

FEDERAL DEPOSIT INSURANCE CORPORATION

12 CFR Part 327

RIN 3064-AD35

Assessments

AGENCY: Federal Deposit Insurance Corporation (FDIC).

ACTION: Notice of proposed rulemaking and request for comment.

SUMMARY: The FDIC is proposing to amend 12 CFR part 327 to: Alter the way in which it differentiates for risk in the risk-based assessment system; revise deposit insurance assessment rates, including base assessment rates; and make technical and other changes to the rules governing the risk-based assessment system.

DATES: Comments must be received on or before November 17, 2008.

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. 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. All comments received will be posted without change to <http://www.fdic.gov/regulations/laws/federal/propose.html> including any personal information provided.

FOR FURTHER INFORMATION CONTACT:

Munsell W. St. Clair, Chief, Banking and Regulatory Policy Section, Division of Insurance and Research, (202) 898-8967; and Christopher Bellotto, Counsel, Legal Division, (202) 898-3801.

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 Act of 2005 (collectively,

the Reform Act).¹ The Reform Act enacted the bulk of the recommendations made by the FDIC in 2001.² The Reform Act, among other things, required that the FDIC, “prescribe final regulations, after notice and opportunity for comment * * * providing for assessments under section 7(b) of the Federal Deposit Insurance Act, as amended * * *,” thus giving the FDIC, through its rulemaking authority, the opportunity to better price deposit insurance for risk.³

The Federal Deposit Insurance Act, as amended by the Reform Act, continues to require 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 due to the composition and concentration of the institution’s assets and liabilities, the amount of loss given failure, and revenue needs of the Deposit Insurance Fund (the fund or DIF).⁴

Before passage of the Reform Act, the deposit insurance funds’ target reserve ratio—the designated reserve ratio (DRR)—was generally set at 1.25 percent. Under the Reform Act, however, the FDIC may set the DRR within a range of 1.15 percent to 1.50 percent of estimated insured deposits. If the reserve ratio drops below 1.15 percent—or if the FDIC expects it to do so within six months—the FDIC must, within 90 days, establish and implement a plan to restore the DIF to 1.15 percent within five years (absent extraordinary circumstances).⁵

The FDIC may restrict the use of assessment credits during any period that a restoration plan is in effect. By statute, however, institutions may apply credits towards any assessment imposed, for any assessment period, in an amount equal to the lesser of (1) the amount of the assessment, or (2) the

amount equal to three basis points of the institution’s assessment base.⁶

The Reform Act also restored to the FDIC’s Board of Directors the discretion to price deposit insurance according to risk for all insured institutions regardless of the level of the fund reserve ratio.⁷

The Reform Act left in place the existing statutory provision allowing the FDIC to “establish separate risk-based assessment systems for large and small members of the Deposit Insurance Fund.”⁸ Under the Reform Act, however, separate systems are subject to a new requirement that “[n]o insured depository institution shall be barred from the lowest-risk category solely because of size.”⁹

The 2006 Assessments Rule

Overview

On November 30, 2006, the FDIC published in the **Federal Register** a final rule on the risk-based assessment system (the 2006 assessments rule).¹⁰ The rule became effective on January 1, 2007.

The 2006 assessments rule created four risk categories and named them Risk Categories I, II, III and IV. These four categories are based on two criteria: capital levels and supervisory ratings. Three capital groups—well capitalized, adequately capitalized, and undercapitalized—are based on the leverage ratio and risk-based capital ratios for regulatory capital purposes. Three supervisory groups, termed A, B, and C, are based upon the FDIC’s consideration of evaluations provided by the institution’s primary federal

⁶ Section 7(b)(3)(E)(iii) of the Federal Deposit Insurance Act (12 U.S.C. 1817(b)(E)(iii)).

⁷ The Reform Act eliminated the prohibition against charging well-managed and well-capitalized institutions when the deposit insurance fund is at or above, and is expected to remain at or above, the designated reserve ratio (DRR). This prohibition was included as part of the Deposit Insurance Funds Act of 1996. Public Law 104-208, 110 Stat. 3009, 3009-479. However, while the Reform Act allows the DRR to be set between 1.15 percent and 1.50 percent, it also generally requires dividends of one-half of any amount in the fund in excess of the amount required to maintain the reserve ratio at 1.35 percent when the insurance fund reserve ratio exceeds 1.35 percent at the end of any year. The Board can suspend these dividends under certain circumstances. The Reform Act also requires dividends of all of the amount in excess of the amount needed to maintain the reserve ratio at 1.50 when the insurance fund reserve ratio exceeds 1.50 percent at the end of any year. 12 U.S.C. 1817(e)(2).

⁸ Section 7(b)(1)(D) of the Federal Deposit Insurance Act (12 U.S.C. 1817(b)(1)(D)).

⁹ 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)).

¹⁰ 71 FR 69282. 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.

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

² After a year long review of the deposit insurance system, the FDIC made several recommendations to Congress to reform the deposit insurance system. See <http://www.fdic.gov/deposit/insurance/initiative/direcommendations.html> for details.

³ Section 2109(a)(5) of the Reform Act. Section 7(b) of the Federal Deposit Insurance Act (12 U.S.C. 1817(b)).

⁴ 12 Section 7(b)(1)(C) of the Federal Deposit Insurance Act (12 U.S.C. 1817(b)(1)(C)). The Reform Act merged the former Bank Insurance Fund and Savings Association Insurance Fund into the Deposit Insurance Fund.

⁵ Section 7(b)(3)(E) of the Federal Deposit Insurance Act (12 U.S.C. 1817(b)(3)(E)).

regulator and other information the FDIC deems relevant.¹¹ Group A consists of financially sound institutions with only a few minor weaknesses; Group B 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 insurance fund; and Group C consists of institutions that pose a substantial probability of loss to the insurance fund unless effective corrective action is taken.¹² Under the

2006 assessments rule, an institution's capital and supervisory groups determine its risk category as set forth in Table 1 below. (Risk categories appear in Roman numerals.)

TABLE 1—DETERMINATION OF RISK CATEGORY

Capital category	Supervisory group		
	A	B	C
Well Capitalized	I		
Adequately Capitalized		II	
Undercapitalized		III	III IV

The 2006 assessments rule established the following base rate schedule and allowed the FDIC Board to adjust rates uniformly from one quarter to the next

up to three basis points above or below the base schedule, provided that no single change from one quarter to the next can exceed three basis points.¹³

Base assessment rates within Risk Category I vary from 2 to 4 basis points, as set forth in Table 2 below.

TABLE 2—CURRENT BASE ASSESSMENT RATES

	Risk category				
	I*		II	III	IV
	Minimum	Maximum			
Annual Rates (in basis points)	2	4	7	25	40

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

The 2006 assessments rule set actual rates beginning January 1, 2007, as set out in Table 3 below.

TABLE 3—CURRENT ASSESSMENT RATES

	Risk category				
	I*		II	III	IV
	Minimum	Maximum			
Annual Rates (in basis points)	5	7	10	28	43

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

These rates remain in effect. Any increase in rates above the actual rates in effect requires a new notice-and-comment rulemaking.

Risk Category I

Within Risk Category I, the 2006 assessments rule charges those institutions that pose the least risk a minimum assessment rate and those that pose the greatest risk a maximum

assessment rate two basis points higher than the minimum rate. The rule charges other institutions within Risk Category I a rate that varies incrementally by institution between the minimum and maximum.

Within Risk Category I, the 2006 assessments rule combines supervisory ratings with other risk measures to further differentiate risk and determine assessment rates. The *financial ratios*

method determines the assessment rates for most institutions in Risk Category I using a combination of weighted CAMELS component ratings and the following financial ratios:

- The Tier 1 Leverage Ratio;
 - Loans past due 30–89 days/gross assets;
 - Nonperforming assets/gross assets;
 - Net loan charge-offs/gross assets;
- and

¹¹ The term “primary federal regulator” is synonymous with the statutory term “appropriate federal banking agency.” Section 3(q) of the Federal Deposit Insurance Act (12 U.S.C. 1813(q)).

¹² The capital groups and the supervisory groups have been in effect since 1993. In practice, the supervisory group evaluations are generally based on an institution's composite CAMELS rating, a

rating assigned by the institution's supervisor at the end of a bank examination, with 1 being the best rating and 5 being the lowest. CAMELS is an acronym for component ratings assigned in a bank examination: Capital adequacy, Asset quality, Management, Earnings, Liquidity, and Sensitivity to market risk. A composite CAMELS rating combines these component ratings, which also range from 1

(best) to 5 (worst). Generally speaking, institutions with a CAMELS rating of 1 or 2 are put in supervisory group A, those with a CAMELS rating of 3 are put in group B, and those with a CAMELS rating of 4 or 5 are put in group C.

¹³ The Board cannot adjust rates more than 2 basis points below the base rate schedule because rates cannot be less than zero.

- Net income before taxes/risk-weighted assets.

The weighted CAMELS components and financial ratios are multiplied by statistically derived pricing multipliers and the products, along with a uniform amount applicable to all institutions subject to the financial ratios method, are summed to derive the assessment rate under the base rate schedule. If the rate derived is below the minimum for Risk Category I, however, the institution will pay the minimum assessment rate for the risk category; if the rate derived is above the maximum rate for Risk Category I, then the institution will pay the maximum rate for the risk category.

The multipliers and uniform amount were derived in such a way to ensure that, as of June 30, 2006, 45 percent of small Risk Category I institutions (other than institutions less than 5 years old) would have been charged the minimum rate and approximately 5 percent would have been charged the maximum rate. While the FDIC has not changed the multipliers and uniform amount since adoption of the 2006 assessments rule, the percentages of institutions that have been charged the minimum and maximum rates have changed over time as institutions' CAMELS component ratings and financial ratios have changed. Based upon June 30, 2008 data, approximately 28 percent of small Risk Category I institutions (other than institutions less than 5 years old) were charged the minimum rate and approximately 19 percent were charged the maximum rate.

The *debt issuer rating method* determines the assessment rate for large institutions that have a long-term debt issuer rating.¹⁴ Long-term debt issuer ratings are converted to numerical values between 1 and 3 and averaged. The weighted average of an institution's CAMELS components and the average converted value of its long-term debt issuer ratings are multiplied by a common multiplier and added to a uniform amount applicable to all institutions subject to the supervisory and debt ratings method to derive the assessment rate under the base rate

schedule. Again, if the rate derived is below the minimum for Risk Category I, the institution will pay the minimum assessment rate for the risk category; if the rate derived is above the maximum for Risk Category I, then the institution will pay the maximum rate for the risk category.

The multipliers and uniform amount were derived in such a way to ensure that, as of June 30, 2006, about 45 percent of Risk Category I large institutions (other than institutions less than 5 years old) would have been charged the minimum rate and approximately 5 percent would have been charged the maximum rate. These percentages have changed little from quarter to quarter thereafter even though industry conditions have changed. Based upon June 30, 2008, data, and ignoring the large bank adjustment (described below), approximately 45 percent of Risk Category I large institutions (other than institutions less than 5 years old) were charged the minimum rate and approximately 11 percent were charged the maximum rate.

Assessment rates for insured branches of foreign banks in Risk Category I are determined using ROCA components.¹⁵

For any Risk Category I large institution or insured branch of a foreign bank, initial assessment rate determinations may be modified up to half a basis point upon review of additional relevant information (the large bank adjustment).¹⁶

With certain exceptions, beginning in 2010, the 2006 assessments rule charges new institutions (those established for less than five years) in Risk Category I, regardless of size, the maximum rate applicable to Risk Category I institutions. Until then, new institutions are treated like all others, except that a well-capitalized institution that has not yet received CAMELS component ratings is assessed at one basis point above the minimum rate applicable to Risk Category I institutions until it receives CAMELS component ratings.

The Need for a Restoration Plan

As part of a separate rulemaking in November 2006, the FDIC also set the

DRR at 1.25 percent, effective January 1, 2007. In November 2007, the Board voted to maintain the DRR at 1.25 percent for 2008.¹⁷ In November 2006, the FDIC projected that the assessment rate schedule established by the 2006 assessments rule would raise the reserve ratio from 1.23 percent at the end of the second quarter of 2006 to 1.25 percent by 2009.¹⁸ At the time, insured institution failures were at historic lows (no insured institution had failed in almost two-and-a-half years prior to the rulemaking, the longest period in the FDIC's history without a failure) and industry returns on assets (ROAs) were near all time highs. The FDIC's projection assumed the continued strength of the industry. By March 2008, the condition of the industry had deteriorated, and FDIC projected higher insurance losses compared to recent years. However, even with this increase in projected failures and losses, the reserve ratio was still estimated to reach the Board's target of 1.25 percent in 2009. Therefore, the Board voted in March 2008 to maintain the existing assessment rate schedule.

Recent failures, as well as deterioration in banking and economic conditions, however, have significantly increased the fund's loss provisions, resulting in a decline in the reserve ratio. As of June 30, 2008, the reserve ratio stood at 1.01 percent, 18 basis points below the reserve ratio as of March 31, 2008. The FDIC expects a higher rate of insured institution failures in the next few years compared to recent years; thus, the reserve ratio may continue to decline. Because the reserve ratio has fallen below 1.15 percent and is expected to remain below 1.15 percent, the FDIC must establish and implement a restoration plan to restore the reserve ratio to 1.15 percent. Absent extraordinary circumstances, the reserve ratio must be restored to 1.15 percent within five years. The FDIC has adopted a restoration plan (the Restoration Plan), the critical component of which is this notice of proposed rulemaking (NPR).¹⁹ To fulfill

¹⁷ 71 FR 69325 (Nov. 30, 2006) and 72 FR 65576 (Nov. 21, 2007).

¹⁸ Beginning in 2007, assessment rates ranged between 5 and 43 cents per \$100 in assessable deposits. When setting the rate schedule, the FDIC projects future changes to the fund balance from losses, operating expenses, assessment and investment revenue, as well as the outlook for insured deposit growth. Since the final rule was issued, the Board has opted to leave rates unchanged.

¹⁹ On October 7, 2008, the FDIC established and implemented the Restoration Plan, which is being published in the *Federal Register* as a companion to this NPR. To determine whether the reserve ratio has returned to the statutory range within five years, the FDIC will rely on the December 31, 2013

¹⁴ The final rule defined a large institution as an institution (other than an insured branch of a foreign bank) that has \$10 billion or more in assets as of December 31, 2006 (although an institution with at least \$5 billion in assets may also 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 reports of condition for four consecutive quarters, the FDIC will reclassify the institution as large beginning the following quarter. If, after December 31, 2006, an institution classified as large reports assets of less than \$10 billion in its reports 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) and 327.9(d)(6).

¹⁵ ROCA stands for Risk Management, Operational Controls, Compliance, and Asset Quality. Like CAMELS components, ROCA component ratings range from 1 (best rating) to a 5 rating (worst rating). Risk Category 1 insured branches of foreign banks generally have a ROCA composite rating of 1 or 2 and component ratings ranging from 1 to 3.

¹⁶ The FDIC has issued additional Guidelines for Large Institutions and Insured Foreign Branches in Risk Category I (the large bank guidelines) governing the large bank adjustment. 72 FR 27122 (May 14, 2007).

the requirements of the Restoration Plan, the FDIC must increase the assessment rates it currently charges. Since the current rates are already 3 basis points uniformly above the base rate schedule established in the 2006 assessments rule, a new rulemaking is required. The FDIC is also proposing other changes to the assessment system, primarily to ensure that riskier institutions will bear a greater share of the proposed increase in assessments.

II. Overview of the Proposal

In this notice of proposed rulemaking, the FDIC proposes to improve the way the assessment system differentiates risk among insured institutions by drawing upon measures of risk that were not included when the FDIC first revised its assessment system pursuant to the Reform Act. The FDIC believes that the proposal will make the assessment system more sensitive to risk. The proposal should also make the risk-based assessment system fairer, by limiting the subsidization of riskier institutions by safer ones. In addition, the FDIC proposes to change assessment rates, including base assessment rates, to raise assessment revenue required under the Restoration Plan.

The FDIC's proposals are set out in detail in ensuing sections, but are briefly summarized here. These changes, except for the proposed rate increase for the first quarter of 2009, which is discussed below, would take effect April 1, 2009.

Risk Category I

The FDIC proposes to introduce a new financial ratio into the financial ratios method. This new ratio would capture brokered deposits (in excess of 10 percent of domestic deposits) that are used to fund rapid asset growth. In addition, the FDIC proposes to update the uniform amount and the pricing multipliers for the weighted average CAMELS rating and financial ratios.

The FDIC proposes that the assessment rate for a large institution with a long-term debt issuer rating be determined using a combination of the institution's weighted average CAMELS component rating, its long-term debt issuer ratings (converted to numbers and averaged) and the financial ratios method assessment rate, each equally weighted. The new method would be known as the large bank method.

Under the proposal, the financial ratios method or the large bank method, whichever is applicable, would determine a Risk Category I institution's initial base assessment rate. The FDIC proposes to broaden the spread between minimum and maximum initial base assessment rates in Risk Category I from the current 2 basis points to an initial range of 4 basis points and to adjust the percentage of institutions subject to these initial minimum and maximum rates.

Adjustments

Under the proposal, an institution's total base assessment rate could vary from the initial base rate as the result of possible adjustments. The FDIC proposes to increase the maximum possible Risk Category I large bank adjustment from one-half basis point to one basis point. Any such adjustment up or down would be made before any other adjustment and would be subject to certain limits, which are described in detail below.

The FDIC proposes to lower an institution's base assessment rate based upon its ratio of long-term unsecured debt and, for small institutions, certain amounts of Tier 1 capital to domestic deposits (the unsecured debt adjustment).²⁰ Any decrease in base assessment rates would be limited to two basis points.

The FDIC proposes to raise an institution's base assessment rate based upon its ratio of secured liabilities to domestic deposits (the secured liability adjustment). An institution's ratio of secured liabilities to domestic deposits (if greater than 15 percent), would increase its assessment rate, but the resulting base assessment rate after any such increase could be no more than 50 percent greater than it was before the adjustment. The secured liability adjustment would be made after any large bank adjustment or unsecured debt adjustment.

An institution in Risk Category II, III or IV would be subject to the unsecured debt adjustment and secured liability adjustment. In addition, the FDIC proposes a final adjustment for brokered deposits (the brokered deposit adjustment) for institutions in these risk categories. An institution's ratio of brokered deposits to domestic deposits (if greater than 10 percent) would increase its assessment rate, but any

increase would be limited to no more than 10 basis points.

Insured Branches of Foreign Banks

The FDIC proposes to make conforming changes to the pricing multipliers and uniform amount for insured branches of foreign banks in Risk Category I. The insured branch of a foreign bank's initial base assessment rate would be subject to any large bank adjustment, but not to the unsecured debt adjustment or secured liability adjustment.

New Institutions

The FDIC also proposes to make conforming changes in the treatment of new insured depository institutions.²¹ For assessment periods beginning on or after January 1, 2010, any new institutions in Risk Category I would be assessed at the maximum initial base assessment rate applicable to Risk Category I institutions, as under the current rule.

Effective for assessment periods beginning before January 1, 2010, until a Risk Category I new institution received CAMELS component ratings, it would have an initial base assessment rate that was two basis points above the minimum initial base assessment rate applicable to Risk Category I institutions, rather than one basis point above the minimum rate, as under the current rule. All other new institutions in Risk Category I would be treated as are established institutions, except as provided in the next paragraph.

Either before or after January 1, 2010: No new institution, regardless of risk category, would be subject to the unsecured debt adjustment; any new institution, regardless of risk category, would be subject to the secured liability adjustment; and a new institution in Risk Categories II, III or IV would be subject to the brokered deposit adjustment. After January 1, 2010, no new institution in Risk Category I would be subject to the large bank adjustment.

