

that the Board retain the existing assessment rate schedule for the second semiannual assessment period of 1995 so that recapitalization is accomplished as soon as possible. The SAIF had an estimated balance of \$1.8 billion (unaudited) at year-end 1994, and SAIF assumes resolution responsibility from the RTC on July 1, 1995. Although estimated failed-institution assets appear manageable for 1995 and 1996, the SAIF remains vulnerable in the short run to a single large-institution failure and to any significant increase in anticipated loss rates.

## VI. Request for Public Comment

Based upon the results of its semiannual review of the recapitalization of the SAIF and of the SAIF assessment rates, the FDIC is inclined to retain the existing assessment rate schedule applicable to SAIF-member institutions. The FDIC wishes to have the benefit of public comment before ending its review for this period, however. The FDIC therefore requests comment as to whether it is appropriate for the FDIC to retain the existing assessment rate schedule applicable to SAIF-members, or whether the rates should be lowered to the statutory minimum of 18 basis points or some point in between. The FDIC is interested in receiving analyses exploring the impact a differential between BIF and SAIF premiums might have on SAIF members, and the FDIC invites comment as to whether the current spread of 8 basis points from the lowest to the highest assessment rates should be retained for SAIF members. The FDIC solicits comment as to how lower SAIF rates would impact current efforts to recapitalize the SAIF. The FDIC further invites comments as to whether current rates are sufficient to recapitalize the SAIF in an expeditious manner.

## VII. Paperwork Reduction Act

No collection of information pursuant to section 3504(h) of the Paperwork Reduction Act of 1980 (44 U.S.C. 3501 *et seq.*) are contained in this proposed rule. Consequently, no information has been submitted to the Office of Management and Budget (OMB) for review.

## VIII. Regulatory Flexibility Analysis

The Board hereby certifies that the proposed rule would not have a significant economic impact on a substantial number of small entities within the meaning of the Regulatory Flexibility Act (5 U.S.C. 601, *et seq.*). This proposed rule will not necessitate the development of sophisticated

recordkeeping or reporting systems by small institutions nor will small institutions need to seek out the expertise of specialized accountants, lawyers, or managers to comply with this proposed rule. Therefore, the provisions of that Act regarding an initial and final regulatory flexibility analysis (Id. at 603 and 604) do not apply here.

## List of Subjects in 12 CFR Part 327

Assessments, Bank deposit insurance, Banks, Banking, Financing Corporation, Savings associations.

For the reasons set forth in the preamble, the Board of Directors of the Federal Deposit Insurance Corporation proposes to amend part 327 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, 1441b, 1817–1819.

2. Paragraph (c)(1) of § 327.9 as added at 59 FR 67165, effective April 1, 1995, will be retained without change. The text of paragraph (c)(1) is republished for the convenience of the reader to read as follows:

### § 327.9 Assessment rate schedules.

\* \* \* \* \*

(c) *SAIF members.* (1) Subject to § 327.4(c), the annual assessment rate for each SAIF member shall be the rate designated in the following schedule applicable to the assessment risk classification assigned by the Corporation under § 327.4(a) to that SAIF member (the schedule utilizes the group and subgroup designations specified in § 327.4(a)):

### SCHEDULE

Capital group	Supervisory subgroup		
	A	B	C
1 .....	23	26	29
2 .....	26	29	30
3 .....	29	30	31

\* \* \* \* \*

By the order of the Board of Directors.

Dated at Washington, D.C., this 31 day of January, 1995.

Federal Deposit Insurance Corporation.

**Robert E. Feldman,**

*Acting Executive Secretary.*

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## FEDERAL DEPOSIT INSURANCE CORPORATION

### 12 CFR Part 327

RIN 3064–AB58

### Assessments; New Assessment Rate Schedule for BIF Member Institutions

**AGENCY:** Federal Deposit Insurance Corporation.

**ACTION:** Proposed Rule.

**SUMMARY:** The Board of Directors (Board) of the Federal Deposit Insurance Corporation (FDIC) is proposing to amend its regulation on assessments to establish a new assessment rate schedule of 4–31 basis points for members of the Bank Insurance Fund (BIF) to apply to the semiannual period in which the reserve ratio of the BIF reaches the designated reserve ratio (DRR) of 1.25% of total estimated insured deposits and to semiannual periods thereafter. The Board is further proposing to amend the assessment risk classification framework to widen the existing assessment rate spread from 8 basis points to 27 basis points.

When the DRR is achieved, the Board is required to set rates to maintain the reserve ratio at the DRR. Based on current projections, the reserve ratio is expected to reach the DRR between May 1 and July 31, 1995. Therefore, the Board is proposing to lower assessment rates to maintain the reserve ratio at the DRR and to maintain a risk-based assessment system. The Board is further proposing to amend the assessments regulation to establish a procedure for adjusting the proposed rate schedule semiannually as necessary to maintain the DRR at 1.25%.

