

**Andrew C. Hove, Jr.  
Acting Chairman  
Federal Deposit Insurance Corporation  
before the  
Committee on Banking, Housing, and Urban Affairs  
Subcommittee on Financial Services and Technology  
United State Senate  
July 30, 1997**

Good morning, Mr. Chairman and members of the Subcommittee. I appreciate this opportunity to testify before you today on behalf of the Federal Deposit Insurance Corporation regarding Year 2000 issues. Computers and computer systems, particularly systems used in banking and finance, employ dates for a large number of functions. Therefore, the potential for problems related to the inability of computer systems to recognize accurately dates beyond 1999 is a significant concern for the financial services industry and for financial institution regulators.

My detailed written testimony discusses Year 2000 issues as they relate to the banking industry, our current supervisory concerns, and the initiatives underway to ensure that financial institutions will be prepared to meet the needs of their customers in the year 2000 and beyond. It also discusses the FDIC's internal remediation efforts.

I submit that written testimony for the record and I will today briefly discuss how the FDIC is working -- along with the other federal banking agencies -- to minimize the potential harm of Year 2000 problems on financial institutions and their customers.

In March of this year, the FDIC directed its regional supervisory staff to review the Year 2000 plans of all FDIC-supervised institutions by year-end 1997. These reviews are being conducted, in cooperation with the respective state banking authorities, at each scheduled examination. For those institutions not scheduled for examination in 1997, this evaluation will be performed by directly contacting the institution. These reviews will be used to identify those financial institutions that need increased supervisory attention.

Since March, the FDIC and state banking authorities have conducted Year 2000 reviews for approximately 2,081 FDIC-supervised financial institutions and 44 third-party computer service providers and software vendors. These numbers represent roughly one-third of all FDIC-supervised financial institutions and servicers. The results indicate that institutions are generally aware of the Year 2000 problem. However, senior management and outside directors usually do not possess in-depth technical knowledge and, as a result, may not have the same appreciation of the risks posed by Year 2000 noncompliance that would be expected in larger, more sophisticated data centers. Examiners have noted the potential for credit quality exposure from corporate borrowers that have not taken steps to solve their own Year 2000 problems. In addition, the reviews to date have identified instances where institutions have failed to recognize potential problems with personal computers and environmental control systems.

Supervisory action will be taken, including enforcement action when warranted, if an institution is not giving this issue the attention it deserves.

The large majority of FDIC-supervised institutions either use third-party servicers for data processing or use purchased software packages on their in-house systems. These institutions must rely on the servicers or vendors to take the necessary steps to make their software Year 2000 compliant. The FDIC's reviews indicate that while most of these systems are not yet Year 2000 compliant, vendors and servicers are working to address the problem.

Because banks rely so heavily on third-party services, the FDIC is working closely with the other federal banking agencies to separately assess the efforts of data processing servicers and software providers in resolving Year 2000 problems. The agencies are currently performing preliminary assessments at each of the 275 data processing servicers that serve financial institutions including the 15 large multiregional data processing servicers that have been identified by the agencies as posing a systemic risk to the financial industry should one or more fail. With respect to software providers, the agencies are performing a similar assessment of the 12 major software products used by a wide segment of financial institutions. We estimate that these twelve packages are used by 75 percent of the FDIC-supervised financial institutions that purchase software applications for their data processing.

This assessment will also include each FDIC-supervised financial institution with total assets greater than \$1 billion, and financial institutions where in-house programming is performed or where the financial institution provides data processing services to other financial institutions. Most of these initial assessments should be finished by the end of the August, with more in-depth reviews to be completed by the federal regulators by June of 1998. The agencies plan to notify the serviced banks when their third party servicer has not taken sufficient action to achieve Year 2000 compliance. We will expect the affected bank to give us clear commitments and specific timetables for remedial action. The results of both the assessments and the reviews will be shared among the banking agencies. In cases where satisfactory responses are not forthcoming, the agencies will coordinate supervisory action, including enforcement action if necessary, to ensure that Year 2000 issues are adequately addressed.

In closing, Mr. Chairman and members of the subcommittee, I want to stress that, while it is too early for the FDIC to predict whether any institution may fail as a result of Year 2000 problems, we will be ready to intervene should an institution's viability be threatened by its inability to maintain accurate books and records. To be prepared for the possibility of failures, we will analyze how the FDIC's traditional resolution and receivership methods would be affected by this type of problem.

Regardless of the difficulties financial institutions may encounter, each depositor will remain fully insured up to the \$100,000 limit. Maintaining consumer confidence in the U.S. banking system will be the primary goal in our planning process.

I will be happy to answer any questions.