CAMELS rating .....	41.4	39.9	14.3
Tier 1 common leverage ratio .....	65.4	74.7	30.5
Distance-to-default .....	62.2	73.7	34.8
Concentration measure .....	52.2	46.0	36.3
Three-year merger-adjusted asset growth rate .....	27.0	15.7	30.5
Core earnings/average assets .....	56.6	55.4	30.0
Credit quality measure .....	43.2	33.7	35.2
Core deposits/total liabilities .....	41.5	33.2	32.9
Liquidity coverage ratio .....	75.1	89.9	31.5
Unfunded commitments/total assets .....	49.1	51.4	32.1
Short-term funding/total assets .....	32.8	24.8	31.8
Loss severity ratio .....	43.3	43.5	30.0
Secured liabilities/total domestic deposits .....	31.3	21.2	31.7
Brokered deposits/total domestic deposits .....	22.3	5.7	33.8

Table 1.2 shows the results of the OLS models after a stepwise selection process and the statistical significance of each measure for years 2005 through 2009. The dependent variable for the model is an expert judgment ranking as of year-end 2009. The measures numbered (1) through (9) are statistically

significant and have a positive sign in regression models for multiple years. Those measures include a weighted average CAMELS rating, a concentration measure, a core earnings to average total assets ratio, a credit quality measure, a core deposits to total liabilities ratio, an unfunded

commitments to total assets ratio, a liquid assets to short-term liabilities ratio, a loss severity measure, and a secured liabilities to total domestic deposits ratio. The measures without coefficients are those that are not statistically significant at a 15 percent confidence level.

Table 1.2

## OLS Stepwise Regression Results

Dependent Variable = Expert Judgment Ranking as of Year-end 2009

Measure Scores	2005	2006	2007	2008	2009
(1) Weighted average CAMELS rating	1.13 *** (0.12)	0.76 *** (0.13)	0.40 *** (0.11)	0.32 *** (0.07)	0.77 *** (0.05)
Tier 1 common capital ratio					
Distance-to-default	-0.26 *** (0.03)	-0.13 *** (0.03)		0.07 * (0.04)	0.19 *** (0.04)
(2) Concentration measure	0.27 *** (0.03)	0.29 *** (0.03)	0.36 *** (0.03)	0.19 *** (0.03)	0.05 ** (0.03)
3-year merger-adjusted asset growth			-0.11 *** (0.04)	-0.12 *** (0.03)	-0.06 ** (0.03)
(3) Core Earnings/Average Total Assets			0.18 *** (0.04)	0.15 *** (0.03)	0.06 * (0.03)
(4) Credit quality measure	0.38 *** (0.05)	0.34 *** (0.05)	0.31 *** (0.04)	0.38 *** (0.04)	0.34 *** (0.03)
(5) Core deposits/total liabilities	0.22 *** (0.04)	0.18 *** (0.05)	0.11 *** (0.04)	0.20 *** (0.04)	
(6) Unfunded Commitments/Total Assets	0.09 *** (0.03)	0.12 *** (0.04)	0.15 *** (0.03)	0.06 * (0.03)	-0.07 ** (0.03)
(7) Liquid Assets/Short-term Liabilities			0.16 *** (0.04)		0.07 ** (0.03)
Short-term funding/total assets		-0.06 (0.04)	-0.09 *** (0.03)	-0.06 ** (0.03)	-0.07 ** (0.03)
(8) Loss severity measure	0.17 *** (0.04)	0.17 *** (0.05)	0.19 *** (0.04)	0.17 *** (0.03)	0.06 *** (0.03)
(9) Secured liabilities/total domestic deposits	0.23 *** (0.04)	0.18 *** (0.05)			0.07 ** (0.03)
Brokered deposits/total domestic deposits					0.12 *** (0.03)
No. Obs	450	454	455	450	436
Adjust. R2	0.55	0.50	0.62	0.71	0.76

Note Standard error in parenthesis

\* Significant at the 10% level \*\* Significant at the 5% Level \*\*\* Significant at the 1% Level

Table 1.3 shows the results of the logistic regression models with a stepwise selection process, and the statistical significance of each measure for years 2005 through 2008. The dependent variable for the model is whether an institution failed before year-end

2009 or not. The risk measures numbered (1) through (5) are statistically significant and have a positive sign in regression models for multiple years. Two additional measures—credit quality measure and unfunded commitments/total assets—are significant in

a regression model for a single year. One measure—a Tier 1 common capital ratio—that is not significant in the OLS model are significant in the logistic regression model.