**DATES:** Written comments must be received by the FDIC on or before April 17, 1995.

**ADDRESSES:** Written comments shall be addressed to the Office of the Executive Secretary, Federal Deposit Insurance Corporation, 550 17th Street NW., Washington, DC 20429. Comments may be hand-delivered to room F–400, 1776 F Street NW., Washington, DC 20429, on business days between 8:30 a.m. and 5 p.m. (FAX number: (202) 898–3838). Comments will be available for inspection in room 7118, 550 17th Street, NW., Washington, DC, between 9 a.m. and 4:30 p.m. on business days.

**FOR FURTHER INFORMATION CONTACT:** Christine Blair, Financial Economist, Division of Research (202) 898–3936; or Connie Brindle, Chief, Assessment Operations Section, Division of Finance, (703) 516–5553; or Lisa Stanley, Senior Counsel, Legal Division (202) 898–7494;

or Cristeena Naser, Attorney, Legal Division (202) 898-3587, Federal Deposit Insurance Corporation, Washington, D.C. 20429.

#### SUPPLEMENTARY INFORMATION:

### I. Background

At present, BIF members are assessed rates for FDIC insurance ranging from 23 basis points for the best risk classification to 31 basis points for the riskiest classification. This assessment schedule is based on the requirements of section 7(b)(2)(E) of the Federal Deposit Insurance Act (FDI Act), 12 U.S.C. 1817(b)(2)(E). That provision was enacted as part of section 302 of the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA) (Pub. L. 102-242, 105 Stat. 2236, 2345) which completely revised the assessment provisions of the FDI Act by requiring the FDIC to: (1) establish a system of risk-based assessments; (2) establish rates sufficient to provide revenue at least equivalent to that generated by an annual 23 basis point rate until the BIF reserve ratio achieves the DRR of 1.25% of total estimated insured deposits; (3) when the reserve ratio remains below the DRR of 1.25%, set rates to achieve that ratio within one year or establish a recapitalization schedule to do so within 15 years; and (4) once the DRR is achieved, set rates to maintain the reserve ratio at the DRR.

Based on the financial condition of the BIF, the Board has established two recapitalization schedules, most recently on May 25, 1993, which estimated that the DRR would be achieved in the year 2002. 58 FR 31150 (May 25, 1993). Once the DRR has been attained, the recapitalization schedule will no longer apply. Due to the health of the banking industry, current projections indicate that the BIF will recapitalize sometime between May 1 and July 31, 1995. Accordingly, the Board must implement the statutory provisions which will apply once the DRR is reached. In particular, because the mandate to collect at a minimum average rate of 23 basis points will no longer be operative, the Board must determine when and how much to lower assessments of BIF members.

Following is a discussion of the statutory provisions which must be considered in determining how and when rates may be set, a proposed new assessment rate schedule, a method for applying the proposed rate in the semiannual period during which the DRR is achieved, and a process for adjusting that assessment schedule in future semiannual periods.

### II. Statutory Framework for Setting Assessment Rates

#### A. Summary

Section 7(b) of the FDI Act governs the Board's authority for setting assessment rates for members of the BIF. 12 U.S.C. 1817(b). The assessment rates the Board is authorized or required to set are dependent on whether the fund's reserve ratio has reached its DRR. The reserve ratio is the dollar amount of the BIF fund balance divided by the estimated insured deposits of BIF members. The Board must set semiannual assessments and the DRR for the BIF and the Savings Association Insurance Fund (SAIF) independently. FDI Act, section 7(b)(2)(B).

The DRR for the BIF currently is 1.25% of estimated insured deposits (i.e., \$1.25 for each \$100 of insured deposits), the minimum level permitted by the FDI Act. FDI Act, section 7(b)(2)(A)(iv). The Board may increase the DRR to such higher percentage as the Board determines to be justified for a particular year by circumstances raising a significant risk of substantial future losses to the fund. However, the Board is not authorized to decrease the DRR below 1.25%. *Id.*

Section 7(b), among other things, directs the Board to:

(1) establish a risk-based assessment system whereby an institution's assessment is based in part on the probability that the deposit insurance fund will incur a loss with respect to that institution [FDI Act, section 7(b)(1)(C)(i)]; and

(2) set assessments, not less than \$2000 annually per BIF member, to "maintain" the reserve ratio "at" 1.25% when that ratio has been achieved [FDI Act, section 7(b)(2)(A)(i)(I), (iii)].