Assessment Rates

To implement the proposed changes to risk-based assessments described above and to raise sufficient revenue to ensure that the goals of the Restoration Plan are accomplished within 5 years as required by statute, initial base assessment rates would be as set forth in Table 4 below.

reserve ratio, which is the first date after October 7, 2013 for which the reserve ratio will be known.

²⁰ Long-term unsecured debt includes senior unsecured and subordinated debt.

²¹ Subject to exceptions, a new insured depository institution is a bank or thrift that has not been chartered for at least five years as of the last

day of any quarter for which it is being assessed. 12 CFR 327.8(l)

TABLE 4—PROPOSED INITIAL BASE ASSESSMENT RATES

	Risk category				
	I*		II	III	IV
	Minimum	Maximum			
Annual Rates (in basis points)	10	14	20	30	45

* Initial base rates that were not the minimum or maximum rate would vary between these rates.

After applying all possible adjustments, minimum and maximum total base assessment rates for each risk

category would be as set out in Table 5 below.

TABLE 5—TOTAL BASE ASSESSMENT RATES

	Risk category I	Risk category II	Risk category III	Risk category IV
Initial base assessment rate	10–14	20	30	45
Unsecured debt adjustment	–2–0	–2–0	–2–0	–2–0
Secured liability adjustment	0–7	0–10	0–15	0–22.5
Brokered deposit adjustment .....	.....	0–10	0–10	0–10
Total base assessment rate	8–21.0	18–40.0	28–55.0	43–77.5

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

The FDIC proposes that these rates and other revisions to the assessment rules take effect for the quarter beginning April 1, 2009, and be reflected in the fund balance as of June 30, 2009, and assessments due September 30, 2009. However, at the time of the issuance of the final rule the FDIC may need to set a higher base rate schedule based on information available at that time, including any intervening institution failures and updated failure and loss projections. A higher base rate schedule may also be necessary because

of changes to the proposal in the final rule, if these changes have the overall effect of changing revenue for a given rate schedule.

The proposed rule would continue to allow the FDIC Board to adopt actual rates that were higher or lower than total base assessment rates without the necessity of further notice and comment rulemaking, provided that: (1) The Board could not increase or decrease rates from one quarter to the next by more than three basis points without further notice-and-comment

rulemaking; and (2) cumulative increases and decreases could not be more than three basis points higher or lower than the total base rates without further notice-and-comment rulemaking.

The FDIC also proposes to raise the current rates uniformly by seven basis points for the assessment for the quarter beginning January 1, 2009, which would be reflected in the fund balance as of March 31, 2009, and assessments due June 30, 2009. Rates for the first quarter of 2009 only would be as follows:

TABLE 6—PROPOSED ASSESSMENT RATES FOR THE FIRST QUARTER OF 2009

	Risk category				
	I*		II	III	IV
	Minimum	Maximum			
Annual Rates (in basis points)	12	14	17	35	50

* Rates for institutions that did not pay the minimum or maximum rate would vary between these rates.

The proposed rates for the first quarter of 2009 would raise almost as much assessment revenue as under the rates proposed beginning April 1, 2009. Data and system requirements do not make it feasible to adopt the proposed changes to the risk-based assessment system discussed in previous paragraphs until the second quarter of 2009.

Technical and Other Changes

The FDIC also proposes to make technical changes and one minor non-

technical change to existing assessment rules. These changes, which would be effective April 1, 2009, are detailed below.

III. Risk Category I: Financial Ratios Method

Brokered Deposits and Asset Growth

The FDIC stated in the 2006 assessments rule that it:

[M]ay conclude that additional or alternative financial measures, ratios or other

risk factors should be used to determine risk-based assessments or that a new method of differentiating for risk should be used. In any of these events, changes would be made through notice-and-comment rulemaking.²²

The FDIC has reached such a conclusion and proposes to add a new financial measure to the financial ratios method. This new financial measure, the adjusted brokered deposit ratio, would measure the extent to which

²² 71 FR 69,282, 69,290.

brokered deposits are funding rapid asset growth. The adjusted brokered deposit ratio would affect only those established Risk Category I institutions whose total assets were more than 20 percent greater than they had been four years previously, after adjusting for mergers and acquisitions, and whose brokered deposits made up more than 10 percent of domestic deposits.^{23 24} Generally speaking, the greater an institution's asset growth and the greater its percentage of brokered deposits, the greater would be the increase in its initial base assessment rate.

If an institution's ratio of brokered deposits to domestic deposits were 10 percent or less or if the institution's asset growth over the previous four years were less than 20 percent, the

adjusted brokered deposit ratio would be zero and would have no effect on the institution's assessment rate. If an institution's ratio of brokered deposits to domestic deposits exceeded 10 percent and its asset growth over the previous four years were more than 40 percent, the adjusted brokered deposit ratio would equal the institution's ratio of brokered deposits to domestic deposits less the 10 percent threshold. If an institution's ratio of brokered deposits to domestic deposits exceeded 10 percent but its asset growth over the previous four years were between 20 percent and 40 percent, the adjusted brokered deposit ratio would be equal to a gradually increasing fraction of the ratio of brokered deposits to domestic

deposits (minus the 10 percent threshold), so that small increases in asset growth rates would lead to only small increases in assessment rates. Overall asset growth rates of 20 to 40 percent would be transformed into a fraction between 0 and 1 by multiplying an amount equal to the overall rate of growth minus 20 percent by 5 and expressing the result as a number rather than as a percentage (so that, for example, 5 times 10 percent would equal 0.500).²⁵ The adjusted brokered deposit ratio would never be less than zero. Appendix A contains a detailed mathematical definition of the ratio. Table 7 gives examples of how the adjusted brokered deposit ratio would be determined.

TABLE 7—ADJUSTED BROKERED DEPOSIT RATIO

A	B	C	D	E	F
Example	Ratio of brokered deposits to domestic deposits	Ratio of brokered deposits to domestic deposits minus 10 percent threshold (Column B minus 10 percent)	Cumulative asset growth rate over four years	Asset growth rate factor	Adjusted brokered deposit ratio (Column C times column E)
1	5.0%	0.0%	5.0%	.....	0.0%
2	15.0%	5.0%	5.0%	.....	0.0%
3	5.0%	0.0%	25.0%	0.250	0.0%
4	35.0%	25.0%	30.0%	0.500	12.5%
5	25.0%	15.0%	50.0%	1.000	15.0%

In Examples 1, 2 and 3, either the institution has a ratio of brokered deposits to domestic deposits that is less than 10 percent (Column B) or its four-year asset growth rate is less than 20 percent (Column D). Consequently, the adjusted brokered deposit ratio is zero (Column F). In Example 4, the institution has a ratio of brokered deposits to domestic deposits of 35 percent (Column B), which, after subtracting the 10 percent threshold, leaves 25 percent (Column C). Its assets are 30 percent greater than they were four years previously (Column D), so the fraction applied to obtain the adjusted brokered deposit ratio is 0.5 (Column E) (calculated as $5 \cdot (30 \text{ percent} - 20 \text{ percent})$, with the result expressed as a number rather than as a percentage)). Its adjusted brokered deposit ratio is, therefore, 12.5 percent (Column F) (which is 0.5 times 25 percent). In Example 5, the institution has a lower ratio of brokered deposits to domestic

deposits (25 percent in Column B) than in Example 4 (35 percent). However, its adjusted brokered deposit ratio (15 percent in Column F) is larger than in Example 4 (12.5 percent) because its assets are more than 40 percent greater than they were four years previously (Column D). Therefore, its adjusted brokered deposit ratio is equal to its brokered deposit to domestic deposit ratio of 25 percent minus the 10 percent threshold (Column F).

The FDIC is proposing this new risk measure for a couple of reasons. A number of costly institution failures, including some recent failures, have experienced rapid asset growth before failure and have funded this growth through brokered deposits. Moreover, statistical analysis reveals a significant correlation between rapid asset growth funded by brokered deposits and the probability of an institution's being downgraded from a CAMELS composite 1 or 2 rating to a CAMELS composite 3,

4 or 5 rating within a year. A significant correlation is the standard the FDIC used when it adopted the financial ratios method in the 2006 assessments rule.

The proposed rule would adopt the definition of brokered deposit in Section 29 of the Federal Deposit Insurance Act (12 U.S.C. 1831f), which is the definition used in banks' quarterly Reports of Condition and Income (Call Reports) and thrifts' quarterly Thrift Financial Reports (TFRs). The FDIC is proposing that all brokered deposits be included in an institution's ratio of brokered deposits to domestic deposits used to determine its adjusted brokered deposit ratio, including brokered deposits that consist of balances swept into an insured institution by another institution, such as balances swept from a brokerage account. At present, it would be impossible to exclude these deposits, since institutions do not separately report them in the Call

²³ Generally, an established institution is a bank or thrift that has been chartered for at least five years as of the last day of any quarter for which it is being assessed. 12 CFR 327.8(m).

²⁴ An institution that four years previously had filed no report of condition or had reported no assets would be treated as having no growth unless

it was a participant in a merger or acquisition (either as the acquiring or acquired institution) with an institution that had reported assets four years previously.

²⁵ The ratio of brokered deposits to domestic deposits and four-year asset growth rate would remain unrounded (to the extent of computer

capabilities) when calculating the adjusted brokered deposit ratio. The adjusted brokered deposit ratio itself (expressed as a percentage) would be rounded to three digits after the decimal point prior to being used to calculate the assessment rate.

Report or TFR. Moreover, sweep programs may be structured so that swept balances are not brokered deposits.²⁶ Nevertheless, the FDIC is particularly interested in comments on whether brokered deposits that consist of swept balances should be excluded from the ratio and, if so, how they should be excluded.

The proposed definition of brokered deposits would also include amounts an institution receives through a network that divides large deposits and places them at more than one institution to ensure that the deposit is fully insured, even where the institution accepts these deposits only on a reciprocal basis, such that, for any deposit received, the institution places the same amount (but held by a different depositor) with another institution through the network. At present, it would again be impossible to exclude these deposits, since institutions do not separately report them in the Call Report or TFR. The FDIC is also particularly interested in comments on whether these deposits should be excluded from the ratio and, if so, how they should be excluded.

The proposed definition would exclude amounts not defined as a brokered deposit by statute. Thus, many high cost deposits would be excluded from the definition, potentially including those received through listing services or the Internet. At present, it would be impossible to include these deposits, since institutions do not separately report them in the Call Report or TFR. Nevertheless, the FDIC is particularly interested in comments on whether these deposits should be included in the definition of brokered deposits for purposes of the adjusted brokered deposit ratio and, if so, how they should be included.

Pricing Multipliers and the Uniform Amount

The FDIC also proposes to recalculate the uniform amount and the pricing multipliers for the weighted average

CAMELS component rating and financial ratios. The existing uniform amount and pricing multipliers were derived from a statistical estimate of the probability that an institution will be downgraded to CAMELS 3, 4 or 5 at its next examination using data from the end of the years 1984 to 2004.²⁷ These probabilities were then converted to pricing multipliers for each risk measure. The proposed new pricing multipliers were derived using essentially the same statistical techniques, but based upon data from the end of the years 1988 to 2006.²⁸ The proposed new pricing multipliers are set out in Table 8 below.

TABLE 8—PROPOSED NEW PRICING MULTIPLIERS

Risk measures*	Pricing multipliers**
Tier 1 Leverage Ratio	(0.056)
Loans Past Due 30—89 Days/ Gross Assets	0.576
Nonperforming Assets/Gross Assets	1.073
Net Loan Charge-Offs/Gross Assets	1.213
Net Income before Taxes/ Risk-Weighted Assets	(0.762)
Adjusted Brokered Deposit Ratio	0.055
Weighted Average CAMELS Component Rating	1.088

* Ratios are expressed as percentages.

** Multipliers are rounded to three decimal places.

To determine an institution's initial assessment rate under the base assessment rate schedule, each of these risk measures (that is, each institution's financial measures and weighted average CAMELS component rating) would continue to be multiplied by the corresponding pricing multipliers. The sum of these products would be added to (or subtracted from) a new uniform amount, 9.872.²⁹ The new uniform

amount is also derived from the same statistical analysis.³⁰ As at present, no initial base assessment rate within Risk Category I would be less than the minimum initial base assessment rate applicable to the category or higher than the initial base maximum assessment rate applicable to the category. The proposed rule would set the initial minimum base assessment rate for Risk Category I at 10 basis points and the maximum initial base assessment rate for Risk Category I at 14 basis points.

To compute the values of the uniform amount and pricing multipliers shown above, the FDIC chose cutoff values for the predicted probabilities of downgrade such that, using June 30, 2008 Call Report and TFR data: (1) 25 percent of small institutions in Risk Category I (other than institutions less than 5 years old) would have been charged the minimum initial assessment rate; and (2) 15 percent of small institutions in Risk Category I (other than institutions less than 5 years old) would have been charged the maximum initial assessment rate.³¹ These cutoff values would be used in future periods, which could lead to different percentages of institutions being charged the minimum and maximum rates.

In comparison, under the current system: (1) Approximately 28 percent of small institutions in Risk Category I (other than institutions less than 5 years old) were charged the existing minimum assessment rate; and (2) approximately 19 percent of small institutions in Risk Category I (other than institutions less than 5 years old) were charged the existing maximum assessment rate based on June 30, 2008 data.

Table 9 gives initial base assessment rates for three institutions with varying characteristics, assuming the proposed new pricing multipliers given above, using initial base assessment rates for institutions in Risk Category I of 10 basis points to 14 basis points.³²

³⁰ The uniform amount would be the same for all institutions in Risk Category I (other than large institutions that have long-term debt issuer ratings, insured branches of foreign banks and, beginning in 2010, new institutions).

³¹ The cutoff value for the minimum assessment rate is a predicted probability of downgrade of approximately 2 percent. The cutoff value for the maximum assessment rate is approximately 15 percent.

³² These are the initial base rates for Risk Category I proposed below.

²⁶ For example, a swept deposit may not be a brokered deposit if: (1) Balances are swept for the primary purposes of facilitating customers' purchase and sale of securities, rather than the placement of funds with depository institutions; (2) swept amounts do not exceed 10 percent of the brokerage's cash management account and retirement account assets; and (3) fees are paid on a per customer or account basis, rather than size of account basis, and are for administrative services, rather than for placement of deposits. Are Funds Held in "Cash Management Accounts" Viewed as Brokered Deposits by the FDIC? (FDIC Advisory Opinion 05–02 Feb. 3, 2005).

²⁷ Data on downgrades to CAMELS 3, 4 or 5 is from the years 1985 to 2005. The "S" component rating was first assigned in 1997. Because the statistical analysis relies on data from before 1997, the "S" component rating was excluded from the analysis.

²⁸ For the adjusted brokered deposit ratio, assets at the end of each year are compared to assets at the end of the year four years earlier, so assets at the end of 1988, for example, are compared to assets at the end of 1984.

²⁹ Appendix A provides the derivation of the pricing multipliers and the uniform amount to be added to compute an assessment rate. The rate derived will be an annual rate, but will be determined every quarter.

TABLE 9—INITIAL BASE ASSESSMENT RATES FOR THREE INSTITUTIONS *

	Pricing multiplier	Institution 1		Institution 2		Institution 3	
		Risk measure value	Contribution to assessment rate	Risk measure value	Contribution to assessment rate	Risk measure value	Contribution to assessment rate
A	B	C	D	E	F	G	H
Uniform Amount	9.872	.....	9.872	.....	9.872	.....	9.872
Tier 1 Leverage Ratio (%)	(0.056)	9.590	(0.537)	8.570	(0.480)	7.500	(0.420)
Loans Past Due 30–89 Days/Gross Assets (%)	0.576	0.400	0.230	0.600	0.345	1.000	0.576
Nonperforming Loans/Gross Assets (%)	1.073	0.200	0.215	0.400	0.429	1.500	1.610
Net Loan Charge-Offs/Gross Assets(%)	1.213	0.147	0.178	0.079	0.096	0.300	0.364
Net Income Before Taxes/Risk-Weighted Assets (%)	(0.762)	2.500	(1.905)	1.951	(1.487)	0.518	(0.395)
Adjusted Brokered Deposit Ratio (%)	0.055	0.000	0.000	12.827	0.705	24.355	1.340
Weighted Average CAMELS Component Ratings	1.088	1.200	1.306	1.450	1.578	2.100	2.285
Sum of contributions .....	.....	.....	9.36	.....	11.06	.....	15.23
Initial Base Assessment Rate .....	.....	.....	10.00	.....	11.06	.....	14.00

* Figures may not multiply or add to totals due to rounding.³³

The initial base assessment rate for an institution in the table is calculated by multiplying the pricing multipliers (Column B) by the risk measure values (Column C, E or G) to produce each measure's contribution to the assessment rate. The sum of the products (Column D, F or H) plus the uniform amount (the first item in Column D, F and H) yields the initial base assessment rate. For Institution 1 in the table, this sum actually equals 9.36 basis points, but the table reflects the proposed initial base minimum assessment rate of 10 basis points. For Institution 3 in the table, the sum actually equals 15.23 basis points, but the table reflects the proposed initial base maximum assessment rate of 14 basis points.

Under the proposed rule, the FDIC would continue to have the flexibility to update the pricing multipliers and the uniform amount annually, without further notice-and-comment rulemaking. In particular, the FDIC would be able to add data from each new year to its analysis and could, from time to time, exclude some earlier years from its analysis. Because the analysis would continue to use many earlier years' data as well, pricing multiplier changes from year to year should usually be relatively small.

On the other hand, as a result of the annual review and analysis, the FDIC may conclude, as it has in the proposed rule, that additional or alternative financial measures, ratios or other risk

factors should be used to determine risk-based assessments or that a new method of differentiating for risk should be used. In any of these events, the FDIC would again make changes through notice-and-comment rulemaking.

Financial measures for any given quarter would continue to be calculated from the report of condition filed by each institution as of the last day of the quarter.³⁴ 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 for all institutions in Risk Category I.³⁵

IV. Risk Category I: Large Bank Method

For large Risk Category I institutions now subject to the debt issuer rating method, the FDIC proposes to derive assessment rates from the financial ratios method as well as long-term debt issuer ratings and CAMELS component ratings. The new method would be known as the large bank method. The rate using the financial ratios method would first be converted from the range of initial base rates (10 to 14 basis points) to a scale from 1 to 3 (financial

ratios score).³⁶ The financial ratios score would be given a 33⅓ percent weight in determining the large bank method assessment rate, as would both the weighted average CAMELS component rating and debt-agency ratings.

The weights of the CAMELS components would remain the same as in the current rule. The values assigned to the debt issuer ratings would also remain the same. The weighted CAMELS components and debt issuer ratings would continue to be converted to a scale from 1 to 3, as they are currently.

The initial base assessment rate under the large bank method would be derived as follows: (1) An assessment rate computed using the financial ratios method would be converted to a financial ratios score; (2) the weighted average CAMELS rating, converted long-term debt issuer ratings, and the financial ratios score would each be multiplied by a pricing multiplier and the products summed; and (3) a uniform amount would be added to the result. The resulting initial base assessment rate would be subject to a minimum and a maximum assessment rate. The pricing multiplier for the weighted average CAMELS ratings, converted long-term debt issuer rating and financial ratios score would be 1.764,

³⁴ Reports of condition include Reports of Income and Condition and Thrift Financial Reports.

³⁵ 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 rating 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.

³⁶ The assessment rate computed using the financial ratios method would be converted to a financial ratios score by first subtracting 8 from the financial ratios method assessment rate and then multiplying the result by one-half. For example, if an institution had an initial base assessment rate of 11, 8 would be subtracted from 11 and the result would be multiplied by one-half to produce a financial ratios score of 1.5.