Table 1.3

## Logistic Stepwise Regression Results

Dependent Variable (1 = Failed; 0 = Not failed)

Measure Scores	2005	2006	2007	2008	2009
(1) Weighted average CAMELS rating	0.06 *** (0.02)	0.06 *** (0.02)	0.13 *** (0.03)	0.07 *** (0.02)	0.09 *** (0.02)
(2) Tier 1 common capital ratio	0.02 ** (0.01)		0.03 *** (0.01)		0.06 *** (0.02)
Distance-to-default					
(3) Concentration measure	0.04 *** (0.01)	0.06 *** (0.01)	0.08 *** (0.02)	0.06 *** (0.01)	
3-year merger-adjusted asset growth					
Core Earnings/Average Total Assets			-0.03 ** (0.01)		
Credit quality measure				0.08 *** (0.03)	
Core deposits/total liabilities		-0.03 *** (0.01)			
(4) Unfunded Commitments/Total Assets	0.05 ** (0.02)	0.07 ** (0.03)	0.04 *** (0.01)		
Liquid Assets/Short-term Liabilities		0.02 ** (0.01)			
Short-term funding/total assets	-0.03 *** (0.01)	-0.05 *** (0.01)	-0.09 *** (0.02)	-0.05 *** (0.01)	-0.04 *** (0.01)
Loss severity measure	0.01 *** (0.01)			-0.04 *** (0.01)	-0.05 *** (0.01)
(5) Secured liabilities/total domestic deposits		0.04 *** (0.01)	0.03 *** (0.01)	0.03 *** (0.01)	0.02 *** (0.01)
Brokered deposits/total domestic deposits			-0.03 *** (0.01)	-0.03 *** (0.01)	
Model Log Likelihood	-114.57	-90.16	-66.21	-58.65	-50.95

Note: Standard error in parenthesis

\* Significant at the 10% level \*\* Significant at the 5% Level \*\*\* Significant at the 1% Level

**Determining Risk Measures Weights**

Table 1.4 shows the results of the OLS model with all ten risk measures that were significant in predicting either the expert judgment ranking or failure. The weights assigned to each of ten risk measures in the scorecard are generally, but not entirely, based on the coefficients for OLS models for 2006 and 2007. For example, the coefficient for the core earnings to average total asset ratio is 0.16 in 2007, and the proposal assigns a weight of 15 percent to core earnings to calculate an institution's ability to withstand asset-related stress score. The coefficients for the concentration measure and credit quality measure are 0.34, and a 35-percent weight is

assigned to each of these measures. The coefficient for the liquid assets to short-term funding (liquidity coverage) ratio is 0.14 in 2007 and the proposal assigns a weight of 20 percent to the liquidity coverage ratio to calculate an institution's ability to withstand funding-related stress score. The coefficients for the core deposits to total liabilities ratio and the unfunded commitments to total assets ratio are 0.20 and 0.12, respectively, in 2006 (and 0.10 and 0.16, respectively, in 2007), and a 40-percent weight is assigned to both these measures to calculate an institution's ability to withstand funding-related stress score.

The weights assigned to the Tier 1 common capital ratio, the 10-day 99-percent VaR to

Tier 1 capital ratio, and the short-term funding to total assets ratio are not based on the OLS regression. For the Tier 1 common capital ratio, the 15-percent weight assigned in the large institution scorecard (and the 10-percent weight assigned in the highly complex institution scorecard) reflects its importance in predicting bank failure. A 10-day 99-percent VaR to Tier 1 capital ratio is a consistent measure of market risk that is important for highly complex institutions. Finally, while the OLS regression does not show a statistical significance, reliance on short-term funding had an effect on how highly complex institutions fared over the past four years.