In the current economic environment, because of investment income alone, the reserve ratio may continue to grow beyond 1.25%. Moreover, a risk-based assessment system contemplates a range of rates such that even if the least risky institutions pay the lowest rate consistent with a meaningful risk-based assessment system, riskier institutions must pay a higher rate. While the Board must set rates to maintain fund reserves at the 1.25% DRR once that level is achieved, even with assessment rates as low as prudently possible the fund could continue to grow as a result of assessments paid by riskier institutions and investment income. The following sections address these statutory directives.

#### B. Directive: Set Rates To Maintain the Reserve Ratio at the DRR

Pursuant to section 7(b)(2)(A)(i) of the FDI Act, the Board must set semiannual assessments to maintain the reserve ratio of the BIF at the DRR taking into consideration the following factors: (1) Expected operating expenses; (2) case resolution expenditures and income; (3) the effect of assessments on members' earnings and capital; and (4) any other factors the Board may deem appropriate. Section 7(b)(2)(A)(iii) limits the Board's discretion to set assessment rates by imposing a minimum semiannual assessment of \$1,000 per BIF member. The directive to "set rates to maintain the reserve ratio at the designated reserve ratio" was enacted as part of the amendments to section 7 made by the FDIC Assessment Rate Act of 1990 (Assessment Rate Act). Public Law 101-508, 104 Stat. 1388, 1388-14. The Assessment Rate Act is Subtitle A of Title II of the Omnibus Budget Reconciliation Act of 1990. While the phrase "set assessments \* \* \* to maintain the reserve ratio at the designated reserve ratio" is not defined in the statute, the legislative history discussed below illuminates Congress' intentions.

1. Interpretations of "maintain \* \* \* at the DRR".

The Board is of the opinion that this phrase establishes the DRR as a target, a position supported both by the difficulty of managing the size of the reserve ratio as well as the statutory history. Changes in the reserve ratio are a function of the size of estimated insured deposits, investment earnings, assessment revenue (which, in turn, is a function of the risk profile of the industry and revenue received from the statutory minimum assessment), and revenue from corporate-owned and other assets, none of which is in the complete control of the FDIC. In addition, operating expenses and insurance losses to the fund will vary.

The primary factors affecting the fund balance are assessment revenues, investment income, operating expenses and insurance losses resulting from bank failures. Assessment revenues depend upon deposit growth, and investment income depends upon interest rate movements as well as factors affecting the fund's investable balance. Deposit growth and interest rate movements in turn are related, but as the number and variety of financial instruments and financial management techniques expand that relationship becomes less predictable. Both deposit growth and interest rates have become more variable and, thus, less predictable

in recent years. Finally, bank failures and the resulting losses for the insurance fund historically have represented a major source of uncertainty in forecasting the fund balance. Failures can arise from developments in the global marketplace, smaller geographic markets, or specific product markets, and the failure rate is affected by numerous other factors. The 1980s offer strong evidence that changes in these determinants and their implications cannot, as a rule, be anticipated far in advance. The specific timing of failures is particularly difficult to project, even for short forecast horizons. Taken together, the above considerations indicate that the reserve ratio cannot be managed with sufficient precision to achieve a precise target consistently.

Section 208 of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) amended section 7(b) of the FDI Act to establish a DRR and set the level at 1.25%. Public Law 101-73, 103 Stat. 183, 206. Prior to FIRREA, beginning in 1980, the FDI Act required or authorized the Board to adjust the amount of assessment income transferred to the insurance fund, and thereby to increase or decrease the rebate amount, based on the actual reserve ratio of the fund within a range from 1.10 percent to 1.40 percent, with 1.25 percent as the target. See discussion *infra*, Rebates.

FIRREA also prescribed minimum annual assessment rates which could be increased from the scheduled levels, "if necessary to restore the fund's ratio of reserves to insured deposits to its *target level* within a reasonable period of time." [Emphasis added.] H.R. Conf. Rep. No. 222, 101st Cong., 1st Sess. 396 (1989). Thus, when the DRR was established, Congress appears to have considered the DRR as a target level.

The view that the DRR is a target finds further support in Senate legislation which was considered when enacting the Assessment Rate Act. Section 1(a) of S. 3045, which was sponsored by then Senate Banking Committee Chairman Riegle and other members of the Senate Banking Committee, required the Board to "maintain the reserve ratio at a level equal to the designated reserve ratio". This language was almost identical to the comparable provision of S. 3093, the Administration bill, which ultimately was enacted. The section-by-section analysis of S. 3045 describes Section 1(a) as permitting

\* \* \* the FDIC to set the assessment rate at the level the FDIC determines to be appropriate: to maintain the Bank Insurance Fund's reserves at the target level (now \$1.25 in reserves for each \$100 in insured deposits,

with the FDIC having the discretion under the current law to increase it to \$1.50); or if the Fund's reserves are below the target level, to restore the reserves to the target level. The FDIC would have 'a reasonable period of time' to restore the Fund's reserves to the target level. [Emphasis added.]