³³ Under the proposed rule, pricing multipliers, the uniform amount, and financial ratios would continue to be rounded to three digits after the decimal point. Resulting assessment rates would be rounded to the nearest one-hundredth (1/100th) of a basis point.

and the uniform amount would be 1.651.³⁷

In recent periods, assessment rates for some large institutions have not responded in a timely manner to rapid changes in these institutions' financial conditions. Based on June 30, 2008 data and ignoring large bank adjustments, under the current system: (1) 45 percent of large institutions in Risk Category I (other than institutions less than 5 years old) would have been charged the existing minimum assessment rate, compared with 28 percent of small institutions; and (2) 11 percent of large institutions in Risk Category I (other than institutions less than 5 years old) would have been charged the existing maximum assessment rate, compared with 19 percent of small institutions. The FDIC's proposed values for pricing multipliers and the uniform amount are such that, using June 30, 2008 data, the percentages of large institutions in Risk Category I (other than new institutions less than 5 years old) that would have been charged the minimum and maximum initial base assessment rates would be the same as the percentages of small institutions that would have been charged these rates (25 percent at the minimum rate and 15 percent at the maximum rate).^{38 39} These cutoff values would be used in future periods, which could lead to different percentages of institutions being charged the minimum and maximum rates.

Large institutions that lack a long-term debt issuer rating are currently assessed using the financial ratios method by itself. This will continue under the proposed rule.

Under the proposed rule, the initial base assessment rate for an institution with a weighted average CAMELS converted value of 1.70, a debt issuer ratings converted value of 1.65 and a financial ratios method assessment rate of 11.50 basis points would be computed as follows:

- The financial ratios method assessment rate less 8 basis points

would be multiplied by one-half (calculated as $(11.5 \text{ basis points} - 8 \text{ basis points}) \cdot 0.5$) to produce a financial ratios score of 1.75.

- The weighted average CAMELS score, debt ratings score and financial ratios score would each be multiplied by 1.764 and summed (calculated as $1.70 \cdot 1.764 + 1.65 \cdot 1.764 + 1.75 \cdot 1.764$) to produce 8.996.

- A uniform amount of 1.651 would be added, resulting in an initial base assessment rate of 10.65 basis points.

The FDIC anticipates that incorporating the financial ratios score into the large bank method assessment rate would result in a more accurate distribution of initial assessment rates and in timelier assessment rate responses to changing risk profiles, while retaining the market and supervisory perspectives that debt and CAMELS ratings provide. A more accurate distribution of initial assessment rates should require fewer large bank adjustments to rates based upon reviews of additional relevant information.⁴⁰

V. Adjustment for Large Institutions and Insured Branches of Foreign Banks in Risk Category I

Under current rules, within Risk Category I, large institutions and insured branches of foreign banks are subject to an assessment rate adjustment (the large bank adjustment). In determining whether to make such an adjustment for a large institution or an insured branch of a foreign bank, the FDIC may consider such information as financial performance and condition information, other market or supervisory information, potential loss severity, and stress considerations. Any large bank adjustment is limited to a change in assessment rate of up to 0.5 basis points higher or lower than the rate determined using the supervisory ratings and financial ratios method, the supervisory and debt ratings method, or the weighted average ROCA component rating method, whichever is applicable. Adjustments are meant to preserve consistency in the orderings of risk 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 to increase the maximum possible large bank adjustment to one basis point and to

make the adjustment to an institution's base assessment rate before any other adjustments are made. The adjustment could not: (1) Decrease any rate so that the resulting rate would be less than the minimum initial base assessment rate; or (2) increase any rate above the maximum initial base assessment rate.

The FDIC makes this proposal for two primary reasons. First, at present, the difference between the minimum and maximum base assessment rates in Risk Category I is two basis points. The maximum one-half basis point large bank adjustment represents 25 percent of the difference between the minimum and maximum rates. While an adjustment of this size is generally sufficient to preserve consistency in the orderings of risk indicated by assessment rates and to ensure fairness, there have been circumstances where more than a half a basis point adjustment would have been warranted. The difference between the minimum and maximum base assessment rates would increase from two basis points under the current system to four basis points under the proposal. A half basis point large bank adjustment would represent only 12.5 percent of the difference between the minimum and maximum rates and would not be sufficient to preserve consistency in the orderings of risk indicated by assessment rates or to ensure fairness. The proposed increase in the maximum possible large bank adjustment would continue to represent 25 percent of the difference between the minimum and maximum rates.

The FDIC expects that, under the proposed rule, large bank adjustments would be made infrequently and for a limited number of institutions.⁴¹ The FDIC's view is that the use of supervisory ratings, financial ratios and agency ratings (when available) would sufficiently reflect the risk profile and rank orderings of risk in large Risk Category I institutions in most (but not all) cases.

The FDIC expects to revise its large bank guidelines. Until then, the guidelines would be applied taking into account the changes resulting from this rulemaking.

³⁷ Appendix 1 provides the derivation of the pricing multipliers and the uniform amount.

³⁸ The cutoff value for the minimum assessment rate is an average score of approximately 1.578. The cutoff value for the maximum assessment rate is approximately 2.334.

³⁹ A "new" institution, as defined in 12 CFR 327.8(l) is generally one that is less than 5 years old, but there are several exceptions, including, for example, certain otherwise new institutions in certain holding company structures. 12 CFR 327.9(d)(7). The calculation of percentages of small institutions, however, was determined strictly by excluding institutions less than 5 years old, rather than by using the definition of a "new" institution and its regulatory exceptions, since determination of whether an institution meets an exception to the definition of "new" requires a case-by-case investigation.

⁴⁰ The FDIC has issued additional Guidelines for Large Institutions and Insured Foreign Branches in Risk Category I (the large bank guidelines) governing these large bank adjustments. 72 FR 27122 (May 14, 2007).

⁴¹ In the six quarters since the 2006 assessment rule went into effect, the total number of adjustments in any one quarter has ranged from 2 to 13. For the second quarter of 2008, the FDIC continued or implemented assessment rate adjustments for 13 large Risk Category I institutions, 12 to increase an institution's assessment rate, and 1 to decrease an institution's assessment rate. Additionally, the FDIC sent four institutions advance notification of a potential upward adjustment in their assessment rate.

VI. Adjustment for Unsecured Debt for all Risk Categories

The FDIC proposes to lower an institution's initial base assessment rate (after making any large bank adjustment) using its ratio of long-term unsecured debt (and, for small institutions, certain amounts of Tier 1 capital) to domestic deposits.⁴² Any decrease in base assessment rates as a result of this unsecured debt adjustment would be limited to two basis points.

For a large institution, the unsecured debt adjustment would be determined by multiplying the institution's long-term unsecured debt as a percentage of domestic deposits by 20 basis points. For example, a large institution with a long-term unsecured debt to domestic deposits ratio of 3.0 percent would see its initial base assessment rate reduced by 0.60 basis points (calculated as 20 basis points \cdot 0.03). An institution with a long-term unsecured debt ratio to domestic deposits of 11.0 percent would have its assessment rate reduced by two basis points, since the maximum possible reduction would be two basis points. (20 basis points \cdot 0.11 = 2.20 basis points, which exceeds the maximum possible reduction.)

For a small institution, the unsecured debt adjustment would factor in a certain amount of Tier 1 capital (qualified Tier 1 capital) in addition to long-term unsecured debt. The amount of qualified Tier 1 capital would be the sum of one-half of the amount between 10 percent and 15 percent of adjusted average assets (between 2 and 3 times the minimum Tier 1 leverage ratio requirement to be a well-capitalized institution) and the full amount of Tier 1 capital exceeding 15 percent of adjusted average assets (above 3 times the minimum Tier 1 leverage ratio requirement) to be a well-capitalized institution).⁴³ The sum of qualified Tier 1 capital and long-term unsecured debt as a percentage of domestic deposits would be multiplied by 20 basis points to produce the unsecured debt adjustment.⁴⁴

For example, consider a small institution with no long-term unsecured debt and a Tier 1 leverage ratio of 17 percent. Assume that each percentage point of the Tier 1 capital ratio equated to a ratio of Tier 1 capital to domestic deposits of 1.1 percent. The unsecured debt adjustment for the portion of capital between 10 percent and 15 percent of adjusted average assets would be 0.55 basis points (calculated as 20 basis points \cdot (1.1 \cdot 0.5 \cdot (0.15—0.10)).⁴⁵ The unsecured debt adjustment for the portion of capital above 15 percent of adjusted gross assets would be 0.44 basis points (calculated as 20 basis points \cdot (1.1 \cdot (0.17—0.15)). The sum of the two portions of the adjustment equals 0.99 basis points.

Ratios for any given quarter would be calculated from the report of condition filed by each institution as of the last day of the quarter.

As noted above, unsecured debt would include senior unsecured and subordinated debt. A senior unsecured liability would be defined as the unsecured portion of other borrowed money.⁴⁶ Subordinated debt would be as defined in the report of condition for the reporting period.⁴⁷ Long-term unsecured debt would be defined as unsecured debt with at least one year

Appendix 2 describes the unsecured debt adjustment for a small institution mathematically.

⁴⁵ Adjusted average assets would be used for Call Report filers; adjusted total assets would be used for TFR filers.

⁴⁶ Other borrowed money is reported on the Call Report in Schedule RC, item 16 and on the Thrift Financial Report as the sum of items SC720, SC740, and SC760.

⁴⁷ The definition of "subordinated debt" in the Call Report is contained in the Glossary under "Subordinated Notes and Debentures." For the June 30, 2008 Call Report, the definition read, in pertinent part, as follows:

Subordinated Notes and Debentures: A subordinated note or debenture is a form of debt issued by a bank or a consolidated subsidiary. When issued by a bank, a subordinated note or debenture is not insured by a federal agency, is subordinated to the claims of depositors, and has an original weighted average maturity of five years or more. Such debt shall be issued by a bank with the approval of, or under the rules and regulations of, the appropriate federal bank supervisory agency * * *

When issued by a subsidiary, a note or debenture may or may not be explicitly subordinated to the deposits of the parent bank * * *

For purposes of the proposed rule, subordinated debt would also include limited-life preferred stock as defined in the report of condition for the reporting period. The definition of "limited-life preferred stock" in the Call Report is contained in the Glossary under "Preferred Stock." For the June 30, 2008 Call Report, the definition read, in pertinent part, as follows:

Limited-life preferred stock is preferred stock that has a stated maturity date or that can be redeemed at the option of the holder. It excludes those issues of preferred stock that automatically convert into perpetual preferred stock or common stock at a stated date.

remaining until maturity. However, institutions separately report neither long-term senior unsecured liabilities nor long-term subordinated debt in the report of condition. In a separate notice of proposed rulemaking, the Federal Financial Institution Examination Council has proposed revising the Call Report to report separately long-term senior unsecured liabilities and subordinated debt that meet this definition. The Office of Thrift Supervision (OTS) has also published a notice of proposed rulemaking that would adopt similar reporting requirements. Until banks separately report these amounts in the Call Report, the FDIC will use subordinated debt included in Tier 2 capital and will not include any amount of senior unsecured liabilities. These adjustments will also be made for TFR filers until thrifts separately report these amounts in the TFR.

When an institution fails, holders of unsecured claims, including subordinated debt, receive distributions from the receivership estate only if all secured claims, administrative claims and deposit claims have been paid in full. Consequently, greater amounts of long-term unsecured claims provide a cushion that can reduce the FDIC's loss in the event of failure.

The FDIC's proposed definition of a long-term senior unsecured liability, however, ignores features that may affect whether the liability would, in fact, reduce the FDIC's loss in the event of failure. The definition would include liabilities with put options or other provisions that would allow the holder to accelerate payment (for example, if capital fell below a certain level). Any kind of put or acceleration feature could undermine the long-term nature of the liability. The FDIC is particularly interested in comment on whether long-term senior unsecured liabilities should exclude those liabilities with put or other acceleration provisions.

The FDIC is proposing that for small institutions (but not large ones) the unsecured debt adjustment include a portion of Tier 1 capital. The FDIC has two primary reasons for this proposal. First, cost concerns and lack of demand generally make it difficult for small institutions to issue unsecured debt in the market. For reasons of fairness, the FDIC believes that small institutions that have large amounts of Tier 1 capital should receive an equivalent benefit for that capital. Second, the FDIC does not want to create an incentive for small institutions to convert existing Tier 1 capital into subordinated debt, for example, by having a shareholder in a closely held corporation redeem shares

⁴² For this purpose, an institution would be "small" if it met the definition of a small institution in 12 CFR 327.8(g)—generally, an institution with less than \$10 billion in assets—except that it would not include an institution that would otherwise meet the definition for which the FDIC had granted a request to be treated as a large institution pursuant to 12 CFR 327.9(d)(6).

⁴³ Adjusted average assets would be used for Call Report filers; adjusted total assets would be used for TFR filers.

⁴⁴ The percentage of qualified Tier 1 capital and long-term unsecured debt to domestic deposits will remain unrounded (to the extent of computer capabilities). The unsecured debt adjustment will be rounded to two digits after the decimal point prior to being applied to the base assessment rate.

and receive subordinated debt. The FDIC is greatly interested in comments on this part of its proposal, including comments on whether the portion of a small institution's Tier 1 capital to be included in the unsecured debt adjustment should include more capital.

The FDIC is also particularly interested in comments on the size of the unsecured debt adjustment and whether it should be larger or smaller. The FDIC believes that the proposed two basis points is sufficient to encourage a significant number of institutions to issue additional subordinated debt or senior unsecured debt, but is interested in the views of commenters.

VII. Adjustment for Secured Liabilities for All Risk Categories

The FDIC proposes to raise an institution's base assessment rates based upon its ratio of secured liabilities to domestic deposits (the secured liability adjustment). An institution's ratio of secured liabilities to domestic deposits (if greater than 15 percent) would increase its assessment rate, but the resulting base assessment rate after any such increase could be no more than 50 percent greater than it was before the adjustment. The secured liability adjustment would be made after any large bank adjustment or unsecured debt adjustment.

Specifically, for an institution that had a ratio of secured liabilities to domestic deposits of greater than 15 percent, the secured liability adjustment would be the institution's base assessment rate (after taking into account previous adjustments) multiplied by the ratio of its secured liabilities to domestic deposits minus 0.15. However, the resulting adjustment could not be more than 50 percent of the institution's base assessment rate (after taking into account previous adjustments). For example, if an institution had a ratio of secured liabilities to domestic deposits of 25 percent, and a base assessment rate before the secured liability adjustment of 12 basis points, the secured liability adjustment would be the base rate multiplied by 0.10 (calculated as 0.25—0.15), resulting in an adjustment of 1.2 basis points. However, if the institution had a ratio of secured liabilities to domestic deposits of 70 percent, its base rate before the secured liability adjustment of 12 basis points would be multiplied by 0.50 rather than 0.55 (calculated as 0.70—0.15), since the resulting adjustment could be only 50 percent of the base assessment rate

before the secured liability adjustment.⁴⁸

Ratios of secured liabilities to domestic deposits for any given quarter would be calculated from the report of condition filed by each institution as of the last day of the quarter. For banks, secured liabilities would include Federal Home Loan Bank advances, securities sold under repurchase agreements, secured Federal funds purchased and "other secured borrowings," as reported in banks' quarterly Call Reports. Thrifts also report Federal Home Loan Bank advances in their quarterly TFR, but, at present, do not separately report securities sold under repurchase agreements, secured Federal funds purchased or "other secured borrowings." The OTS has also published a notice of proposed rulemaking to revise the TFR so that thrifts will separately report these items. Until the TFR is revised, any of these secured amounts not reported separately from unsecured or other liabilities by a thrift in its TFR would be imputed based on simple averages for Call Report filers as of June 30, 2008. As of that date, on average, 63.0 percent of the sum of Federal funds purchased and securities sold under repurchase agreements reported by Call Report filers were secured, and 49.4 percent of other borrowings were secured.

At present, an institution's secured liabilities do not directly affect its assessments. The exclusion of secured liabilities can lead to inequity. An institution with secured liabilities in place of another's deposits pays a smaller deposit insurance assessment, even if both pose the same risk of failure and would cause the same losses to the FDIC in the event of failure.

To illustrate with a simple example, assume that Bank A has \$100 million in insured deposits, while Bank B has \$50 million in insured deposits and \$50 million in secured liabilities. Each poses the same risk of failure and is charged the same assessment rate. At failure, each has assets with a market value of \$80 million. The loss to the DIF would be identical for Bank A and Bank B (\$20 million each). The total assessments paid by Bank A and Bank B, however, would not be identical. Because secured liabilities do not currently figure into an institution's assessment, the DIF would receive twice as much assessment revenue from Bank A as from Bank B

⁴⁸ Under the proposed rule, the ratio of secured deposits to domestic deposits would be rounded to three digits after the decimal point. The resulting amount and adjusted assessment rate would be rounded to the nearest one-hundredth (1/100th) of a basis point.

over a given period (despite identical FDIC losses at failure).

In general, under the current rules, substituting secured liabilities for unsecured liabilities (including subordinated debt) raises the FDIC's loss in the event of failure without providing increased assessment revenue. Substituting secured liabilities for deposits can also lower an institution's franchise value in the event of failure, which increases the FDIC's losses, all else equal.⁴⁹

VIII. Adjustment for Brokered Deposits for Risk Categories II, III and IV

In addition to the unsecured debt adjustment and the secured liability adjustment, the FDIC is proposing that an institution in Risk Category II, III, or IV also be subject to an assessment rate adjustment for brokered deposits (the brokered deposit adjustment). This adjustment would be limited to those institutions whose ratio of brokered deposits to domestic deposits was greater than 10 percent; asset growth rates would not affect the adjustment. The adjustment would be determined by multiplying 25 basis points times the difference between an institution's ratio of brokered deposits to domestic deposits and 0.10.⁵⁰ However, the adjustment would never be more than 10 basis points. The adjustment would be added to the base assessment rate after all other adjustments had been made. Ratios for any given quarter would be calculated from the Call Reports or TFRs filed by each institution as of the last day of the quarter.

A brokered deposit would again be as defined in Section 29 of the Federal Deposit Insurance Act (12 U.S.C. 1831f), which is the definition used in banks' quarterly Call Reports and thrifts quarterly TFRs. However, the FDIC is again particularly interested in comments on whether the definition of a brokered deposit for purposes of the brokered deposit ratio should exclude sweep accounts or deposits received through a network on a reciprocal basis that meet the statutory definition of a brokered deposit or should include high cost deposits, including those received through a listing service and the

⁴⁹ Overall, whether substituting secured liabilities for deposits increases, decreases, or leaves unchanged the FDIC's loss given failure also depends on how the substitution affects the proportion of insured and uninsured deposits, but FDIC's assessment revenue will always decline with a substitution.

⁵⁰ Under the proposed rule, the ratio of brokered deposits to domestic deposits would be rounded to three digits after the decimal point. The resulting brokered deposit charge would be rounded to the nearest one-hundredth (1/100th) of a basis point.

Internet, that do not meet the statutory definition.

Significant reliance on brokered deposits tends to increase an institution's risk profile, particularly as the institution's financial condition weakens. Insured institutions—particularly weaker ones—typically pay higher rates of interest on brokered deposits. When an institution becomes noticeably weaker or its capital declines, the market or statutory restrictions may limit its ability to attract, renew or roll over these deposits, which can create significant liquidity challenges.⁵¹

Also, significant reliance on brokered deposits tends to decrease greatly the franchise value of a failed institution. In a typical failure, the FDIC seeks to find a buyer for a failed institution's branches among the institutions located in or around the service area of the failed institution. A potential buyer usually seeks to increase its market share in the service area of the failed institution through the acquisition of the failed institution and its assets and deposits, but most brokered deposits originate from outside an institution's market area. The more core deposits that the buyer can obtain through the acquisition of the failed institution, the greater the market share of deposits (and the loans and other products that typically follow the core deposits) it can capture. Furthermore, brokered deposits may not be part of many potential buyers' business plans, limiting the field of buyers. Thus, the lower franchise value of the failed institution created by its reliance on brokered deposits leads to a lower price for the failed institution, which increases the FDIC's losses upon failure.