Table 1.4

## OLS Regression Results: Proposed Measures

Dependent Variable = Expert Judgment Ranking as of Year-end 2009

Measure Scores	2005	2006	2007	2008	2009
Weighted Average CAMELS	0.89 *** (0.12)	0.64 *** (0.14)	0.41 *** (0.12)	0.36 *** (0.08)	0.89 *** (0.05)
Tier 1 common capital ratio	0.06 (0.05)	0.08 * (0.05)	0.02 (0.04)	0.01 (0.04)	-0.01 (0.03)
Concentration Measure	0.27 *** (0.03)	0.29 *** (0.03)	0.34 *** (0.03)	0.18 *** (0.03)	0.07 ** (0.03)
Core Earnings/Average Total Assets	-0.05 (0.05)	0.02 (0.05)	0.16 *** (0.04)	0.16 *** (0.03)	0.13 *** (0.03)
Credit quality measure	0.26 *** (0.06)	0.28 *** (0.05)	0.34 *** (0.04)	0.42 *** (0.03)	0.36 *** (0.03)
Core deposits/total liabilities	0.16 *** (0.05)	0.20 *** (0.05)	0.10 ** (0.05)	0.17 *** (0.04)	0.11 *** (0.04)
Unfunded Commitments/Total Assets	0.06 (0.04)	0.12 *** (0.04)	0.16 *** (0.03)	0.06 * (0.03)	-0.06 ** (0.03)
Liquid Assets/Short-term Liabilities	0.06 (0.05)	0.02 (0.04)	0.14 *** (0.04)	0.03 (0.03)	0.04 (0.03)
Loss severity measure	0.21 *** (0.04)	0.21 *** (0.05)	0.22 *** (0.05)	0.17 *** (0.04)	0.07 ** (0.03)
Secured liabilities/total domestic deposits	0.17 *** (0.05)	0.10 * (0.05)	-0.04 (0.05)	0.01 (0.04)	-0.03 (0.04)
No. Obs	453	455	455	450	434
Adjust. R2	0.49	0.49	0.61	0.69	0.74

Note: Standard error in parenthesis

\* Significant at the 10% level \*\* Significant at the 5% Level \*\*\* Significant at the 1% Level

**OLS regression results: CAMELS and the Current Small Bank Financial Ratios**

Table 1.5 shows the results of the OLS regression model with the weighted average

CAMELS rating only. These results show that while the weighted average CAMELS rating is statistically significant in predicting an expert judgment ranking as of year-end 2009,

it only explains a small percentage of the variation in the year-end 2009 expert judgment ranking—particularly in models for 2005 (10 percent) through 2007 (19 percent).

Table 1.5

## OLS Regression Results: Weighted Average CAMELS

Dependent Variable = Expert Judgment Ranking as of Year-end 2009

Variable	2005	2006	2007	2008	2009
Weighted Average CAMELS	27.40 *** (3.78)	30.44 *** (3.65)	34.51 *** (3.34)	36.08 *** (2.13)	36.05 *** (1.51)
No. Obs	439	445	446	439	421
Adjust. R2	0.10	0.13	0.19	0.40	0.58

Note: Standard error in parenthesis

\* Significant at the 10% level \*\* Significant at the 5% Level \*\*\* Significant at the 1% Level

Table 1.6 shows the results of the OLS regression model with a weighted average CAMELS rating and the current small bank financial ratios. These results show that adding financial ratios improves the ability to

predict the year-end 2009 expert judgment ranking; however, the improvement is not as significant as in the model with proposed measures. For example, in 2006, the model with current small bank financial ratios

would have predicted slightly over 20 percent of the variation in the current expert judgment ranking. This compares to nearly 50 percent for the model with proposed measures.

Table 1.6

## OLS Regression Results: Current Small Bank Financial Ratios

Dependent Variable = Expert Judgment Ranking as of Year-end 2009

Measure Scores	2005	2006	2007	2008	2009
Weighted average CAMELS rating	24.53 *** (3.73)	23.18 *** (3.78)	22.92 *** (3.70)	22.19 *** (2.96)	25.87 *** (2.29)
Tier 1 Leverage Ratio	-0.43 ** (0.19)	-0.47 ** (0.22)	-1.23 *** (0.31)	-0.45 (0.36)	-0.05 (0.29)
Loans Past Due 30-89 Days/Gross Assets	7.81 ** (3.90)	16.02 *** (3.53)	9.32 *** (1.86)	8.81 *** (2.22)	5.16 *** (1.45)
Nonperforming Assets/Gross Assets	30.00 *** (6.36)	9.97 *** (3.32)	5.00 *** (1.60)	2.15 ** (0.91)	2.60 *** (0.65)
Net Loan Charge-Offs/Gross Assets	-14.21 *** (2.88)	-12.38 *** (2.91)	-3.89 (2.51)	-3.03 ** (1.45)	-1.19 (0.74)
Net Income before Taxes/Risk-Weighted Assets	-0.03 (0.67)	-0.58 (0.63)	-1.94 ** (0.80)	-0.95 ** (0.43)	-0.25 * (0.13)
Adjusted Brokered Deposit Ratio	0.16 *** (0.06)	0.12 ** (0.06)	0.17 *** (0.05)	0.12 *** (0.04)	0.08 ** (0.04)
No. Obs	445	451	452	445	427
Adjust. R2	0.19	0.21	0.32	0.48	0.64

