FEDERAL DEPOSIT INSURANCE CORPORATION

12 CFR Part 304

Forms, Instructions, and Reports

AGENCY: Federal Deposit Insurance Corporation ("FDIC").

ACTION: Proposed rule.

SUMMARY: The FDIC is proposing to substitute for its current regulation on reporting fully insured brokered deposits and fully insured deposits placed directly by other depository institutions (12 CFR 304.6) a new requirement calling for the reporting of planned rapid growth by whatever means, including the solicitation and acceptance of brokered deposits and direct deposits by other depository institutions. Essentially, the new proposal would require an insured bank to report by means of a check-off question on its Reports of Condition and Income any intention to grow rapidly, that is, by more than nine percent during the following three months. Any bank reporting an intention to grow that rapidly would be prohibited from implementing its plans for a period of 30 days from the submission of its Reports of Condition and Income. As an interim measure, unless and until a question regarding planned rapid growth can be included on the Reports of Condition and Income, insured banks would be required to report their intention to grow rapidly by means of a letter or other written communication mailed or otherwise directed to the appropriate FDIC regional director for bank supervision. Moreover, whenever rapid growth occurs that was not planned and covered by a prior notice given through a Reports of Condition and Income submission or separate letter or other communication, the bank would be required to report promptly the fact of that growth to the appropriate FDIC regional director for supervision.

DATES: Comments must be received by June 5, 1989.

ADDRESS: Send comments to Hoyle L. Robinson, Executive Secretary, Federal Deposit Insurance Corporation, 550 17th Street, NW., Washington, DC 20429. Comments may be hand delivered to Room 6092 on business days between 8:30 a.m. and 5:00 p.m. Comments may also be inspected in Room 6092 between 8:30 a.m. and 5:00 p.m. on business days.

FOR FURTHER INFORMATION CONTACT: William G. Hrindac, Examination Specialist, Division of Bank Supervision, (202) 898–6892, Federal Deposit Insurance Corporation, 550 17th Street, NW., Washington, DC 20429.

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

The notice requirements contained in the proposed regulation do not constitute "collections of information" for purposes of the Paperwork Reduction Act (44 U.S.C. 3501 *et seq.*) and therefore are not subject to the Office of Management and Budget ("OMB") clearance provisions of that Act. This is because the notice requirements fall within the exception to the definition of "information" set out in § 1320.7(j)(1) of OMB regulations implementing the "collection of information clearance" provisions of the Act (5 CFR Part 1320). It is recognized, however, that the notice requirements do place an affirmative obligation on a bank to notify the FDIC of its intended action to grow rapidly or that rapid growth has occurred. Any costs associated with these notices would appear, however, to be minimal. The proposed regulation does not specify the content of the written notices or require the bank to provide any more specific information beyond that indicated.

Regulatory Flexibility Act

The FDIC's Board of Directors hereby certifies that the proposed regulation will not have a significant economic impact on a substantial number of small entities because it will simply require occasional reporting by a relatively small percentage of insured banks regarding their intent to grow rapidly or the fact that they have grown rapidly. These types of communications have always been a routine part of the bank supervisory process. Moreover, the additional economic impact will be more than offset by the elimination of explicit reporting requirements calling for the special compilation and periodic reporting of data on fully insured brokered deposits and direct deposits of other depository institutions. Overall, the net impact of the change may be a significant reduction in the cost and burden on small banks. Consequently, the provisions of the Regulatory Flexibility Act relating to an initial and final regulatory flexibility analysis (5 U.S.C. 603 and 604) are not applicable.

Discussion

A number of instances have developed over the last few years where insured banks have grown very rapidly in a short period of time and have concurrently developed serious asset and/or other problems. In fact, some of these institutions have failed very quickly thereafter, even though these same banks had operated satisfactorily prior to the unwise growth.

Various mechanisms have been used to fund that growth, including brokered deposits, direct borrowings, use of repurchase agreements, direct solicitation of deposits throughout the country by a "money desk" operation, and simply paying above market rates. The FDIC believes it necessary to enhance its ability to monitor rapid growth in time to apply appropriate supervision.