In addition, as noted earlier, several institutions that have recently failed have experienced rapid asset growth before failure and have funded this growth through brokered deposits. The FDIC believes that these reasons warrant the additional charge for significant levels of brokered deposits.

To illustrate the brokered deposit adjustment with a simple example, take a Risk Category II institution with an initial base assessment rate of 20 basis points and a ratio of brokered deposits to domestic deposits of 40 percent. Multiplying 25 basis points times the difference between the institution's ratio of brokered deposits to domestic

deposits and 10 percent yields 7.5 basis points (calculated as 25 basis points \cdot (0.4–0.1)). Because this amount is less than the maximum possible brokered deposit adjustment of 10 basis points, the brokered deposit adjustment would be as calculated, 7.5 basis points. Assuming that the secured liabilities adjustment for this institution is 2 basis points and that the institution has no other assessment rate adjustments, the total base assessment rate would be 29.5 basis points (calculated as (20 basis points + 2 basis points + 7.5 basis points)).

IX. Insured Branches of Foreign Banks

Because the base assessment rates would be higher and the difference between the minimum and maximum initial base assessment rates would increase from two to four basis points under the proposal, the FDIC proposes to make a conforming change for insured branches of foreign banks in Risk Category I. Under the proposal, an insured branch of a foreign bank's weighted average of ROCA component ratings would be multiplied by 5.291 (which would be the pricing multiplier) and 1.651 (which would be a uniform amount for all insured branches of foreign banks) would be added to the product.⁵² The resulting sum would equal a Risk Category I insured branch of a foreign bank's initial base assessment rate, provided that the amount could not be less than the minimum initial base assessment rate nor greater than the maximum initial assessment rate. A Risk Category I insured branch of a foreign bank's initial base assessment rate would be subject to any large bank adjustment. Total base assessment rates could not be less than the minimum initial base assessment rate applicable to Risk Category I institutions nor greater than the maximum initial base assessment rate applicable to Risk Category I institutions. Insured branches of a foreign bank not in Risk Category I are charged the initial base assessment rate

for the risk category in which they are assigned.

No insured branch of a foreign bank in any risk category would be subject to the unsecured debt adjustment, secured liability adjustment or brokered deposit adjustment. Insured branches of foreign banks are branches, not independent depository institutions. In the event of failure, the FDIC would not necessarily have access to the institution's capital or be protected by its subordinated debt or unsecured liabilities. Consequently, an unsecured debt adjustment would appear to be inappropriate. At present, these branches do not report comprehensively on secured liabilities. In the FDIC's view, the burden of increased reporting on secured liabilities would outweigh any benefit.

X. New Institutions

The FDIC also proposes to make conforming changes in the treatment of new insured depository institutions.⁵³ For assessment periods beginning on or after January 1, 2010, any new institutions in Risk Category I would be assessed at the maximum initial base assessment rate applicable to Risk Category I institutions, as under the current rule.

Effective for assessment periods beginning before January 1, 2010, until a Risk Category I new institution received CAMELS component ratings, it would have an initial base assessment rate that was two basis points above the minimum initial base assessment rate applicable to Risk Category I institutions, rather than one basis point above the minimum rate, as under the current rule.⁵⁴ All other new institutions in Risk Category I would be treated as are established institutions, except as provided in the next paragraph.

Either before or after January 1, 2010: no new institution, regardless of risk category, would be subject to the unsecured debt adjustment; any new institution, regardless of risk category, would be subject to the secured liability adjustment; and a new institution in Risk Categories II, III or IV would be subject to the brokered deposit

⁵² An insured branch of a foreign bank's weighted average ROCA component rating would continue to 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 uniform amount for insured branches is identical to the uniform amount under the large bank method. The pricing multiplier for insured branches is three times the amount of the pricing multiplier under the large bank method, since the initial base rate for an insured branch depends only on one factor (weighted average ROCA ratings), while the initial base rate under the large bank method depends on three factors, each equally weighted.

⁵³ Subject to exceptions, a new insured depository institution is a bank or thrift that has not been chartered for at least five years as of the last day of any quarter for which it is being assessed. 12 CFR 327.8(l).

⁵⁴ Certain credit unions that convert to a bank or thrift charter and certain otherwise new insured institutions in a holding company structure may be considered established institutions. Both before and after January 1, 2010, any such institution that is well capitalized but has not yet received CAMELS component ratings will be assessed at two basis points above the minimum initial base assessment rate applicable to Risk Category I institutions.

⁵¹ An adequately capitalized institution can accept, renew and rollover brokered deposits only by obtaining a waiver from the FDIC. Even then, interest rate restrictions apply. An undercapitalized institution may not accept, renew or rollover brokered deposits at all. Section 29 of the Federal Deposit Insurance Act (12 U.S.C. 1831f).

adjustment. After January 1, 2010, no new institution in Risk Category I would be subject to the large bank adjustment.

XI. Assessment Rate Schedule

Recent failures have significantly increased the fund's loss provisions, resulting in a decline in the reserve ratio. As of June 30, 2008, the reserve ratio stood at 1.01 percent, 18 basis points below the reserve ratio as of March 31, 2008. This is the lowest reserve ratio for a combined bank and thrift insurance fund since March 31, 1995. The FDIC expects a higher rate of

insured institution failures in the next few years compared to recent years; thus, the reserve ratio may continue to decline. Because the reserve ratio has fallen below 1.15 percent and is expected to remain below 1.15 percent, the FDIC is required to establish and implement a Restoration Plan to restore the reserve ratio to 1.15 percent within five years, that is, by October 7, 2013.⁵⁵ To fulfill the requirements of the Restoration Plan that the FDIC is adopting simultaneously with the proposed rule, the FDIC must increase

the average assessment rates it currently charges. Since the current rates are already 3 basis points uniformly above the base rate schedule established in the 2006 assessments rule, a new rulemaking is required. The other proposed changes to the assessment system described above also require new rulemaking.

Base Rate Schedule

Effective April 1, 2009, the FDIC proposes to set initial base assessment rates as described in Table 10 below.

TABLE 10—PROPOSED INITIAL BASE ASSESSMENT RATES

	Risk category				
	I *		II	III	IV
	Minimum	Maximum			
Annual Rates (in basis points)	10	14	20	30	45

* Rates for institutions that did not pay the minimum or maximum rate would vary between these rates.

After making all possible adjustments under the proposed rule, total base assessment rates for each risk category would be within the ranges set forth in Table 11 below.

TABLE 11—TOTAL BASE ASSESSMENT RATES AFTER ADJUSTMENTS *

	Risk category I	Risk category II	Risk category III	Risk category IV
Initial base assessment rate	10–14	20	30	45
Unsecured debt adjustment	–2–0	–2–0	–2–0	–2–0
Secured liability adjustment	0–7	0–10	0–15	0–22.5
Brokered deposit adjustment .....	.....	0–10	0–10	0–10
Total base assessment rate	8–21.0	18–40.0	28–55.0	43–77.5

* All amounts for all risk categories are in basis points annually. Rates for institutions that did not pay the minimum or maximum rate would vary between these rates. Adjustments would be applied in the order listed in the table. The large bank adjustment would be made before any other adjustment.

The proposed base rates are intended to improve the way the assessment system differentiates risk among insured institutions and make the risk-based assessment system fairer, by limiting the subsidization of riskier institutions by safer ones. They are also intended to increase assessment revenue while the Restoration Plan is in effect in order to raise the reserve ratio to the minimum threshold of 1.15 percent within 5 years of the Plan's implementation. As explained in the next Section, given the FDIC's projections (described below), the proposed rate schedule would raise the reserve ratio to 1.26 percent by the end of 2013.

Actual Rate Schedule, Ability To Adjust Rates and Effective Date

Based on the information currently available, the FDIC proposes setting actual rates at the proposed total base assessment rate schedule effective April 1, 2009. The FDIC projects that this schedule would raise the overall average assessment rate to 13.5 basis points beginning in April 2009 and 12.6 basis points in 2010 and thereafter, from a 6.3 basis point average assessment rate (before accounting for credit use) as of June 30, 2008. For institutions in Risk Category I, the projected average rate would be 11.6 basis points beginning in April 2009 and 11.9 basis points in 2010

and thereafter, up from 5.5 basis points as of June 30, 2008.⁵⁶

However, at the time of the issuance of the final rule, the FDIC may need to set a higher base rate schedule based on information available at that time, including any intervening institution failures and updated failure and loss projections. A higher base rate schedule may also be necessary because of changes to the proposal in the final rule, if these changes have the overall effect of changing revenue for a given rate schedule. In order to fulfill the statutory requirement to return the fund reserve ratio to 1.15 percent, the base rate schedule in the final rule could be substantially higher than the proposed

⁵⁵ Data on estimated insured deposits and the reserve ratio are available only for each quarter-end; therefore, the reserve ratio for the end of the fourth quarter of 2013 will be the first reserve ratio

available after October 7 to measure compliance with the Restoration Plan's requirements. Deposit data needed to compute the reserve ratio will be available in February of the following year.

⁵⁶ Changes in the projected average rates under the proposed schedule over time reflect projected changes in the migration of institutions within and across risk categories.

base assessment rate schedule (for example, if projected or actual losses at the time of the final rule greatly exceed the FDIC's current estimates). The base rate schedule in the final rule could possibly be lower than the proposed base rate schedule. The FDIC seeks particular comment on possible alternative base rate schedules.

The rate schedule and the other revisions to the assessment rules would take effect for the quarter beginning April 1, 2009, which would be reflected in the June 30, 2009 fund balance and the invoices for assessments due September 30, 2009.

The proposed rule would continue to allow the FDIC Board to adopt actual rates that were higher or lower than total base assessment rates without the necessity of further notice-and-comment rulemaking, provided that: (1) The Board could not increase or decrease rates from one quarter to the next by more than three basis points; and (2) cumulative increases and decreases could not be more than three basis points higher or lower than the adjusted base rates. Continued retention of this flexibility would enable the Board to act in a timely manner to fulfill its mandate

to raise the reserve ratio to at least 1.15 percent within the 5-year timeframe.

Assessment Rates for the First Quarter of 2009

The FDIC also proposes to raise the current rates uniformly by seven basis points for the assessment for the quarter beginning January 1, 2009, which would be reflected in the fund balance as of March 31, 2009, and assessments due June 30, 2009. Rates for the first quarter of 2009 only would be as set forth in Table 12:

TABLE 12—PROPOSED ASSESSMENT RATES FOR THE FIRST QUARTER OF 2009

	Risk category				
	I *		II	III	IV
	Minimum	Maximum			
Annual Rates (in basis points)	12	14	17	35	50

* Rates for institutions that did not pay the minimum or maximum rate would vary between these rates.

The proposed rates for the first quarter of 2009 would raise almost as much assessment revenue as under the rates proposed beginning April 1, 2009. Data and system requirements do not make it feasible to adopt the proposed changes to the risk-based assessment

system discussed above until the second quarter of 2009.

XII. Assessment Revenue Needs Under the Restoration Plan

Summary

Table 13 shows projected minimum initial base assessment rates needed to

raise the reserve ratio to 1.15 percent (the lower bound under the requirements for the Restoration Plan) in 2013 for alternative average annual insured deposit growth rates and total costs of bank failures from 2008 through 2013.

TABLE 13—MINIMUM INITIAL BASE ASSESSMENT RATES (IN BASIS POINTS) NEEDED TO RAISE THE RESERVE RATIO TO 1.15 PERCENT IN 2013

Insured deposit growth rate	If institution failures from 2008 to 2013 cost in total: *					
	\$20 Billion	\$30 Billion	\$40 Billion	\$50 Billion	\$60 Billion	\$70 Billion
3%	5	5	8	11	13	16
4%	5	6	9	11	14	16
5%	5	7	9	11	14	16
6%	5	7	9	12	14	17
7%	5	8	10	12	15	17

* Costs include \$12.8 billion for actual and projected failures in 2008.

Under the FDIC's proposed rate schedule, the average rate is projected to be 13.5 basis points in 2009 (once the rates become effective in April) and 12.6 basis points in 2010 and beyond. For institutions in Risk Category I, the average rate is projected to be 11.6 basis points beginning in April 2009, rising to 11.9 basis points in 2010 and beyond. Given the FDIC's projections, the proposed rates would increase the reserve ratio to 1.26 percent by year-end 2013.

Current and emerging economic difficulties, particularly in the housing and construction sector, financial markets and commercial real estate,

contribute to the FDIC's expectation of higher losses for the insurance fund. The insurance fund balance and reserve ratio are likely to experience further declines before recovering as the current problems confronting the banking industry abate. The FDIC projects that the reserve ratio will continue to fall for the remainder of this year and early 2009 to a low of 0.65 to 0.70 percent, as the fund's loss reserves for anticipated failures increase. Higher assessment revenue should begin to increase the reserve ratio gradually in the latter part of 2009. As described in more detail below, the FDIC's best estimate is that institution failures could cost the

insurance fund approximately \$40 billion from 2008 to 2013, of which approximately \$13 billion represent actual and projected costs incurred this year (including almost \$9 billion for the failure in July of one institution with over \$30 billion in assets). The FDIC bases its loss projections on: Analysis of specific troubled institutions and risk factors that may adversely affect other institutions; analysis of recent and expected loss rates given failure; stress analyses of the effects of housing price declines and an economic slowdown in specific geographic areas on loan losses and bank capital; and recent and

historic supervisory rating downgrade and failure rates.

The FDIC also assumes that insured deposits would increase on average 5 percent per year from 2008 to 2013. This assumption is in line with the most recent 12-month growth rate and average annual growth rates over the past 5 and 10 years.

Table 13 shows that an initial minimum rate of 9 basis points is necessary for the reserve ratio to reach 1.15 percent by 2013 assuming that failures between 2008 and 2013 cost \$40 billion and that insured deposits increase on average by 5 percent annually. With an initial minimum rate of 9 basis points, the FDIC projects that the reserve ratio would equal 1.18 percent by the end of 2013.⁵⁷ The FDIC's proposed rates, with an initial minimum rate of 10 basis points, would raise the reserve ratio to 1.26 percent by 2013. The FDIC believes that it would be prudent to provide this margin for error in the event that losses exceed the FDIC's best estimate or insured deposit growth is more rapid than expected.

The FDIC had previously expected that the reserve ratio would reach the 1.25 percent DRR by 2009, consistent with the Board's objectives for the insurance fund. The recent decline in the reserve ratio and projected higher rate of bank failures over the next few years make the possibility of reaching the DRR next year remote absent very high assessment rates, which the FDIC believes would be inappropriate under current conditions. Nonetheless, the goal of reaching the 1.25 percent DRR remains in effect. Under the proposed rates, the reserve ratio is projected to reach 1.26 percent by the end of 2013.

The FDIC recognizes that there is considerable uncertainty about its projections for losses and insured deposit growth, and that changes in assumptions about these and other factors could lead to different assessment revenue needs and rates. Under the terms of the Restoration Plan, the FDIC must update its projections for the insurance fund balance and reserve ratio at least semiannually while the Restoration Plan is in effect and adjust rates as necessary. In the event that losses exceed the FDIC's best estimate or insured deposit growth is more rapid than expected, the Board will be able to adjust assessment rates.

⁵⁷ If the minimum initial rate was 8 basis points or less, the reserve ratio is projected to fall short of the 1.15 percent threshold.

Factors Considered in Setting the Level of Assessment Rates

In setting assessment rates, the FDIC's Board of Directors has considered the following factors required by statute:

(i) The estimated operating expenses of the Deposit Insurance Fund.

(ii) The estimated case resolution expenses and income of the Deposit Insurance Fund.

(iii) The projected effects of the payment of assessments on the capital and earnings of insured depository institutions.

(iv) The risk factors and other factors taken into account pursuant to section 7(b)(1) of the Federal Deposit Insurance Act (12 U.S.C. Section 1817(b)(1)) under the risk-based assessment system, including the requirement under section 7(b)(1)(A) of the Federal Deposit Insurance Act (12 U.S.C. 1817(b)(1)(A)) to maintain a risk-based system.

(v) Other factors the Board of Directors has determined to be appropriate.⁵⁸

The factors considered in setting assessment rates are discussed in more detail below.

Case Resolution Expenses (Insurance Fund Losses)

Insurance fund losses from recent insured institution failures and an expected higher rate of failures over the next few years will tend to reduce the fund balance and reserve ratio.

The FDIC expects that housing price declines, financial market turmoil, and generally weaker economic conditions will continue to exert stress on banking industry earnings and credit quality in the near term, most notably in residential real estate and construction and development lending. Significant uncertainty remains about the outlook for a recovery in mortgage securitization markets and the return of confidence to financial markets overall. Economic activity in the industrial Midwest has especially suffered from higher energy

and commodity prices. Housing market downturns in Arizona, California, Nevada, Florida, and other coastal areas are contributing to declines in construction and consumer spending and economic downturns in those areas. Regional disparities in housing market and economic conditions, as well as financial market difficulties, have led in turn to variation in prospects among banks. Institutions most at risk include: (1) Those with large volumes of subprime and nontraditional mortgages, particularly those heavily reliant on securitization; and (2) those with heavy concentrations of residential real estate and construction and development loans in markets with the greatest housing price declines. Within each of these groups, those heavily reliant on non-core funding incur additional risks should the availability of these funds decline as conditions deteriorate.

In developing its projections of losses to the insurance fund, the FDIC drew from several sources. First, the FDIC relied heavily on supervisory analysis of troubled institutions. Supervisors also identified risk factors present in currently troubled institutions (or that were present in institutions that recently failed) to help analyze the potential for other institutions with those risk factors to cause losses to the insurance fund. Second, the FDIC drew on its analysis of losses to the fund in the event of failure. Current financial market and economic difficulties make simple reliance on the historical average or model estimates based on historical data inappropriate for projecting loss rates given failure, particularly in the near term.

The FDIC also relied on stress analysis designed to evaluate the effect of a large and widespread decline in housing prices and related deterioration in overall economic conditions on the capital positions and earnings of insured institutions. The stress test simulated the effects of high and rising loan loss rates directly resulting from falling housing prices and rising unemployment rates in various geographic areas to identify institutions most vulnerable to these types of stress. Under the stress test, institutions operating in those areas with the worst housing and economic conditions experience the largest increase in loss rates.

The FDIC categorized well-capitalized institutions into various groups based on stress test results and supervisory analysis. Based on recent and historical downgrade and failure experience, the FDIC then applied downgrade and failure assumptions for each group to

⁵⁸ Section 2104 of the Reform Act (amending section 7(b)(2) of the Federal Deposit Insurance Act, 12 U.S.C. 1817(b)(2)(B)). The risk factors referred to in factor (iv) include:

(i) The probability that the Deposit Insurance Fund will incur a loss with respect to the institution, taking into consideration the risks attributable to—

(I) Different categories and concentrations of assets;

(II) different categories and concentrations of liabilities, both insured and uninsured, contingent and noncontingent; and

(III) any other factors the Corporation determines are relevant to assessing such probability;

(ii) the likely amount of any such loss; and

(iii) the revenue needs of the Deposit Insurance Fund.