Note: Standard error in parenthesis

\* Significant at the 10% level \*\* Significant at the 5% Level \*\*\* Significant at the 1% Level

## Appendix 2

## Conversion of Total Score Into Initial Base Assessment Rate

The formula for converting an institution's total score into an initial assessment rate is based on a single-variable logistic regression model, which uses an institution's total score

as of year-end 2006 to predict whether the institution has failed on or before year-end 2009. The logistic model is specified as:

$$\text{Fail}(0,1)_i = -7.7660 + (0.0875 \times \text{Score}_{i,2006})$$

Where:

*Fail* is whether an institution *i* failed on or before year-end 2009 or not; and <sup>3</sup>

*Score* is an institution *i*'s total score as of year-end 2006.

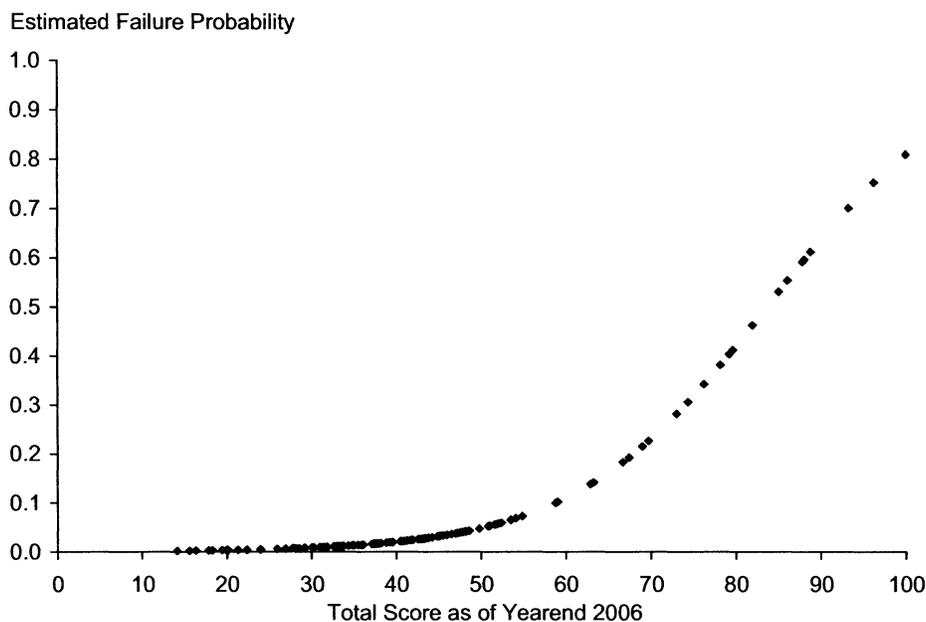
The plotted points in Chart 5.1 show the estimated failure probabilities for the actual total scores using the logistic model and the results are nonlinear.

<sup>3</sup> For the purpose of regression analysis, large institutions that received significant government

support or merged with another entity with government support are deemed to have failed.

Chart 2.1

## Estimated Failure Probabilities Based on Total Score as of Year-end 2006



The proposed calculation of the initial assessment rates approximates this nonlinear relationship for scores between 30 and 90. A score of 30 or lower results in the minimum

initial base assessment rate and a score of 90 or higher results in the maximum initial base assessment rate. Assuming an assessment rate range of 40 basis points, the initial base

assessment rate for an institution with a score greater than 30 and less than 90 would be:

$$Rate = MinimumRate - 0.165289 + \left( 68.02027 \times \left( \frac{Score}{100} \right)^5 \right)$$

### Appendix 3

#### Analysis of the Projected Effects of the Payment of Assessments on the Capital and Earnings of Insured Depository Institutions

This analysis estimates the effect in 2010 of deposit insurance assessments on the equity capital and profitability of all insured institutions, based on the total base assessment rates adopted in the final rule. For purposes of determining pre-tax, pre-assessment income in 2010, the analysis assumes that income in 2010 will equal annualized income for the second half of 2009, adjusted for mergers.