Since a bank may obtain its funding from a variety of sources in addition to brokered deposits, the FDIC believes that any effort to monitor and control rapid growth in insured banks should not focus solely or even principally on brokered deposits. Instead, the focus should be on rapid growth *per se* as an indication of the need for close monitoring and supervisory oversight. Moreover, in order to assess its insurance risk, the FDIC believes that, insofar as practical, it should receive as much prior notice of anticipated rapid growth as possible in order to deter and perhaps forestall imprudent loans and investments before the fact rather than attempting to control and limit abuses and losses after the fact.

To this end, the FDIC proposes to substitute in lieu of its current requirements on quarterly reporting of fully insured brokered deposits and fully insured direct deposits of other depository institutions (§ 304.6 of FDIC's regulations), a new section 304.6 that essentially would require 30 days advance written notification of an insured bank's intent to grow rapidly, i.e., by more than nine percent of assets over any consecutive three-month period. The notification would be filed as part of the bank's Reports of Condition and Income submission by means of a check-off question asking whether the bank intended to grow

rapidly during the following three months. Until and unless such a question is included on the Reports of Condition and Income, a notice of intent to grow rapidly would be given by letter or other written communication directed to the appropriate FDIC regional director for supervison. No special funding plan or arrangement designed to rapidly increase the assets of a bank could be implemented until 30 days following written notice given either through the submission of a Reports of Condition and Income or a separate letter or other written communication. A written notification would also be required within seven days whenever an insured bank increased its assets by more than nine percent during any period unless the growth was pursuant to a previously reported notice of intent to grow rapidly.

The proposed regulation makes clear that the reporting requirements are not intended to cover situations in which the growth threshold is exceeded as a result of normal growth expected of a new bank during its first year of operation (unless pursuant to a special funding plan or arrangement for which notice was not previously given), a merger or consolidation, or seasonal changes in deposit growth or lending and repayment patterns customary for the particular bank.

The FDIC is also soliciting comment on any other possible reporting scheme designed to inform the FDIC in advance of planned rapid growth in a more efficient and less burdensome manner.

Confidential Treatment of Notices

All notices or other information received in accordance with the regulation outside the Reports of Condition and Income will be treated as confidential by the FDIC. It is the agency's opinion based upon a review of relevant case law that such notices or other information will be exempt from required public disclosure under the Freedom of Information Act. The notices or information will contain or constitute confidential commercial or financial information within the meaning of 5 U.S.C. 552(b)(4) and also fall within the parameters of 5 U.S.C. 552(b)(8) which exempts from public disclosure information contained in or related to examination, operating or condition reports prepared for the use of the FDIC or any other agency responsible for the supervision of financial institutions.

Statutory Authority

In order to properly discharge its supervisory responsibilities and to adequately administer and protect the deposit insurance fund, it is essential that the FDIC have accurate, up-to-date information regarding actions taken by insured banks that may pose a threat to bank safety and soundness and/or pose a threat to the insurance fund. The FDIC's purpose in proposing a prior notice requirement before an insured bank may institute any special funding plan and notice otherwise whenever rapid growth occurs is to provide the FDIC with a mechanism to obtain in a timely fashion information that is needed in order that the FDIC may assess the risks posed to the insurance fund, coordinate with other bank regulatory authorities, prepare for and schedule examinations of insured banks when and where they are most needed, and properly evaluate bank management, current and future capital and liquidity needs, etc. in light of plans which may substantially alter the nature of a bank's balance sheet.