Section 7(b)(1)(C) of the Federal Deposit Insurance Act (12 U.S.C. 1817(b)(1)(C)).

project the cost of failure to the fund over the next few years.⁵⁹

Based on the various sources of information described above, the FDIC projects that the costs of institution failures from 2008 through 2013 may be approximately \$40 billion. This figure includes almost \$13 billion for the costs of actual and projected failures in 2008. The FDIC recognizes the considerable degree of uncertainty surrounding these projections and its analyses reveal that either higher or lower losses are plausible. This uncertainty underscores the need to update the outlook for insurance fund losses on a regular basis—at least semiannually—while the Restoration Plan is in effect and to consider adjustments to assessment rates.

Operating Expenses and Investment Income

The FDIC estimates that its operating expenses in 2008 will be \$1 billion. Thereafter, the FDIC projects that operating expenses will increase on average by 5 percent annually.

The FDIC projects that its investment contributions (investment income plus or minus unrealized gains or losses on available-for-sale securities) this year will total \$3.7 billion, or 7 percent of the start-of-year fund balance. A one-time unrealized gain of \$1.6 billion from reclassifying the fund's held-to-maturity securities as available for sale as of June 30, 2008 bolsters this figure. Projected increases in interest rates, which will

reduce the value of these securities, will partly offset this gain next year.⁶⁰ In addition, the FDIC expects that it will invest new funds in short-term securities (primarily overnight investments) to accommodate increased bank failure activity. The FDIC generally expects that these investments will earn lower rates than the longer-term securities that they are replacing and will therefore result in less interest income to the fund. Accounting for all of these factors, the FDIC projects investments to contribute an amount equal to 2.0 percent of the starting fund balance in 2009, rising gradually to 3.5 percent by 2011 and thereafter.

Assessment Revenue, Credit Use, and the Distribution of Assessments

The FDIC expects that assessment revenue in 2008 will total \$3.0 billion: \$4.4 billion in gross assessments charged less \$1.4 billion in credits used. By the end of 2008, the projections indicate that only 4 percent of the original \$4.7 billion in credits awarded will be remaining. As part of the Restoration Plan, the FDIC has the authority to restrict credit use while the plan is in effect, providing that institutions may still apply credits against their assessments equal to the lesser of their assessment or 3 basis points.⁶¹ The FDIC has decided not to restrict credit use in the Restoration Plan. The FDIC projects that the amount of credits remaining at the time that the proposed new rates go into effect will be

very small and that their continued use will have very little effect on the assessment rates necessary to meet the requirements of the plan.⁶²

Accounting for the use of remaining credits, proposed uniform increase to current rates for the first quarter of 2009 and the proposed assessment rates effective April 1, 2009, and assuming 5 percent annual growth in the assessment base (which is approximately domestic deposits), the FDIC projects that the fund will earn assessment revenue of \$10.3 billion for all of 2009.

For the quarter beginning April 1, 2009, the FDIC has derived gross assessment revenue (i.e., before applying any remaining credits) by assigning each insured institution to an assessment rate based on the proposed rate schedule and factors described above. Table 14 shows the distribution of institutions and domestic deposits by risk category (divided into four parts for Risk Category I) under the proposed initial base rate schedule (effective April 1, 2009) based on data as of June 30, 2008; Table 15 shows the distribution of institutions and domestic deposits by bands of proposed total base assessment rates.⁶³ For purposes of assessment revenue projections beginning next April, the FDIC relied on the proposed assessment rates based on data as of June 30, 2008, but also accounted for projected migration of institutions across risk categories as supervisory ratings change.

TABLE 14—DISTRIBUTION OF INITIAL BASE ASSESSMENT RATES AND DOMESTIC DEPOSITS*

[Data as of June 30, 2008]

Risk category	Initial assessment rate	Number of institutions	Percent of institutions	Domestic deposits (in billions of \$)	Percent of domestic deposits
I	10	1,775	21	823.0	12
	10.01–12.00	2,976	35	2,945.7	42
	12.01–13.99	1,758	21	1,714.4	24
	14	1,219	14	593.3	8
II	20	588	7	896.5	13
III	30	121	1	27.1	0
IV	45	14	0	29.1	0

* This table and the following two tables exclude insured branches of foreign banks.

⁵⁹ For those institutions that were well rated one year ago but performed poorly under the stress simulations when applied to their balance sheets from last year, the FDIC identified the extent to which these institutions received supervisory ratings downgrades over the following year. To look beyond what may happen over one year, the FDIC supplemented this information with data from the late 1980s and early 1990s (a period of many bank failures) on ratings downgrades over a five-year horizon for institutions with financial characteristics similar to those performing poorly under the stress analysis. With this information, the

FDIC developed projections of the volume of well-rated institutions likely to be downgraded over the next few years. The FDIC then considered data on failure rates from the late 1980s and early 1990s to project failure rates for those institutions that may be downgraded over the next few years, as well as those that are currently not well rated.

⁶⁰ Future interest rate assumptions are based on consideration of recent Blue Chip Financial Forecasts as well as recent forward rate curves. Forward rates are expected yields on securities of varying maturities for specific future points in time

that are derived from the term structure of interest rates. (The term structure of interest rates refers to the relationship between current yields on comparable securities with different maturities.)

⁶¹ Section 7(b)(3)(E)(iv) of the Federal Deposit Insurance Act (12 U.S.C. 1817(b)(3)(E)(iv)).

⁶² For 2008, 2009 and 2010, credits may not offset more than 90 percent of an institution's assessment. Section 7(e)(3)(D)(ii) of the Federal Deposit Insurance Act (12 U.S.C. 1817(e)(3)(D)(ii)).

⁶³ The assessment base is almost equal to total domestic deposits.

TABLE 15—DISTRIBUTION OF TOTAL BASE ASSESSMENT RATES AND DOMESTIC DEPOSITS *
[Data as of June 30, 2008]

Risk category	Total base assessment rate	Number of institutions	Percent of institutions	Domestic deposits (in billions of \$)	Percent of domestic deposits
I	8.00–10.00	1,834	22	806.6	11
	10.01–12.00	2,674	32	3,047.6	43
	12.01–14.00	2,588	31	1,632.5	23
	14.01–21.00	632	7	589.7	8
II	18.00–20.00	346	4	204.7	3
	20.01–40.00	242	3	691.8	10
III	28.00–30.00	72	1	8.0	0
	30.01–55.00	49	1	19.1	0
IV	43.00–45.00	9	0	5.8	0
	45.01–77.5	5	0	23.3	0

* Because of data limitations, secured liability adjustments for TFR filers are calculated using imputed values based on simple averages of Call Report filers as of June 30, 2008 (discussed below). Unsecured debt adjustments are calculated using “Qualifying subordinated debt and redeemable preferred stock” included in Tier 2 capital.

As noted earlier, the proposed changes to risk-based assessments are intended to better capture differences in risk and impose a greater share of the necessary increase in overall assessments on riskier institutions. Table 16 shows how institutions would have fared if the FDIC had proposed

leaving the current risk-based assessment system unchanged except for a uniform increase in rates that would have produced the same revenue as under the proposed schedule. To produce the same revenue, the FDIC would have had to increase the current rates uniformly by 7.6 basis points,

based upon data as of June 30, 2008. As the table shows, 85 percent of institutions, with 74 percent of domestic deposits, would pay a lower rate under the proposed assessment rate schedule than under a uniform increase of 7.6 basis points to the current rate schedule.

TABLE 16—DIFFERENCE BETWEEN PROPOSED ASSESSMENT RATES AND A UNIFORM INCREASE IN CURRENT RATES TO RAISE THE SAME REVENUE
[Data as of June 30, 2008]

Compared to a uniform increase in current rates, proposed rates are:	Number of institutions	Percent of institutions	Domestic deposits (in billions of \$)	Percentage of total domestic deposits
Over 4 bp lower	339	4	64	1
2–4 bp lower	3,070	36	1,551	22
0–2 bp lower	3,819	45	3,551	51
0–2 bp higher	463	5	785	11
2–4 bp higher	541	6	321	5
4–6 bp higher	110	1	121	2
6–8 bp higher	49	1	244	3
8–10 bp higher	18	0	245	3
Over 10 bp higher	42	0	146	2

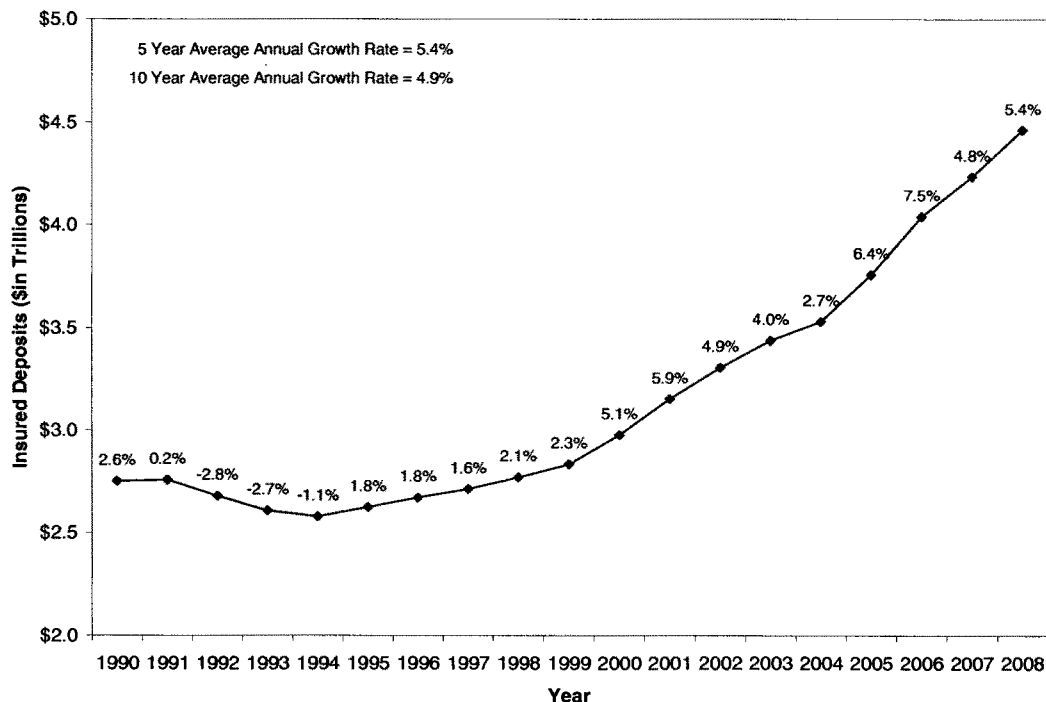
Estimated Insured Deposits

The FDIC believes that it is reasonable to plan for annual insured deposit

growth of 5 percent. Over the 12 months ending June 30, 2008, estimated insured deposits increased by 5.4 percent. The most recent five and ten year average

growth rates are also approximately 5 percent. Chart 1 depicts insured deposit growth since 1990.

Chart 1
Annual Insured Deposit Growth Rates
(June to June)



Projections of insured deposits are subject to considerable uncertainty. Insured deposit growth over the near term could rise more rapidly due to a “flight to quality” attributable to financial and economic uncertainties. On the other hand, as the experience of the late 1980s and early 1990s demonstrated, lower overall growth in the banking industry and the economy could depress rates of growth of total domestic and insured deposits. As Table 13 shows, a one percentage point increase or decrease in average annual insured deposit growth rates will not have a significant effect on the assessment rates necessary to meet the requirements of the Restoration Plan, other factors equal.

Effect on Capital and Earnings

Appendix 3 contains an analysis of the effect of proposed rates on the capital and earnings of insured institutions. Given the assumptions in the analysis, for the industry as a whole, projected total assessments in 2009 would result in capital that would be 0.3 percent lower than if the FDIC did not charge assessments and 0.1 percent lower than if current assessment rates remained in effect. The proposed assessments would cause 6 institutions

whose equity-to-assets ratio would have exceeded 4 percent in the absence of assessments to fall below that percentage and 5 institutions to fall below 2 percent. The proposed increase in assessments would cause 3 institutions whose equity-to-assets ratio would have exceeded 4 percent under current assessments to fall below that threshold and 1 institution to fall below 2 percent.

For the industry as a whole, assessments in 2009 would result in pre-tax income that would be 11 percent lower than if the FDIC did not charge assessments and 5.6 percent lower than if current assessment rates remained in effect. Appendix 3 also provides an analysis of the range of effects on capital and earnings.

Other Factors That the Board May Consider

In its consideration of proposed rates, the FDIC Board has considered other factors that it deems appropriate, as permitted by law.

Flexibility to accommodate economic and industry conditions. The Reform Act generally provides up to 5 years for the FDIC to raise the fund’s reserve ratio to at least 1.15 percent under the Restoration Plan. The FDIC Board had

previously set rates with an objective of raising the reserve ratio to the 1.25 percent DRR by next year. The recent decline in the reserve ratio and an anticipated higher rate of bank failures over the next few years make the possibility of reaching the 1.25 percent DRR—or even 1.15 percent—next year remote absent very high assessment rates. The FDIC believes that such high rates would be inappropriate under current and projected economic and financial conditions. The FDIC’s proposed rates take advantage of the flexibility to raise rates more gradually.

Reaching the DRR. The FDIC had previously expected that the reserve ratio would reach the 1.25 percent DRR by 2009, consistent with the Board’s objectives for the insurance fund. The recent decline in the reserve ratio and an anticipated increase in bank failures make the possibility of reaching the DRR next year remote absent very high assessment rates, which the FDIC believes would be inappropriate under current conditions. Nonetheless, the goal of reaching the 1.25 percent DRR remains in effect. Under the proposed rates, the reserve ratio is projected to reach 1.26 by the end of 2013.

Updating projections regularly. The FDIC recognizes that there is

considerable uncertainty about its projections for losses and insured deposit growth, and that changes in assumptions about these and other factors could lead to different assessment revenue needs and rates. The FDIC projects that, under its proposed rates, the reserve ratio will increase to 1.26 percent by year-end 2013, providing a margin for error in the event that losses exceed the FDIC's best estimate or insured deposit growth is more rapid than expected. Nonetheless, the FDIC expects to update its projections for the insurance fund balance and reserve ratio at least semiannually while the Restoration Plan is in effect and adjust rates as necessary.

XIII. Technical and Other Changes

The FDIC is proposing to change the way assessment rates are determined for a large institution that is subject to the large bank method (or an insured branch of a foreign bank) when it moves from Risk Category I to Risk Category II, III or IV during a quarter.

At present, if, during a quarter, a CAMELS (or ROCA) rating change occurs that results in a large institution that is subject to the supervisory and debt ratings method or an insured branch of a foreign bank moving from Risk Category I to Risk Category II, III or IV, the institution's assessment rate for the portion of the quarter that it was in Risk Category I is based upon its assessment rate for the prior quarter. No new Risk Category I assessment rate is developed for the quarter in which the institution moves to Risk Category II, III or IV.⁶⁴

The opposite holds true for a small institution or a large institution subject to the financial ratios method when it moves from Risk Category I to Risk Category II, III or IV during a quarter. A new Risk Category I assessment rate is developed for the quarter in which the institution moves to Risk Category II, III or IV.⁶⁵

The FDIC proposes that when a large institution subject to the large bank method or an insured branch of a foreign bank moves from Risk Category I to Risk Category II, III or IV during a quarter, a new Risk Category I

assessment rate be developed for that quarter. That rate for the portion of the quarter that the institution was in Risk Category I would be determined as for any other institution in Risk Category I subject to the same pricing method, except that the rate would only apply for the portion of the quarter that the institution was actually in Risk Category I.

Since implementation of the 2006 assessments rule in 2007, several large institutions that were subject to the supervisory and debt ratings method have moved from Risk Category I to a Risk Category II or III. More than once, changes occurred in these institutions' debt ratings or CAMELS component ratings while the institution was in Risk Category I, but the institutions' assessment rates for the quarter did not reflect these changes. In one case, an institution received a debt rating downgrade early in the quarter, but, because it fell to Risk Category II on the 89th day of the quarter, this debt rating downgrade did not affect its assessment rate. The FDIC's proposal is intended to correct these outcomes and better ensure that an institution's assessment rate reflects the risk that it poses.

The FDIC is also proposing to amend its assessment regulations to correct technical errors and make clarifications to the regulatory language in several sections of Part 327 for the reasons set forth below.

A technical correction is proposed to the language of 12 CFR 327.3(a), the regulatory requirement that each depository institution pay an assessment to the Corporation. Language creating an exception "as provided in paragraph (b) of this section" was inadvertently retained in the initial clause of section 327.3(a) when the assessment regulations were amended in 2006. Formerly, paragraph (b) excepted newly insured institutions from payment of assessments for the semiannual period in which they became insured institutions; that exception was eliminated in 2006. Paragraph (b) now addresses quarterly certified statement invoices and payment dates. Accordingly, the FDIC proposes to amend section 327.3(a) to eliminate the reference to paragraph (b).

12 CFR 327.6(b)(1) addresses assessments for the quarter in which a terminating transfer occurs when the acquiring institution uses average daily balances to calculate its assessment base. In that situation, section 327.6(b)(1) provides that the terminating institution's assessment for that quarter is reduced by the percentage of the quarter remaining after the terminating transfer occurred, and calculated at the

acquiring institution's assessment rate. Although it can be inferred that the terminating institution's assessment base for that quarter is to be used in the reduction calculation, the section is not explicit. Accordingly, the FDIC proposes to amend the section to clarify that the reduction calculation is accomplished by applying the acquirer's rate to the terminating institution's assessment base for that quarter.

12 CFR 327.8(i) defines *Long Term Debt Issuer Rating* as the "current rating" of an insured institution's long-term debt obligations by one of the named ratings companies. "Current rating" is defined in § 327.8(i) as "one that has been confirmed or assigned within 12 months before the end of the quarter for which the assessment rate is being determined." The section also provides: "If no current rating is available, the institution will be deemed to have no long-term debt issuer rating." The language of § 327.8(i) requires the FDIC to disregard a long-term debt issuer rating that is still in effect—that is, it has not been withdrawn and replaced by another rating—if it is greater than 12 months old when the FDIC calculates an institution's assessment rate. To remedy this, the FDIC proposes to amend § 327.8(i) to read as follows:

(i) *Long-Term Debt Issuer Rating*. A long-term debt issuer rating shall mean a rating of an insured depository institution's long-term debt obligations by Moody's Investor Services, Standard & Poor's, or Fitch Ratings that has not been withdrawn before the end of the quarter being assessed. A withdrawn rating shall mean one that has been withdrawn by the rating agency and not replaced with another rating by the same agency. A long-term debt issuer rating does not include a rating of a company that controls an insured depository institution, or an affiliate or subsidiary of the institution.

Consistent with this amendment, the FDIC proposes to amend two references to long-term debt issuer rating, as defined in § 327.8(i), "*in effect at the end of the quarter being assessed*" that appear in 12 CFR 327.9(d) and 12 CFR 327.9(d)(2). The proposal is to amend these sections by deleting the phrase "*in effect at the end of the quarter being assessed*" and to add "*as defined in § 327.8(i)*" to section 327.9(d)(2) so that its construction parallels section 327.9(d).

12 CFR 327.8(l) and (m) define "*New depository institution*" and "*Established depository institution*." The former is "a bank or thrift that has not been chartered for at least five years as of the last day of any quarter for which it is being assessed"; the latter is "a bank or thrift that has been chartered for at least

⁶⁴ 12 CFR 327.9(d)(5).