While deposit insurance assessments (whatever the rate) generally will result in reduced institution profitability and capitalization compared to the absence of assessments, the reduction will not necessarily equal the full amount of the assessment. Two factors can mitigate the effect of assessments on institutions' profits and capital. First, a portion of the assessment may be transferred to customers in the form of higher borrowing rates, increased service fees and lower deposit interest rates. Since information is not readily available on the extent to which institutions are able to share assessment costs with their customers,

however, this analysis assumes that institutions bear the full after-tax cost of the assessment. Second, deposit insurance assessments are a tax-deductible operating expense; therefore, the assessment expense can lower taxable income. This analysis considers the effective after-tax cost of assessments in calculating the effect on capital.

An institution's earnings retention and dividend policies also influence the extent to which assessments affect equity levels. If an institution maintains the same dollar amount of dividends when it pays a deposit insurance assessment as when it does not, equity (retained earnings) will be less by the full amount of the after-tax cost of the assessment. This analysis instead assumes that an institution will maintain its dividend rate (that is, dividends as a fraction of net income) unchanged from the weighted average rate reported over the four quarters ending December 31, 2009. In the event that the ratio of equity to assets falls below 4 percent, however, this assumption is modified such that an institution retains the amount necessary to achieve a 4 percent minimum and distributes any remaining funds according to the dividend payout rate.

The proposed changes involve increases in premiums for some institutions and reductions in premiums for other institutions. Because overall revenue remains almost constant, the effect on aggregate earnings and capital is small. Projections show that imposition of the new premiums will increase aggregate capital by 2 one-hundredths of one percent (0.02 percent) over one year. For institutions whose initial earnings are positive, the change in premiums will increase earnings by an average of 0.87 percent (on an asset weighted basis). For institutions whose initial earnings are negative, the change in premiums will increase losses by an average of 0.85 percent (on an asset weighted basis).

There are two institutions for which the imposition of the new premiums would make a critical difference that would cause their tier 1 capital ratio to fall below 2 percent over a one-year horizon. A check was also made whether the imposition of the new premiums would make a difference in whether an institution's equity-to-capital ratio would fall below 4 percent in a one-year horizon, but there are no institutions critically affected in this way.

Among current Risk Category I institutions, 6,030 institutions' assessment rates would

decrease, 28 institutions' assessment rates would increase and 2 institutions' assessment rates would remain unchanged. All of the institutions whose rates would increase are large institutions as currently defined. For institutions whose assessment rates would decrease and whose earnings would otherwise be positive, earnings would increase by an average of 1.2 percent (on an asset weighted basis). For institutions whose assessment rates would decrease and whose earnings would otherwise be negative, losses would decline by an average of 1.0 percent (on an asset weighted basis). For institutions whose assessment rates would increase and whose earnings would otherwise be positive, earnings would decrease by an average of 1.6 percent. For institutions whose assessment rates would increase and whose earnings would otherwise be negative, losses would increase by an average of 4.8 percent.

Among current Risk Category II institutions, 11 institutions' assessment rates

would decrease, 16 institutions' assessment rates would increase and 1,182 institutions' assessment rates (including the rates for all small Risk Category II institutions) would remain unchanged. For institutions whose assessment rates would decrease and whose earnings would otherwise be positive, earnings would increase by an average of 25.5 percent (on an asset weighted basis). For institutions whose assessment rates would decrease and whose earnings would otherwise be negative, losses would decline by an average of 2.1 percent (on an asset weighted basis). For institutions whose assessment rates would increase and whose earnings would otherwise be positive, earnings would decrease by an average of 2.5 percent (on an asset weighted basis). For institutions whose assessment rates would increase and whose earnings would otherwise be negative, losses would increase by an average of 4.1 percent (on an asset weighted basis).

Among current Risk Category III and IV institutions, 728 out of 729 institutions' assessment rates would increase. For institutions whose assessment rates would increase and whose earnings would otherwise be positive, earnings would be reduced by an average of 0.9 percent (on an asset weighted basis). For institutions whose assessment rates would increase and whose earnings would otherwise be negative, losses would increase by an average of 1.0 percent (on an asset weighted basis).

By order of the Board of Directors.

Dated at Washington, DC, this 13th day of April 2010.

Federal Deposit Insurance Corporation.

**Robert E. Feldman,**

*Executive Secretary.*

[FR Doc. 2010-10161 Filed 4-30-10; 8:45 am]

**BILLING CODE 6714-01-P**