The FDIC's action in proposing to amend Part 304 of the FDIC's regulations to provide for such notice is fully consistent with the FDIC's purpose and is authorized by sections 7, 8, 9(Eighth), and 10(b) of the Federal Deposit Insurance Act (12 U.S.C. 1817, 1818, 1819, 1820(b)). Under section 9 of the FDI Act the FDIC has broad general authority to issue regulations "as it may deem necessary to carry out the provisions of the [Federal Deposit Insurance Act] or of any other law which it has the responsibility of administering or enforcing * * *" 12 U.S.C. 1819(Tenth). It is settled that binding legislative-type rules based on general rulemaking authority may be issued so long as the rules are reasonably related to the purposes of the enabling legislation containing the general rulemaking authority. *Mourning v. Family Publications Services*, 411 U.S. 336, 369 (1973) (quoting *Thorpe v. Housing Authority of the City of Durham*, 393 U.S. 269, 280–281 (1969)). The preamble to the legislation placing federal deposit insurance on a permanent basis states that the Banking Act of 1935 was "[t]o provide for the sound, effective, and uninterrupted operation of the banking system . . ." Pub. L. No. 74–305, 49 Stat. 684 (1935). The clear goal of the FDI Act as demonstrated by the express language of the statute and its legislative history is to protect the safety and soundness of insured banks. In order to do so, the FDIC must be fully informed of what actions insured banks plan to take that may present risks to their safety or soundness and may ultimately endanger the deposit insurance fund. The ability of a federal bank regulatory agency to adopt regulations in harmony with safety and soundness concerns based upon general rulemaking authority was judicially recognized long ago, *Continental Bank and Trust Company v. Woodall*, 239 F.2d 707, 710 (10th Cir.), *cert. denied*, 353 U.S. 909 (1957), and recently reaffirmed by the D.C. Circuit in a case involving a challenge to a regulation by another federal insurer of deposits, *Lincoln Savings and Loan Association v. Federal Home Loan Bank Board*, 856 F.2d 1558 (D.C. Cir. 1988).

As the safety and soundness of the deposit insurance fund is inextricably connected with bank safety and soundness, *Federal Deposit Insurance Corporation v. Citizens State Bank*, 130 F.2d 102, 104 n. 6 (8th Cir. 1942) and the FDIC has a congressional mandate to pay insured deposits whenever a bank is closed "on account of inability to meet the demands of its depositors" (12 U.S.C. 1821 (f)), the FDIC must preserve the solvency of the insurance fund in order to fulfill its mandate when called upon. It is not surprising, therefore, that the FDIC's authority to protect the deposit insurance fund by the adoption of substantial regulations applicable to all insured banks has been judicially recognized. *National Council of Savings Institutions v. Federal Deposit Insurance Corporation*, 664 F. Supp. 572 (D.D.C. 1987). Furthermore, the FDIC is authorized under section 8 of the FDI Act (12 U.S.C. 1818) to initiate cease-and-desist proceedings whenever a bank is engaging in an unsafe or unsound banking practice and to terminate deposit insurance whenever a bank is engaging in such practices or is in an unsafe or unsound condition. The FDIC is not confined to initiating individual enforcement or termination actions under section 8 but may, at its discretion, adopt substantive regulations defining what constitutes an unsafe or unsound banking practice and what circumstances will warrant the termination of deposit insurance.

Independent Bankers Association v. Heimann, 613 F. 2d 1161, 1169 (D.C. Cir. 1979), *cert. denied*, 449 U.S. 823 (1980). As the FDIC is authorized to adopt substantive regulations for the purpose of protecting bank safety and soundness and for the prupose of protecting the deposit insurance fund, the FDIC clearly has the authority to adopt regulations simply requiring that the FDIC receive prior notice of a bank's plans to take certain actions that may adversely affect bank safety and soundness and the deposit insurance fund.

Not only does it logically follow from the above that the FDIC may require the reports proposed herein, the FDIC is expressly authorized to do so with respect to insured state nonmember banks. Section 7 of the FDI Act (12 U.S.C. 1817) provides that the FDIC may collect reports of condition "and such other reports as the Board [of Directors] may from time to time require." These reports are necessary in order that, among other things, the FDIC can properly discharge its responsibility under section 10(b) of the FDI Act (12 U.S.C. 1820 (b)) to schedule and undertake a special examination of an insured bank other than a state nonmember bank when the FDIC has reason to believe that such examination is necessary to determine the condition of the bank. It follows, therefore, based on section 9, that the FDIC has the authority to require the reports from insured banks other than state nonmembers in order that it might fulfill its responsibility to undertake such examinations.