⁶⁵ 12 CFR 327.9(d)(1)(ii). In fact, the FDIC had provided in the preamble to the 2006 assessments rule that no new Risk Category I assessment rate would be determined for any large institution for the quarter in which it moved to Risk Category II, III or IV, but, as the result of a drafting inconsistency, this intention was not realized in the regulatory text. 71 FR 69,282, 69,293 (Nov. 30, 2006). The FDIC now believes that a new Risk Category I assessment rate should be determined for any large institution for the quarter in which it moves to Risk Category II, III or IV.

five years as of the last day of any quarter for which it is being assigned.” In the FDIC’s view, this regulatory language allows a previously uninsured institution to be treated as an established institution based on charter date. To remedy this, the FDIC proposes to amend sections 327.8(l) and (m) to read as follows:

(l) *New depository institution.* A new insured depository institution is a bank or thrift that has been federally insured for less than five years as of the last day of any quarter for which it is being assessed.

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

12 CFR 327.9(d)(7)(viii), which addresses rates applicable to institutions subject to the subsidiary or credit union exception, contains language making the section applicable “[o]n or after January 1, 2010. * * *” This language is redundant of language in section 327.9(d)(7)(i)(A) and the FDIC proposes to delete it.

XIV. Effective Date

The FDIC proposes that a final rule following this proposed rule would become effective on April 1, 2009, except for the proposed uniform increase of seven basis points to current assessment rates, which would take effect January 1, 2009, for the assessment for the first quarter of 2009 only.

XV. Request for Comments

The FDIC seeks comment on every aspect of this proposed rulemaking. In particular, the FDIC seeks comment on the issues set out below. The FDIC asks that commenters include reasons for their positions.

Brokered Deposits

1. Under the proposal, the definition of brokered deposits for purposes of both the adjusted brokered deposit ratio and the brokered deposit adjustment would include sweep accounts and deposits received through a network on a reciprocal basis that meet the statutory definition of a brokered deposit, but would exclude high cost deposits, including those received through a listing service and the Internet, that do not meet the statutory definition of a brokered deposit.

a. Should sweep accounts that meet the statutory definition of brokered deposits be excluded from the definition of brokered deposits for purposes of the adjusted brokered deposit ratio or the

brokered deposit adjustment? If so, how?

b. Should deposits received through a network on a reciprocal basis that meet the statutory definition of brokered deposits be excluded from the definition of brokered deposits for purposes of the adjusted brokered deposit ratio or the brokered deposit adjustment? If so, how?

c. Should high cost deposits, including those received through a listing service and the Internet, that do not meet the statutory definition of a brokered deposit be included in the definition of brokered deposits for purposes of the adjusted brokered deposit ratio or the brokered deposit adjustment? If so, how?

The Adjusted Brokered Deposit Ratio

2. Should the proposed new adjusted brokered deposit ratio be included in the financial ratios method?

3. Under the proposal, only brokered deposits in excess of 10 percent of domestic deposits would be considered. Is this the proper amount or should the percentage be higher or lower?

4. Under the proposal, asset growth over the previous 4 years would have to be greater than 20 percent to potentially trigger the adjusted brokered deposit ratio.

a. Should this amount be higher or lower? Should a different time period be used?

b. Under the proposal, asset growth rates would be determined using data adjusted for mergers and acquisitions. An institution that acquires a new institution (one less than five years old) or that acquires branches from another institution would, in effect, be treated as if its assets had grown from internal growth (since its assets four years previously would not increase, but its current assets would).

i. Should asset growth rates be determined using data adjusted for mergers and acquisitions? An argument can be made that growth from mergers and acquisitions is still growth.

ii. Should growth arising from merger with or the acquisition of or by an institution with no assets four years previously be excluded from the asset growth determination?

iii. Should growth arising from the acquisition of branches from another institution be excluded from the asset growth determination? If so, how could this be done, given that institutions do not report branch acquisitions in the Call Report or TFR?

The Large Bank Method

5. Under the proposal, the assessment rate for a large institution with a long-

term debt issuer rating would be determined using a combination of the institution’s weighted average CAMELS component rating, its long-term debt issuer ratings (converted to numbers and averaged) and the financial ratios method assessment rate, each equally weighted.

a. Should the financial ratios method be incorporated in this manner?

b. Should the weight assigned to each of the three measures be equal, as proposed, or should different weights be assigned?

The Large Bank Adjustment

6. Under the proposal, the maximum large bank adjustment would be increased to one basis point. Should it be increased? Should it be increased further?

The Unsecured Debt Adjustment—

7. Under the proposal, an institution’s base assessment rate could be lowered for the unsecured debt adjustment.

a. Should there be an unsecured debt adjustment?

b. For a large institution, the unsecured debt adjustment would be determined by multiplying the institution’s long-term unsecured debts as a percentage of domestic deposits by 20 basis points.

i. Is this the proper way to calculate an unsecured debt adjustment for a large institution?

ii. Should other amounts be included in the unsecured debt adjustment?

iii. Should any amounts be excluded from the adjustment?

c. Are the proposed definitions of long-term unsecured debts the right definitions or should they be changed?

i. Should a long-term senior unsecured or subordinated debt that has put options or other provisions that would allow the holder to accelerate payment (for example, if capital fell below a certain level) be excluded from the definition? (Under the proposal, it would not be.)

d. Under the proposal, for senior unsecured or subordinated debt to be considered “long-term,” it must have a remaining maturity of at least one year. Should this period be longer? If so, how long should it be?

e. For a small institution, the unsecured debt adjustment would factor in qualified amounts of Tier 1 capital in addition to long-term unsecured debt. The amount of qualified Tier 1 capital would be the sum of one-half of the Tier 1 capital amount between 10 percent and 15 percent of adjusted average assets (for Call Report filers) or adjusted total assets (for TFR filers) and the full amount of Tier 1 capital amount

exceeding 15 percent of adjusted average assets (for Call Report filers) or adjusted total assets (for TFR filers).

i. Should Tier 1 capital be included in the unsecured debt adjustment for a small institution?

ii. Some may be concerned that this proposal might, in effect, establish new capital standards. An alternative would be to count some portion of all Tier 1 capital above 5 percent (the minimum amount needed for an institution to be well capitalized) in the unsecured debt adjustment for small institutions. Is this alternative preferable to the proposal? If so, what portion of Tier 1 capital above 5 percent should be included in the unsecured debt adjustment?

iii. Should the definition of qualified Tier 1 capital be otherwise expanded to include larger amounts of capital or reduced to exclude more capital?

iv. Should other amounts be included in the unsecured debt adjustment?

8. Under the proposal, any decrease in base assessment rates resulting from an unsecured debt adjustment would be limited to two basis points. Is this amount sufficient to encourage a significant number of institutions to issue additional subordinated debt or senior unsecured debt? Should the maximum possible adjustment be larger or smaller?

9. Under the proposal, the unsecured debt adjustment could lower an institution's rate below the minimum initial base assessment rate for its risk category. Should this be allowed?

The Secured Liability Adjustment

10. Under the proposal, an institution's base assessment rates could be increased by the secured liability adjustment.

a. Should there be a secured liabilities adjustment?

b. Should the 15 percent ratio of secured liabilities to domestic deposits be increased or decreased?

c. Should any increase in assessment rates resulting from the secured liability adjustment be limited to 50 percent or should another limit or no limit apply?

Brokered Deposit Adjustment

11. Under the proposal, an institution in Risk Category II, III or IV would also be subject to an adjustment for brokered deposits.

a. Should a brokered deposit adjustment be made?

b. Is the manner of calculating the adjustment appropriate or should it be changed?

i. Should the threshold ratio of brokered deposits to domestic deposits be 10 percent or some higher or lower amount?

ii. Should the multiplication factor be 25 basis points or some higher or lower amount?

c. Should the adjustment be limited to 10 basis points?

Assessment Rates

12. Under the proposal, effective April 1, 2009, the spread between minimum and maximum initial base assessment rates in Risk Category I would increase from the current 2 basis points to an initial range of 4 basis points. Is this the appropriate spread or should it be greater or less?

13. Under the proposal, effective April 1, 2009, based upon June 30, 2008 data, the percentage of both large and small established Risk Category I institutions subject to: (a) The minimum initial base assessment rate would be set at 25 percent; and (b) the maximum initial base assessment rate would be set at 15 percent. (These percentages would change over time as institution's risk measures change.) Are these the proper percentages or should they be higher or lower?

14. Under the proposal, effective April 1, 2009, initial base assessment rates would be as set forth in Table 17 below.

TABLE 17—PROPOSED INITIAL BASE ASSESSMENT RATES

	Risk category				
	I *		II	III	IV
	Minimum	Maximum			
Annual Rates (in basis points)	10	14	20	30	45

* Initial base rates that were not the minimum or maximum rate would vary between these rates.

Should these be the initial base assessment rates or should they be decreased or increased?

15. Under the proposal, effective April 1, 2009, after applying all possible adjustments, total base assessment rates

for each risk category would be as set out in Table 18 below.

TABLE 18—RANGE OF TOTAL BASE ASSESSMENT RATES*

	Risk category I	Risk category II	Risk category III	Risk category IV
Initial base assessment rate	10—14	20	30	45
Unsecured debt adjustment	—2—0	—2—0	—2—0	—2—0
Secured liability adjustment	0—7	0—10	0—15	0—22.5
Brokered deposit adjustment .....	.....	0—10	0—10	0—10
Total base assessment rate	8—21.0	18—40.0	28—55.0	43—77.5

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

a. Are these the appropriate rates or should they be decreased or increased?

b. Is the maximum assessment rates applicable to Risk Categories III and IV

so high that they might cause the failure of an institution that might not otherwise fail? Should rates for Risk Categories III or IV be capped at lower

amounts? If so, what should the cap(s) be?

c. Under the proposal, an institution's initial base assessment rate would be

calculated and adjustments made in the following order: First, any large bank adjustment; second, any unsecured debt adjustment; third, any secured liability adjustment; and, finally, any brokered deposit adjustment. Is this the appropriate order or should it be changed?

16. The proposed rule would continue to allow the FDIC Board to adopt actual rates that were higher or lower than total base assessment rates without the necessity of further notice-and-comment rulemaking, provided that: (1) The Board could not thereafter increase or decrease rates from one quarter to the next by more than three basis points; and (2) cumulative increases and decreases could not be more than three basis points higher or lower than the adjusted base rates without further notice-and-comment rulemaking. Should the Board the FDIC should retain this authority to make changes within prescribed limits to assessment rates, as proposed, without the necessity of additional notice-and-comment rulemaking?

Assessment Rates for the First Quarter of 2009

17. Should the FDIC uniformly increase current assessment rates by seven basis points for the first quarter of 2009 as proposed? Should the increase be greater or less? Should any rate increase be postponed until the second quarter of 2009 when the proposed changes to the assessment system would take effect?

Definition of well capitalized for assessment purposes

18. Recently, some institutions have had to write down or write off the value of stock in Fannie Mae and Freddie Mac. If an institution is adequately or undercapitalized for assessment purposes, but would be well capitalized absent such a write-down or write-off, should it be treated as well capitalized for assessment purposes? If an institution is undercapitalized for assessment purposes, but would be adequately capitalized absent such a write-down or write-off, should it be treated as adequately capitalized for assessment purposes? If so, how would the institution receive such different capital treatment? Should it have to file a request for review with the FDIC?

XVI. 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 proposal and publish the analysis for comment.⁶⁶ 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.⁶⁷ 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 proposed technical and other changes to the FDIC’s assessment regulations. Nonetheless, the FDIC is voluntarily

undertaking an initial regulatory flexibility analysis of the proposal and seeking comment on it.

As of June 30, 2008, of the 8,451 insured commercial banks and savings institutions, there were 4,758 small insured depository institutions as that term is defined for purposes of the RFA (i.e., those with \$165 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 the statutory requirement that the FDIC adopt a restoration plan that provides that the fund reserve ratio reach at least 1.15 percent within five years (absent extraordinary circumstances) and by the FDIC’s aggregate insurance losses, expenses, investment income, and insured deposit growth, among other factors. In this analysis, each institution’s existing rate is increased uniformly so that total FDIC assessment revenue would equal that provided under the proposed rates. Therefore, beginning April 1, 2009, the proposed rule would merely alter the distribution of assessments among insured institutions compared to the adjusted existing rates. Using the data as of June 30, 2008, the FDIC calculated the total assessments that would be collected under the base rate schedule in the proposed rule.

The economic impact of the proposal on each small institution for RFA purposes (i.e., institutions with assets of \$165 million or less) was then calculated as the difference in annual assessments under the proposed rule compared to the existing rule as a percentage of the institution’s annual revenue and annual profits, assuming the same total assessments collected by the FDIC from the banking industry.^{68 69 70}

Based on the June 2008 data, of the total of 4,758 small institutions, five percent would have experienced an increase in assessments equal to five percent or more of their total revenue. These figures do not reflect a significant economic impact on revenues for a substantial number of small insured institutions. Table 19 below sets forth the results of the analysis in more detail.

⁶⁶ See 5 U.S.C. 603, 604 and 605.

⁶⁷ 5 U.S.C. 601.

⁶⁸ Throughout this regulatory flexibility analysis (unlike the rest of the notice of proposed rulemaking), a “small institution” refers to an institution with assets of \$165 million or less.

⁶⁹ An institution’s total revenue is defined as the sum of its annual net interest income and non-interest income. An institution’s profit is defined as income before taxes and extraordinary items, gross of loan loss provisions.

⁷⁰ The proposed rates for the first of 2009 would not alter the present distribution of rates, but would uniformly raise the rates for all institutions, including all small institutions for RFA purposes.

TABLE 19—PROPOSED ASSESSMENTS COMPARED TO A UNIFORM INCREASE IN ASSESSMENTS AS A PERCENTAGE OF INSTITUTION TOTAL REVENUE

Change	Number of institutions	Percent of institutions
More than 10 percent lower	142	2.98
5 to 10 percent lower	1,150	24.17
0 to 5 percent lower	2,975	62.53
0 to 5 percent higher	253	5.32
5 to 10 percent higher	167	3.51
More than 10 percent higher	71	1.49
Total	4,758	100.00

The FDIC performed a similar analysis to determine the impact on profits for small institutions. Based on June 2008 data, of those small institutions with reported profits, about

6 percent would have an increase in assessments equal to 10 percent or more of their profits. Again, these figures do not reflect a significant economic impact on profits for a substantial

number of small insured institutions. Table 20 sets forth the results of the analysis in more detail.

TABLE 20—PROPOSED ASSESSMENTS COMPARED TO A UNIFORM INCREASE IN ASSESSMENTS AS A PERCENTAGE OF INSTITUTION PROFITS*

Change	Number of institutions	Percent of institutions
More than 30 percent lower	496	13.17
20 to 30 percent lower	471	12.51
10 to 20 percent lower	1,666	44.25
5 to 10 percent lower	624	16.57
0 to 5 percent lower	227	6.03
0 to 10 percent more	63	1.67
Greater than 10 percent	218	5.79
Total	3,765	100.00

* Institutions with negative or no profit were excluded. These institutions are shown separately in Table 21.

Table 20 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 proposal on these institutions by

determining the annual assessment change (either an increase or a decrease) that would result. Table 21 below shows that just over 6 percent (61) of the 991 small insured institutions with negative

or no reported profits would have an increase of \$20,000 or more in their annual assessments.

TABLE 21—PROPOSED ASSESSMENTS COMPARED TO A UNIFORM INCREASE IN ASSESSMENTS FOR INSTITUTIONS WITH NEGATIVE OR NO REPORTED PROFIT

Change in assessments	Number of institutions	Percent of institutions
\$20,000 decrease or more	62	6.26
\$10,000–\$20,000 decrease	100	10.09
\$5,000–\$10,000 decrease	213	21.49
\$1,000–\$5,000 decrease	349	35.22
\$0–\$1,000 decrease	63	6.36
\$0–\$10,000 increase	89	8.98
\$10,000–\$20,000 increase	54	5.45
\$20,000 increase or more	61	6.16
Total	991	100.0

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, if adopted in final form, 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.⁷¹

Commenters are invited to provide the FDIC with any information they may have about the likely quantitative effects of the proposal on small insured depository institutions (those with \$165 million or less in assets).

XVII. 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.

A. 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, Pub. L. 109–173, 119 Stat. 3605.

2. Revise § 327.3(a)(1) to read as follows:

§ 327.3 Payment of assessments.

(a) *Required.* (1) *In general.* Each insured depository institution shall pay to the Corporation for each assessment period an assessment determined in accordance with this part 327.

* * * * *

3. Revise § 327.6(b)(1) to read as follows:

§ 327.6 Terminating transfers; other terminations of insurance.

* * * * *

(b) *Assessment for quarter in which the terminating transfer occurs—(1) Acquirer using Average Daily Balances.* If an acquiring institution's assessment base is computed using average daily balances pursuant to § 327.5, the

terminating institution's assessment for the quarter in which the terminating transfer occurs shall be reduced by the percentage of the quarter remaining after the terminating transfer and calculated at the acquiring institution's rate and using the assessment base reported in the terminating institution's report of condition for that quarter.

* * * * *

4. Revise § 327.8(g), (h), (i), (l), and (m), and add paragraphs (o), (p), (q) and (r) 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 (other than an insured branch of a foreign bank or an institution classified as large for purposes of § 327.9(d)(8)) shall be classified as a small institution. If, after December 31, 2006, an institution classified as large under paragraph (h) of this section reports assets of less than \$10 billion in its 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)(8) 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) 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 reports of condition for four consecutive quarters, the FDIC will reclassify the institution as large beginning the following quarter.

(i) *Long-Term Debt Issuer Rating.* A long-term debt issuer rating shall mean a rating of an insured depository institution's long-term debt obligations by Moody's Investor Services, Standard & Poor's, or Fitch Ratings that has not been withdrawn before the end of the quarter being assessed. A withdrawn rating shall mean one that has been withdrawn by the rating agency and not replaced with another rating by the same agency. A long-term debt issuer rating does not include a rating of a company that controls an insured depository institution, or an affiliate or subsidiary of the institution.

* * * * *

(l) *New depository institution.* A new insured depository institution is a bank or thrift that has been federally insured for less than five years as of the last day of any quarter for which it is being assessed.

(m) *Established depository institution.* An established insured depository institution is a bank or thrift 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), (5) of this section and § 327.9(d)(10)(ii), (iii), 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 into a new institution, 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 section.

(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

⁷¹ 5 U.S.C. 605.

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.

* * * * *

(o) *Unsecured debt*—For purposes of the unsecured debt adjustment as set forth in § 327.9(d)(5), 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)(5), senior unsecured liabilities shall be the unsecured portion of other borrowed money as reported on reports of condition (Call Reports and Thrift Financial Reports).

(q) *Subordinated debt*—For purposes of the unsecured debt adjustment as set forth in § 327.9(d)(5), subordinated debt shall be as defined in the report of condition for the reporting period; however, subordinated debt shall also include limited-life preferred stock as defined in the 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)(5), long-term unsecured debt shall be unsecured debt with at least one year remaining until maturity.

5. Revise §§ 327.9 and 327.10 to read as follows:

§ 327.9 Assessment risk categories and pricing methods.

(a) *Risk Categories.*—Each insured depository institution 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.* All institutions in Supervisory Group A that are Well Capitalized;

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

(3) *Risk Category III.* All institutions in Supervisory Groups A and B that are Undercapitalized, and all institutions in Supervisory Group C that are Well Capitalized or Adequately Capitalized; and

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

(b) *Capital evaluations.* An institution 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 institution 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 Initial Base Assessment Rates for Risk Category I Institutions.* Subject to paragraphs (d)(2)(i), (4), (5), (6), (8), (9) and (10) of this section, an insured depository institution in Risk Category I, except for a large institution that has at least one long-term debt issuer rating, as defined in § 327.8(i), shall have its initial base assessment rate determined using the financial ratios method set forth in paragraph (d)(1) of this section. A large insured depository institution in Risk Category I that has at least one long-term debt issuer rating shall have its initial base assessment rate determined using the large bank method set forth in paragraph (d)(2) of this section (subject to paragraphs (d)(2)(i), (4), (5), (6), (8), (9) and (10) of this section). The initial base assessment rate for a large institution whose assessment rate in the prior quarter was determined using the large bank method, but which no longer has a long-term debt issuer rating, shall

be determined using the financial ratios method.

(1) *Financial ratios method.* Under the financial ratios method for 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)(4), (5) and (6) of this section, as appropriate (which will produce the total 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; 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. 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%. Appendix A to this subpart contains the initial values of the pricing multipliers and uniform amount, describes their derivation, 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)(4), (5), and (6) 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)(5), (6) and (7), 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 whose initial base assessment rate is determined using the financial ratios method moving from Risk Category II, III or IV to Risk Category I, 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 financial ratios method, subject to adjustment pursuant to paragraphs (d)(4), (5), and (6) 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)(5), (6) and (7), 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. 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.

(2) *Large bank method.* A large insured depository institution in Risk Category I that has at least one long-term debt issuer rating, as defined in § 327.8(i), shall have its initial base assessment rate determined using the large bank method. The initial base assessment rate under the large bank method shall be derived from three components, each given a 33⅓ percent weight: A component derived using the financial ratios method, a component derived using long-term debt issuer ratings, and a component derived using CAMELS component ratings. An institution's initial base assessment rate using the financial ratios method will be converted from the range of initial base assessment rates to a scale of from 1 to 3 by subtracting 8 from its initial base assessment rate (expressed in basis points) and dividing the result by 2. The quotient will equal an institution's financial ratios score. Its CAMELS component ratings will be weighted to derive a weighted average CAMELS rating using the same weights applied in the financial ratios method as set forth under paragraph (d)(1) of this section. Long-term debt issuer ratings will be converted to numerical values between 1 and 3 as provided in Appendix B to this subpart and the converted values will be averaged. The financial ratios score, the weighted average CAMELS rating and the average of converted long-term debt issuer ratings each will be multiplied by 1.764 (which shall be the pricing multiplier), and the products will be summed. To this result will be added 1.651 (which shall be a uniform amount for all institutions subject to the large bank method). 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)(4), (5), and (6) of this section, as appropriate (which will produce the total base assessment rate), and adjusted for the actual assessment rates set by the Board pursuant to § 327.10(c), will equal an institution's 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.

(i) *Implementation of Large Bank Method Changes between Risk Categories.* If, during a quarter, a CAMELS rating change occurs that results in an institution whose Risk Category I initial base assessment rate is determined using the large bank method or 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 as for any other institution in Risk Category I whose initial base assessment rate is determined using the large bank method, subject to adjustments pursuant to paragraph (d)(4), (5), and (6) of this section, as appropriate, and adjusted for the actual assessment rates set by the Board under § 327.10(c). If, during a quarter, a CAMELS rating change occurs that results in a large institution with a long-term debt issuer rating or 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 under paragraphs (d)(2) (and (d)(4), (5), and (6)) or (d)(3) (and (d)(4), (5), and (6)) of this section, as appropriate.

(ii) *Implementation of Large Bank Method Changes within Risk Category I.* If, during a quarter, an institution whose Risk Category I initial base assessment rate is determined using the large bank method remains in Risk Category I, but the financial ratios score, a CAMELS component or a long-term debt issuer rating changes that would affect the institution's initial base assessment rate, or 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 paragraphs (d)(2) (and (d)(4), (5), and (6)) or (d)(3) (and (d)(4), (5), and (6)) of this section, as appropriate.

(3) *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, as determined under paragraph (d)(3)(ii) of this section.

(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 5.291 (which shall be the pricing multiplier). To this result will be added 1.651 (which shall be a uniform amount for all insured branches of foreign banks). The resulting sum—the initial base assessment rate—subject to adjustments pursuant to paragraph (d)(4) of this section and adjusted for assessment rates set by the FDIC pursuant to § 327.10(c), 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, or the brokered deposit adjustment.

(4) *Adjustment for large banks or insured branches of foreign banks—*(i) *Basis for and size of adjustment.* Within Risk Category I, large institutions and insured branches of foreign banks except new institutions as provided under paragraph (d)(9)(i)(A) of this section, are subject to adjustment of their initial base assessment rate. Any such large bank adjustment shall be limited to a change in assessment rate of up to one basis point higher or lower than the rate determined using the financial ratios method, the large bank method, or the weighted average ROCA component rating method, whichever is applicable. In determining whether to make this assessment rate adjustment for a large institution or an insured branch of a foreign bank, the FDIC may consider other relevant information in addition to the factors used to derive the risk assignment under paragraphs (d)(1), (2), or (3) of this section. Relevant information includes financial performance and condition information, other market or supervisory information, potential loss severity, and stress considerations, as described in Appendix C to this subpart.

(ii) *Adjustment subject to maximum and minimum rates.* No adjustment to the initial base assessment rate for large banks shall decrease any rate so that the resulting rate would be less than the minimum initial base assessment rate, or increase any rate above the maximum

initial base assessment rate in effect for the quarter.

(iii) *Prior notice of adjustments—*(A) *Prior notice of upward adjustment.* Prior to making any upward large bank adjustment to an institution's initial base assessment rate 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 and when the adjustment will take effect.

(B) *Prior notice of downward adjustment.* Prior to making any downward large bank adjustment to an institution's initial base assessment rate because of considerations of additional risk information, the FDIC will formally notify the institution's primary federal regulator and provide an opportunity to respond.

(iv) *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 large bank adjustment to an institution's initial base assessment rate is warranted, taking into account any revisions to weighted average CAMELS component ratings, long-term debt issuer ratings, and financial ratios, 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, until it determines that an adjustment is no longer warranted. 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.

(v) *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 large bank adjustment to an institution's initial base assessment rate is warranted, taking into account any revisions to weighted average CAMELS component ratings, long-term debt issuer ratings, and financial ratios, 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 assessment rate 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.

(vi) *Adjustment without notice.*

Notwithstanding the notice provisions set forth above, the FDIC may change an institution's initial base assessment rate without advance notice under this paragraph, if the institution's supervisory or agency ratings or the financial ratios set forth in Appendix A to this subpart deteriorate.

(5) *Unsecured debt adjustment to initial base assessment rate for all institutions.* All institutions within all risk categories, except new institutions as provided under paragraph (d)(9)(i)(C) of this section and insured branches of foreign banks as provided under paragraph (d)(3)(iii) of this section, are subject to downward adjustment of their initial base assessment rates for unsecured debt, based on the ratio of long-term unsecured debt (and, for small institutions as defined in paragraph (d)(5)(ii) of this section, specified amounts of Tier 1 capital) to domestic deposits. Any such adjustment shall be made after any adjustment under paragraph (d)(4) of this section.

(i) *Large institutions*—The unsecured debt adjustment for large institutions shall be determined by multiplying the institution's ratio of long-term unsecured debt to domestic deposits by 20 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 one-half of the amount between 10 percent and 15 percent of adjusted average assets (for institutions that file Call Reports) or adjusted total assets (for institutions that file Thrift Financial Reports) and the full amount of Tier 1 capital exceeding 15 percent of adjusted average assets (for institutions that file Call Reports) or adjusted total assets (for institutions that file Thrift Financial Reports). The ratio of the sum of qualified Tier 1 capital and long-term unsecured debt to domestic deposits will be multiplied by 20 basis points to produce the unsecured debt adjustment for small institutions.

(iii) *Limitation*—No unsecured debt adjustment for any institution shall exceed two basis points.

(iv) *Applicable reports of condition*—Ratios for any given quarter shall be calculated from reports of condition (Call Reports and Thrift Financial Reports) filed by each institution as of

the last day of the quarter. Until institutions separately report long-term senior unsecured liabilities and long-term subordinated debt in their reports of condition, the FDIC will use subordinated debt included in Tier 2 capital and will not include any amount of senior unsecured liabilities in calculating the unsecured debt adjustment.

(6) *Secured liabilities adjustment for all institutions.* All institutions within all risk categories, except insured branches of foreign banks as provided under paragraph (d)(3)(iii) of this section, are subject to upward adjustment of their initial base assessment rate based upon the ratio of their secured liabilities to domestic deposits. Any such adjustment shall be made after any applicable large bank adjustment or unsecured debt adjustment.

(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 thrifts*—Secured liabilities for thrifts include Federal Home Loan Bank advances as reported in quarterly thrift financial reports. Secured liabilities for thrifts also include securities sold under repurchase agreements, secured Federal funds purchased or other borrowings that are secured when those items are separately reported in thrift financial reports. Until that time, any of these secured amounts not reported separately from unsecured or other liabilities in the TFR will be imputed based on simple averages for Call Report filers as of June 30, 2008. As of that date, on average, 63.0 percent of the sum of Federal funds purchased and securities sold under repurchase agreements reported by Call Report filers were secured, and 49.4 percent of other borrowings were secured.

(iii) *Calculation*—An institution's ratio of secured liabilities to domestic deposits will, if greater than 15 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 15 percent, the institution's initial base assessment rate (after taking into account any adjustment under paragraphs (d)(5) or (6) of this section) will be multiplied by one plus the ratio of its secured liabilities to domestic

deposits minus 0.15. Ratios of secured liabilities to domestic deposits shall be calculated from the report of condition filed by each institution as of the last day of the quarter.

(7) *Brokered Deposit Adjustment for Risk Categories II, III, and IV.* All institutions in Risk Categories II, III, and IV, except insured branches of foreign banks as provided under paragraph (d)(3)(iii) of this section, shall be subject to an initial base assessment rate adjustment for brokered deposits. Any such brokered deposit adjustment shall be made after any adjustment under paragraph (d)(5) or (6). A brokered deposit is as defined in Section 29 of the Federal Deposit Insurance Act (12 U.S.C. 1831f). 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 the difference between an institution's ratio of brokered deposits to domestic deposits and 0.10 by 25 basis points. The maximum brokered deposit adjustment will be 10 basis points. Brokered deposit ratios for any given quarter are calculated from the reports of condition filed by each institution as of the last day of the quarter.

(8) *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 initial base assessment rate as a large institution. The FDIC will grant such a request if it determines that it has sufficient information to do so. The absence of long-term debt issuer ratings alone will not preclude the FDIC from granting a request. The initial base assessment rate for an institution without a long-term debt issuer rating will be derived using the financial ratios method, but will be subject to adjustment as a large institution under paragraph (d)(4) of this section. 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).

(9) *New and established institutions and exceptions*—(i) *New Risk Category I institutions*—(A) *Rule as of January 1, 2010*. Effective for assessment periods beginning on or after January 1, 2010, a new institution 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)(9)(ii) and (iii) of this section. No new institution in Risk Category I shall be subject to the large bank adjustment as determined under paragraph (d)(4) of this section.

(B) *Rule prior to January 1, 2010*. Prior to January 1, 2010, a new institution's initial base assessment rate shall be determined under paragraph (d)(1) or (2) of this section, as appropriate. Prior to January 1, 2010, a Risk Category I institution that has no CAMELS component ratings 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. The initial base assessment rate will be determined by annualizing, where appropriate, financial ratios obtained from the reports of condition that have been filed, until the institution files four reports of condition.

(C) *Applicability of adjustments to new institutions prior to and as of January 1, 2010*. No new institution in any risk category shall be subject to the unsecured debt adjustment as determined under paragraph (d)(5) of this section. All new institutions in any Risk Category shall be subject to the secured liability adjustment as determined under paragraph (d)(6) of this section. All new institutions in Risk Categories II, III, and IV shall be subject to the brokered deposit adjustment as determined under paragraph (d)(7) of this section.

(ii) *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.

(iii) *Rate applicable to institutions subject to subsidiary or credit union exception*. If an 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. The assessment rate will be determined by annualizing, where appropriate, financial ratios obtained from all reports of condition that have been filed, until it receives a long-term debt issuer rating.

(iv) *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).

(10) *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)(4), (5), (6) or (7) of this section.

§ 327.10 Assessment rate schedules.

(a) *Assessment Rate Schedule for First Quarter of 2009 and Initial Base Assessment Rate Schedule Beginning April 1, 2009*. The annual assessment rate for an insured depository institution for the quarter beginning January 1, 2009 shall be the rate prescribed in the following schedule:

TABLE 1 TO PARAGRAPH (A)—ASSESSMENT RATE SCHEDULE FOR FIRST QUARTER OF 2009

	Risk category				
	I *		II	III	IV
	Minimum	Maximum			
Annual Rates (in basis points)	12	14	17	35	50

The annual initial base assessment rate for an insured depository institution beginning April 1, 2009, shall be the rate prescribed in the following schedule:

TABLE 2 TO PARAGRAPH (A)—INITIAL BASE ASSESSMENT RATE SCHEDULE BEGINNING APRIL 1, 2009

	Risk category				
	I *		II	III	IV
	Minimum	Maximum			
Annual Rates (in basis points)	10	14	20	30	45

* Initial base rates that are not the minimum or maximum rate will vary between these rates.

(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 20, 30, and 45 basis points, respectively.

(3) 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) *Total Base Assessment Rate Schedule after Adjustments.* For assessment periods beginning on or after

April 1, 2009, the total base assessment rates after adjustments for an insured depository institution shall be the rate prescribed in the following schedule.

TABLE 1 TO PARAGRAPH (b)—TOTAL BASE ASSESSMENT RATE SCHEDULE (AFTER ADJUSTMENTS) *

	Risk category I	Risk category II	Risk category III	Risk category IV
Initial base assessment rate	10–14	20	30	45
Unsecured debt adjustment	–2–0	–2–0	–2–0	–2–0
Secured liability adjustment	0–7	0–10	0–15	0–22.5
Brokered deposit adjustment .....	.....	0–10	0–10	0–10
Total base assessment rate	8–21.0	18–40.0	28–55.0	43–77.5

* 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.

(1) *Risk Category I Total Base Assessment Rate Schedule.* The annual total base assessment rates for all institutions in Risk Category I shall range from 8 to 21 basis points.

(2) *Risk Category II Total Base Assessment Rate Schedule.* The annual total base assessment rates for Risk Category II shall range from 18 to 40 basis points.

(3) *Risk Category III Total Base Assessment Rate Schedule.* The annual total base assessment rates for Risk Category III shall range from 28 to 55 basis points.

(4) *Risk Category IV Total Base Assessment Rate Schedule.* The annual total base assessment rates for Risk Category IV shall range from 43 to 77.5 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 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 Appendices A, B, and C 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;

- The minimum initial base assessment rate for Risk Category I, equal to 10 basis points, 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

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

where Downgrade(0,1)_{i,t} (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 assets growth rate factor that ranges from 0 to 1 as shown in Equation 2 below. The assets growth rate factor (*A_{i,T}*) is calculated by subtracting 0.2 from the four-year cumulative asset growth rate (expressed as a number rather than as a percentage), adjusted for mergers and acquisitions, and multiplying the remainder by 5. The factor cannot be less than 0 or greater than 1.

Equation 2

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

$$\text{where } A_{i,T} = \left[\left(\frac{\text{Assets}_{i,T} - \text{Assets}_{i,T-4}}{\text{Assets}_{i,T-4}} - 0.2 \right) * 5 \right], \text{ subject to } 0 \leq A_{i,T} \leq 1 \text{ and } B_{i,T} \geq 0.$$

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. In addition, 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.

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.

TABLE A.1—DEFINITIONS OF REGRESSORS—Continued

Regressor	Description
Adjusted Brokered Deposits/Domestic Deposits (%).	Brokered deposits divided by domestic deposits less 0.10 multiplied by the asset growth rate factor (four year cumulative asset growth rate (expressed as a number rather than as a percentage) divided by 5 less one).
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 each for the “E” and “L” components. (For the regression, the “S” component is omitted.)

The financial variable regressors used to estimate the downgrade probabilities are obtained from quarterly reports of condition (Reports of Condition and Income and Thrift Financial Reports). The weighted average of the “C,” “A,” “M,” “E” and “L” component ratings regressor is based on component ratings obtained from the most recent bank examination conducted within 24 months before the date of the report of condition.

The Statistical Model uses ordinary least squares (OLS) regression to estimate downgrade probabilities. The model is estimated with data from a multi-year period (as explained below) for all institutions in Risk Category I, except for institutions

established within five years before the date of the report of condition.

The OLS regression estimates coefficients, β_j for a given regressor j and a constant amount, β_0 , as specified in equation 1. As shown in equation 3 below, these coefficients are multiplied by values of risk measures at time T , which is the date of the report of condition corresponding to the end of the quarter for which the assessment rate is computed. The sum of the products is then added to the constant amount to produce an estimated probability, d_{iT} , that an institution will be downgraded to 3 or worse within 3 to 12 months from time T .

The risk measures are financial ratios as defined in Table A.1, except that the loans past due 30 to 89 days ratio and the nonperforming asset ratio are adjusted to exclude the maximum amount recoverable from the U.S. Government, its agencies or government-sponsored agencies, under guarantee or insurance provisions. Also, the weighted sum of six CAMELS component ratings is used, with weights of 25 percent each for the “C” and “M” components, 20 percent for the “A” component, and 10 percent each for the “E,” “L,” and “S” components.

Equation 3

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

III. Minimum and Maximum Downgrade Probability Cutoff Values

The pricing multipliers are also determined by minimum and maximum downgrade probability cutoff values, which will be computed as follows:

- The minimum downgrade probability cutoff value will be the maximum downgrade probability among the twenty-five percent of all small insured institutions in Risk Category I (excluding new institutions) with the lowest estimated downgrade probabilities, computed using values of the

risk measures as of June 30, 2008.^{72 73} The minimum downgrade probability cutoff value is approximately 2 percent.

- The maximum downgrade probability cutoff value will be the minimum downgrade probability among the fifteen percent of all small insured institutions in Risk Category I (excluding new institutions) with the highest estimated downgrade probabilities, computed using values of the risk measures as of June 30, 2008. The maximum downgrade probability cutoff value is approximately 15 percent.

IV. Derivation of Uniform Amount and Pricing Multipliers

The uniform amount and pricing multipliers used to compute the annual base assessment rate in basis points, P_{iT} , for any such institution i at a given time T will be determined from the Statistical Model, the minimum and maximum downgrade probability cutoff values, and minimum and maximum initial base assessment rates in Risk Category I as follows:

Equation 4

$$P_{iT} = \alpha_0 + \alpha_1 * d_{iT} \text{ subject to } \text{Min} \leq P_{iT} \leq \text{Min} + 4$$

⁷² As used in this context, a “new institution” means an institution that has been chartered as a bank or thrift for less than five years.