Accordingly, for the reasons stated in this notice, and pursuant to the FDIC's authority under sections 7, 8, 9(Eighth), and 10(b) of the Federal Deposit Insurance (12 U.S.C. 1817, 1818, 1819(Eighth), 1820(b)), the FDIC proposes to delete § 304.6 of its regulations (12 CFR 304.6) and substitute in lieu thereof the following new § 304.6.

List of Subjects in 12 CFR Part 304

Banks, banking; Bank reports.

Accordingly, the FDIC hereby proposes to amend Part 304 of Title 12 *Code of Federal Regulations* as follows.

PART 304—FORMS, INSTRUCTIONS, AND REPORTS

1. The authority citation for Part 304 continues to read as follows:

Authority: 5 U.S.C. 552, 12 U.S.C. 1817, 1818, 1819, 1820.

2. It is proposed that § 304.6 be revised to read as follows:

§ 304.6 Notification of rapid growth.

(a) Until and unless a question regarding planned rapid growth is included on the Reports of Condition and Income filed by insured banks, an insured bank may not undertake any special funding plan or arrangement designed to increase its assets by more than nine percent during any consecutive three-month period without first notifying the appropriate FDIC regional director for supervision in writing at least 30 days in advance of the implementation of the special funding plan or arrangement. For purposes of this requirement, a special funding plan or arrangement is any effort to rapidly increase the assets of the bank by any means. Such means may include, for example, borrowings, solicitation and acceptance of deposits from or through the intermediation of brokers or affiliates, solicitation of deposits outside the bank's normal trade area, or paying rates on deposits that are higher than locally competing depository institutions. A notification filed pursuant to this requirement need only state the bank's intention to grow rapidly and shall be considered given on the date post-marked or delivered to the FDIC regional office if by means other than placement in the mails.

(b) In the event a question is included on the Report of Condition and Income asking whether the reporting bank intends to grow rapidly, i.e., grow by more than nine percent during the following three months, the bank would by check-mark indicate affirmatively that it plans to grow rapidly and the submission of its Report of Condition and Income shall satisfy the notification requirement prescribed in paragraph (a) of this section. The bank may not implement its growth plans for 30 days following the date of submission of its Reports of Condition and Income. For this purpose, date of submission means the date on which the Reports were mailed, transmitted electronically or by fax machine to the FDIC or other federal banking authority.

(c) In the event a question concerning rapid growth is included on the Reports of Conditions and Income and an insured bank between filing dates determines to grow rapidly, it may not implement any special funding plan or arrangement designed to achieve rapid growth without first notifying the appropriate FDIC regional director for supervision in writing at least 30 days in advance. The notice need only state the bank's intent to grow rapidly and shall be considered given on the date post-marked or delivered to the FDIC regional office if by means other than placement in the mails.

(d) Unless rapid growth occurs pursuant to a plan or arrangement for which notice was previously given, an insured bank shall notify the appropriate FDIC regional director in writing within seven days whenever its assets increase by more than nine percent during any consecutive three-month period. The notice need only report the fact of that growth and shall be considered given on the date post-marked or delivered to the FDIC regional office if by means other than placement in the mails.

(e) The reporting requirements prescribed in this section are not intended to apply to situations in which the growth threshold of nine percent during any consecutive three-month period is exceeded as a result of normal growth expected of a newly chartered bank during its first year of operation (unless it has implemented a special funding plan or arrangement for which no prior notification has been given), a merger or consolidation, or seasonal changes in deposit growth or lending and repayment patterns that are customary for the particular bank.

(f) Additional information regarding growth plans and activities may be required from time to time through direct inquiry.

By order of the Board of Directors.

Dated at Washington, DC this 21st day of March 1989.

Federal Deposit Insurance Corporation.

Hoyle L. Robinson,

Executive Secretary.

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