⁷³ For purposes of calculating the minimum and maximum downgrade probability cutoff values, institutions that have less than \$100,000 in

domestic deposits are assumed to have no brokered deposits.

where α_0 and α_1 are a constant term and a scale factor used to convert d_{iT} (the estimated downgrade probability for institution i at a given time T from the Statistical Model) to an assessment rate, respectively, and Min is the minimum initial base assessment rate expressed in basis points. (P_{iT} is expressed

as an annual rate, but the actual rate applied in any quarter will be $P_{iT}/4$.) The maximum initial base assessment rate is 4 basis points above the minimum ($Min + 4$)

Solving equation 4 for minimum and maximum initial base assessment rates simultaneously,

$$Min = \alpha_0 + \alpha_1 * 0.0181 \text{ and } Min + 4 = \alpha_0 + \alpha_1 * 0.1505$$

where 0.0181 is the minimum downgrade probability cutoff value and 0.1505 is the maximum downgrade probability cutoff value, results in values for the constant amount, α_0 , and the scale factor, α_1 :

Equation 5

$$\alpha_0 = Min - \frac{4 * 0.0181}{(0.1505 - 0.0181)} = Min - 0.547$$

and Equation 6

$$\alpha_1 = \frac{4}{(0.1505 - 0.0181)} = 30.211$$

Substituting equations 3, 5 and 6 into equation 4 produces an annual initial base assessment rate for institution i at time T , P_{iT} ,

in terms of the uniform amount, the pricing multipliers and the ratios and weighted

average CAMELS component rating referred to in 12 CFR 327.9(d)(2)(i):

Equation 7

$$P_{iT} = [(Min - 0.547) + 30.211 * \beta_0] + 30.211 * [\beta_1 (\text{Tier 1 Leverage Ratio}_T)] + \\ 30.211 * [\beta_2 (\text{Loans past due 30 to 89 days ratio}_T)] + \\ 30.211 * [\beta_3 (\text{Nonperforming asset ratio}_T)] + \\ 30.211 * [\beta_4 (\text{Net loan charge-off ratio}_T)] + \\ 30.211 * [\beta_5 (\text{Net income before taxes ratio}_T)] + \\ 30.211 * [\beta_6 (\text{Weighted average CAMELS component rating}_T)] + \\ 30.211 * [\beta_7 (\text{Brokered Deposit-AssetGrowth Interaction Term}_T)]$$

again subject to $Min \leq P_{iT} \leq Min + 4$

where $(Min - 0.547) + 30.211 * \beta_0$ equals the uniform amount, $30.211 * \beta$ is a pricing multiplier for the associated risk measure j , and T is the date of the report of condition corresponding to the end of the quarter for which the assessment rate is computed.

V. Updating the Statistical Model, Uniform Amount, and Pricing Multipliers

The initial Statistical Model is estimated using year-end financial ratios and the

weighted average of the “C,” “A,” “M,” “E” and “L” component ratings over the 1988 to 2006 period and downgrade data from the 1989 to 2007 period. The FDIC may, from time to time, but no more frequently than annually, re-estimate the Statistical Model with updated data and publish a new formula for determining initial base assessment rates—Equation 7—based on updated uniform amounts and pricing

multipliers. However, the minimum and maximum downgrade probability cutoff values will not change without additional notice-and-comment rulemaking. The period covered by the analysis will be lengthened by one year each year; however, from time to time, the FDIC may drop some earlier years from its analysis.

Appendix B to Subpart A**NUMERICAL CONVERSION OF LONG-TERM DEBT ISSUER RATINGS**

Current long-term debt issuer rating	Converted value
Standard & Poor's:	
AAA	1.00
AA+	1.05
AA	1.15
AA-	1.30
A+	1.50
A	1.80
A-	2.20
BBB+	2.70
BBB or worse	3.00

NUMERICAL CONVERSION OF LONG-TERM DEBT ISSUER RATINGS—Continued

Current long-term debt issuer rating	Converted value
Moody's:	
Aaa	1.00
Aa ¹	1.05
Aa ²	1.15
Aa ³	1.30
A1	1.50
A2	1.80
A3	2.20
Baa ¹	2.70
Baa ² or worse	3.00
Fitch's:	

NUMERICAL CONVERSION OF LONG-TERM DEBT ISSUER RATINGS—Continued

Current long-term debt issuer rating	Converted value
AAA	1.00
AA+	1.05
AA	1.15
AA-	1.30
A+	1.50
A	1.80
A-	2.20
BBB+	2.70
BBB or worse	3.00

Appendix C to Subpart A**ADDITIONAL RISK CONSIDERATIONS FOR LARGE RISK CATEGORY I INSTITUTIONS**

Information Source	Examples of associated risk indicators or information
Financial Performance and Condition Information.	<p>Capital Measures (Level and Trend).</p> <ul style="list-style-type: none"> Regulatory capital ratios. Capital composition. Dividend payout ratios. Internal capital growth rates relative to asset growth. <p>Profitability Measures (Level and Trend).</p> <ul style="list-style-type: none"> Return on assets and return on risk-adjusted assets. Net interest margins, funding costs and volumes, earning asset yields and volumes. Noninterest revenue sources. Operating expenses. Loan loss provisions relative to problem loans. Historical volatility of various earnings sources. <p>Asset Quality Measures (Level and Trend).</p> <ul style="list-style-type: none"> Loan and securities portfolio composition and volume of higher risk lending activities (e.g., sub-prime lending). Loan performance measures (past due, nonaccrual, classified and criticized, and renegotiated loans) and 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. Loan loss reserve trends. Loan growth and underwriting trends. Off-balance sheet credit exposure measures (unfunded loan commitments, securitization activities, counterparty derivatives exposures) and hedging activities. <p>Liquidity and Funding Measures (Level and Trend).</p> <ul style="list-style-type: none"> Composition of deposit and non-deposit funding sources. Liquid resources relative to short-term obligations, undisbursed credit lines, and contingent liabilities. <p>Interest Rate Risk and Market Risk (Level and Trend).</p> <ul style="list-style-type: none"> Maturity and repricing information on assets and liabilities, interest rate risk analyses. Trading book composition and Value-at-Risk information.
Market Information	<ul style="list-style-type: none"> Subordinated debt spreads. Credit default swap spreads. Parent's debt issuer ratings and equity price volatility. Market-based measures of default probabilities. Rating agency watch lists. Market analyst reports.
Information Source	Examples of associated risk indicators or information
Stress Considerations	<p>Ability to Withstand Stress Conditions.</p> <ul style="list-style-type: none"> Internal analyses of portfolio composition and risk concentrations, and vulnerabilities to changing economic and financial conditions. Stress scenario development and analyses. Results of stress tests or scenario analyses that show the degree of vulnerability to adverse economic, industry, market, and liquidity events. Examples include: <ul style="list-style-type: none"> An evaluation of credit portfolio performance under varying stress scenarios. An evaluation of non-credit business performance under varying stress scenarios. An analysis of the ability of earnings and capital to absorb losses stemming from unanticipated adverse events. Contingency or emergency funding strategies and analyses. Capital adequacy assessments. <p>Loss Severity Indicators.</p>

ADDITIONAL RISK CONSIDERATIONS FOR LARGE RISK CATEGORY I INSTITUTIONS—Continued

Information Source	Examples of associated risk indicators or information
	<ul style="list-style-type: none">• Nature of and breadth of an institution's primary business lines and the degree of variability in valuations for firms with similar business lines or similar portfolios.• Ability to identify and describe discreet business units within the banking legal entity.• Funding structure considerations relating to the order of claims in the event of liquidation (including the extent of subordinated claims and priority claims).• Extent of insured institutions assets held in foreign units.• Degree of reliance on affiliates and outsourcing for material mission-critical services, such as management information systems or loan servicing, and products.• Availability of sufficient information, such as information on insured deposits and qualified financial contracts, to resolve an institution in an orderly and cost-efficient manner.

Dated at Washington, DC, this 7th day of October, 2008.
Federal Deposit Insurance Corporation.
By order of the Board of Directors.
Federal Deposit Insurance Corporation.
Valerie Best,
Assistant Executive Secretary.

Appendix 1
Uniform Amount and Pricing Multipliers for Large Risk Category I Institutions Where Long-Term Debt Issuer Ratings Are Available

The uniform amount and pricing multipliers for large Risk Category I institutions with long-term debt issuer ratings were derived from:

- The average long-term debt issuer rating, converted into a numeric value (the long-term debt score) ranging from 1 to 3;
- The weighted average CAMELS rating, as defined in Appendix A;
- The assessment rate calculated using the financial ratios method described in Appendix A, converted to a value ranging from 1 to 3 (the financial ratios score);
- Minimum and maximum cutoff values for an institution's score (the average of the long-term debt score, weighted average

CAMELS rating and financial ratios score), based on data from June 30, 2008, which was used to determine the proportion of large banks charged the minimum and maximum initial base assessment rates applicable to Risk Category I; and

- Minimum and maximum initial base assessment rates for Risk Category I

The financial ratios assessment rate (A_f) calculated using the pricing multipliers and uniform amount described in Appendix A was converted to a financial ratios score (S_f), with a value ranging from 1 to 3 as shown in Equation 1:

Equation 1

$$S_f = (A_f - 8) * 0.5$$

Each institution's score (S_i) was calculated by dividing its weighted average CAMELS rating (S_w), long-term issuer score (S_d) and financial ratios score (S_f) by 1/3 each, and summing the resulting values as shown in Equation 2:

Equation 2

$$S_i = (1/3) * S_{w,i} + (1/3) * S_{d,i} + (1/3) * S_{f,i}$$

The pricing multipliers were determined by minimum and maximum score cutoff values, which were computed as follows:

- The minimum score cutoff value is the maximum score among the twenty-five percent of all large insured institutions in Risk Category I (excluding new institutions) with the lowest scores, computed as of June 30, 2008.⁷⁴ The minimum score cut-off value is 1.578.
- The maximum score cutoff value is the minimum score among the fifteen percent of all large insured institutions in Risk Category I (excluding new institutions) with the highest scores, computed as of June 30, 2008. The maximum score cut-off value is 2.334.

The uniform amount and pricing multipliers used to compute the annual base assessment rate in basis points, $P_{i,T}$, for a large institution i (with a long-term debt rating) at a given time T were determined based on the minimum and maximum score cut-off values, and the minimum and maximum initial base assessment rates in Risk Category I as follows:

Equation 3

$$P_{i,T} = \alpha_0 + \alpha_1 * S_{i,T} \text{ subject to } Min \leq P_{i,T} \leq Min + 4$$

where α_0 and α_1 are, respectively, a constant term and a scale factor used to convert $S_{i,T}$ (an institution's score at time T) to an assessment rate, and Min is the minimum initial base assessment rate expressed in basis points. (Under the proposal, the minimum initial base assessment rate is 10 basis points, so Min equals 10.)

Substituting minimum and maximum score cutoff values (1.578 and 2.334, respectively) for $S_{i,T}$ and minimum and maximum initial base assessment rates (Min and $Min + 4$, respectively) for $P_{i,T}$ in equation 3 produces equations 4 and 5 below.

Equation 4

$$Min = \alpha_0 + \alpha_1 * 1.578$$

Equation 5

$$Min + 4 = \alpha_0 + \alpha_1 * 2.334$$

Solving both equations simultaneously results in:

Equation 6

$$\alpha_0 = Min - \frac{4 * 1.578}{(2.334 - 1.578)} = Min - 8.349$$

Equation 7

$$\alpha_1 = \frac{4}{(2.334 - 1.578)} = 5.291$$

⁷⁴ As used in this context, a "new institution" means an institution that has been chartered as a bank or thrift for less than five years.

Substituting equations 6 and 7 into equation 2 produces the following equation for P_{iT}

Equation 8

$$P_{iT} = (Min - 8.349) + 5.291 * \left[(1/3) * S_{w,iT} + (1/3) * S_{d,iT} + (1/3) * S_{f,iT} \right] \\ = (Min - 8.349) + 1.764 * S_{w,iT} + 1.764 * S_{d,iT} + 1.764 * S_{f,iT}$$

where $Min - 8.349$ is the uniform amount and 1.764 is a pricing multiplier. Since Min equals 10 under the proposal, the uniform amount equals 1.651.

Appendix 2

Unsecured Debt Adjustment for a Small Institution

The unsecured debt adjustment for a small institution would be calculated based on the sum of the institution's long-term senior unsecured debt, long-term subordinated debt

and qualified Tier 1 capital as a percentage of total domestic deposits.

Qualified Tier 1 capital depends on the institution's Tier 1 capital and adjusted average or total assets and would be calculated in one of two ways. If the institution's Tier 1 leverage ratio were greater than 15 percent, qualified Tier 1 capital would be calculated as:

Equation 1

$$Q_i = C_i - (G_i * 0.125), \text{ subject to } Q_i > 0$$

where Q is qualified Tier 1 capital, C is total Tier 1 capital and G is the adjusted average or total assets for an institution i . If the institution's Tier 1 leverage ratio were greater than 10 percent but less than 15 percent, then qualified Tier 1 capital would be calculated as:

Equation 2

$$Q_i = 0.5 * [C_i - (G_i * 0.10)], \text{ subject to } Q_i > 0$$

The unsecured debt adjustment would then be calculated as:

Equation 3

$$Adj_i = \left(\frac{U_i + S_i + Q_i}{D_i} \right) * 20 \text{ basis points}, \text{ subject to } Adj_i \leq 2 \text{ basis points}$$

where Adj is the unsecured debt adjustment, U is long-term unsecured senior debt, S is long-term subordinated debt and D is domestic deposits for institution i .

Appendix 3

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

I. Introduction

This analysis estimates the effect in 2009 of proposed deposit insurance assessments on the equity capital and profitability of all insured institutions, assuming that the Board adopts the proposed rule.⁷⁵ The analysis assumes that each institution's pre-tax, pre-assessment income in 2009 is equivalent to the amount reported over the four quarters ending in June 2008. Each institution's rate

under the proposed rate schedule is based on data as of June 30, 2008.⁷⁶ In addition, the projected use of one-time credits authorized under the Reform Act is taken into consideration in determining the effective assessment for an institution.

II. Analysis of the Projected Effects on Capital and Earnings

While deposit insurance assessment rates 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.⁷⁷

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

⁷⁵ Beginning April 1, 2009, initial minimum base assessment rates would range from 10 to 45 basis points under the proposal. After adjustments to the base rates, total base rates would range from 8 to 77.5 basis points. For the first quarter of 2009, assessment rates would range from 12 to 50 basis points.

⁷⁶ For purposes of this analysis, the assessment base (like income) is not assumed to increase, but is assumed to remain at June 2008 levels. All income statement items used in this analysis were adjusted for the effect of mergers. Institutions for which four quarters of earnings data were unavailable, including insured branches of foreign banks, were excluded from this analysis.

⁷⁷ The analysis does not incorporate any tax effects from an operating loss carry forward or carry back.

rate (that is, dividends as a fraction of net income) unchanged from the weighted average rate reported over the four quarters ending June 30, 2008. 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 equity capital of insured institutions as of June 30, 2008 was \$1.35 trillion.⁷⁸ Based on the assumptions for earnings described above, year-end 2009 equity capital is projected to equal \$1.373 trillion if the recommended assessment rates are adopted. In the absence of an assessment, total equity

would be an estimated \$5 billion higher. Alternatively, total equity would be an estimated \$2 billion higher if current rates remained in effect.

Table A.1 shows the distribution of the effects of assessments (net of credits) on 2009 equity capital levels across the banking industry compared to no assessments. On an industry weighted average basis, projected total assessments in 2009 would result in capital that is 0.3 percent less than in the absence of assessments. Table A.2 shows the distribution of the effects of the proposed increase in assessments on 2009 equity capital levels across the banking industry. On an industry weighted average basis, the projected increases in assessments in 2009

would result in capital that is 0.1 percent less than if current assessment rates remained in effect.

The analysis indicates that assessments would cause 6 institutions whose equity-to-assets ratio would have exceeded 4 percent in the absence of assessments to fall below that percentage and 5 institutions to have below 2 percent equity-to-assets that otherwise would not have. Alternatively, compared to current assessments, the proposed increase in assessments would cause 3 institutions whose equity-to-assets ratio would otherwise have exceeded 4 percent to fall below that threshold and 1 institution to fall below 2 percent equity-to-assets.

TABLE A.1—PERCENTAGE REDUCTION IN EQUITY CAPITAL DUE TO ASSESSMENTS

[\$ in billions]

Reduction in capital (percent)	Number of institutions	Percent of institutions (percent)	Total assets	Percent of assets
0.0–0.1	785	9	2,527	19
0.1–0.2	835	10	1,191	9
0.2–0.3	914	11	1,253	9
0.3–0.4	928	11	4,617	35
0.4–0.5	896	11	620	5
0.5–1.0	2,770	33	1,573	12
>1.0	1,210	15	1,515	11
Total	8,338	100	13,296	100

TABLE A.2—PERCENTAGE REDUCTION IN EQUITY CAPITAL DUE TO PROPOSED INCREASES IN ASSESSMENTS

[\$ in billions]

Reduction in capital (percent)	Number of institutions	Percent of institutions (percent)	Total assets	Percent of assets (percent)
0.0–0.1	1,893	23	4,348	33
0.1–0.2	2,427	29	5,662	43
0.2–0.3	1,940	23	995	7
0.3–0.4	956	11	954	7
0.4–0.5	444	5	580	4
0.5–1.0	547	7	436	3
> 1.0	131	2	322	2
Total	8,338	100	13,296	100

11 insured branches of foreign banks and 113 institutions having less than 4 quarters of reported earnings were excluded from this analysis. Equity capital referred to in this analysis is the same as defined under Generally Accepted Accounting Principles.

The effect of assessments on institution income is measured by deposit insurance assessments as a percent of income before assessments, taxes, and extraordinary items (hereafter referred to as “income”). This income measure is used in order to eliminate the potentially transitory effects of extraordinary items and taxes on profitability. Table A.3 shows that, under the proposed rate schedule, approximately 56 percent of profitable institutions are projected to owe assessments that are less

than 8 percent of income in 2009. The median projected reduction in income for profitable institutions under the recommended rates is 7.3 percent, while the weighted average reduction for the same institutions is 4.4 percent. For the industry as a whole (including profitable and unprofitable institutions), assessments in 2009 would reduce income by 11 percent.

Table A.4 shows that the proposed increase in assessments from current levels exceeds 5 percent of income in 2009 for approximately

33 percent of profitable institutions. The median projected reduction in income for profitable institutions from the proposed increase in rates under the proposal is 3.6 percent, while the weighted average reduction for the same institutions is 2.2 percent. For the industry as a whole (including profitable and unprofitable institutions), the increase in assessments in 2009 would reduce income by 5.6 percent compared to current rates.

⁷⁸ This excludes equity for those mentioned in the note to Tables A.1 and A.2.

TABLE A.3—ASSESSMENTS AS A PERCENT OF INCOME FOR PROFITABLE INSTITUTIONS
[\$ in billions]

Assessments as pct. of income	Number of profitable institutions	Percent of institutions (percent)	Assets of profitable institutions	Percent of assets (percent)
0.0–4.0	1,036	15	4,021	42
4.0–6.0	1,618	23	1,293	13
6.0–8.0	1,303	18	2,367	25
8.0–10.0	768	11	336	3
10.0–12.0	475	7	396	4
12.0–15.0	497	7	311	3
15.0–20.0	428	6	274	3
> 20.0	1,001	14	621	6
Total	7,126	100	9,618	100

TABLE A.4—PROPOSED INCREASES IN ASSESSMENTS AS A PERCENT OF INCOME FOR PROFITABLE INSTITUTIONS
[\$ in billions]

Assessments as pct. of income	Number of profitable institutions	Percent of institutions (percent)	Assets of profitable institutions	Percent of assets (percent)
0.0–0.5	126	2	723	8
0.5–1.0	87	1	573	6
1.0–2.0	768	11	2,529	26
2.0–3.0	1,702	24	1,185	12
3.0–4.0	1,345	19	2,616	27
4.0–5.0	754	11	437	5
5.0–10.0	1,382	19	919	10
> 10.0	962	13	636	7
Total	7,126	100	9,618	100

Income is defined as income before taxes, extraordinary items, and deposit insurance assessments. Assessments are adjusted for the use of one-time credits. Unprofitable institutions are defined as those having negative merger-adjusted income (as defined above) over the 4 quarters ending June 30, 2008, and, by assumption, in 2009. There were 1212 unprofitable institutions excluded from Tables A.3 and A.4. 11 insured branches of foreign banks and 113 institutions having less than 4 quarters of reported earnings were excluded from this analysis. Figures may not sum to totals due to rounding.

Dated at Washington DC, this 7th day of
October, 2008.

By order of the Board of Directors.

Federal Deposit Insurance Corporation.

Valerie J. Best,

Assistant Executive Secretary.

[FR Doc. E8–24186 Filed 10–8–08; 4:15 pm]

BILLING CODE 6714–01–P