The Senate banking committee clearly considered the DRR as a target.

Finally, FDICIA section 104, Recapitalizing the Bank Insurance Fund, amended the assessment rate provisions of section 7(b)(1)(C) (in effect December 19, 1991 through December 31, 1993) as follows:

If the reserve ratio of the Bank Insurance Fund *equals or exceeds* the fund's designated reserve ratio under subparagraph (B), the Board of Directors shall set semiannual assessment rates for members of that fund as appropriate to maintain the reserve ratio at the designated reserve ratio. [Emphasis added.]

Thus Congress appears to have recognized that the reserve ratio would fluctuate around a target DRR.

Treating the DRR as a target would necessarily include the concept of fluctuations above and below the target, thus incorporating into the rate-setting process a measure of economic reality. If the reserve ratio falls below 1.25% in a semiannual period, the Board could adjust the assessment schedule in the next semiannual period to restore the ratio. Section 7(b)(3)(A) of the FDI Act contemplates precisely that. That section provides that, after the DRR is achieved, if the reserve ratio falls below the DRR, the Board is required to set semiannual assessments sufficient to increase the reserve ratio to the DRR within one year or in accordance with a recapitalization schedule promulgated to restore the reserve ratio to the DRR within 15 years. Conversely, when the reserve ratio rises above the DRR for any semiannual period, the Board could adjust the assessment schedule downward to reflect the increase.

Current projections show, however, that even if the assessment rate for risk classification 1A banks were as low as possible consistent with a meaningful risk-based assessment system, the fund may continue to grow as a result of the revenue from investment income. In such a case where the rates are set as low as possible consistent with a risk-based assessment system and the fund nevertheless continues to grow, the Board considers that it will have complied with the statute because the Board will have *set rates* to maintain the reserve ratio at 1.25% in accordance with statutory requirements for a risk-based assessment system.

Congress could not have understood that the reserve ratio can be maintained

precisely at 1.25%. Under this interpretation, amounts in excess of that fixed point should be returned to the industry. However, as discussed above, the FDIC cannot completely control the factors that produce fluctuations in the level of the reserve ratio. Therefore, management of the reserve ratio is necessarily imprecise. In the current economic situation, the fund will likely grow beyond the DRR as a result of investment income alone. Thus, an interpretation which requires the FDIC to maintain the reserve ratio precisely at 1.25% would necessarily require a mechanism for providing assessment credits (known as rebates) to BIF members for amounts in excess of 1.25%. Putting aside issues of whether investment income, reserve corpus or both can be rebated, more importantly, the FDIC's authority in section 7(d), 12 U.S.C. 1817(d), to provide assessment credits was deleted in FDICIA as being obsolete. See, section-by-section analysis of section 212(e)(3) of S. 543 which became the language of section 302(a) of FDICIA at 138 *Cong. Rec.* S2073 (daily ed. February 21, 1992). See discussion *infra*, Rebates.

The Board believes that viewing the DRR as a target is the correct position because (1) it reflects economic reality and the impossibility of maintaining the reserve ratio precisely at 1.25%; (2) it gives effect to other relevant requirements in the statute for a minimum assessment, a risk-based assessment system, and maintenance of the DRR; and (3) it better comports with Congressional intent as indicated by the legislative history and the fact that Congress eliminated the rebate authority of section 7(d).

2. BIF Members shall pay a minimum semiannual assessment of \$1,000.

Section 302 of FDICIA completely revised section 7(b) of the FDI Act. The minimum assessment language was modified only to reflect the fact that rates are to apply semiannually and to combine separate provisions into a single provision applicable to both the BIF and SAIF as follows:

The semiannual assessment for each member of a deposit insurance fund shall be not less than \$1,000. FDI Act, section 7(b)(2)(A)(iii).

After FDICIA, BIF members must pay the greater of their risk-based rate or \$2000 each year.

### C. The FDIC Shall Establish a Risk-Based Assessment System

In FDICIA, Congress completely restructured the basis upon which assessment rates are determined. Section 302(a) of FDICIA required the

FDIC to establish by January 1, 1994, a risk-based assessment system based on:

(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;

(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.

Within the scope of these broad factors, FDIC was granted complete discretion to design a risk-based assessment system. See, *i.e.*, S. Rep. No. 167, 102d Cong., 1st Sess., 57 (1991). One statutory restraint, however, is that the system must be designed so that as long as the BIF reserve ratio *remains* below the DRR, the total amount raised by semiannual assessments on members cannot be less than the total amount resulting from a flat rate of 23 basis points. FDI Act, section 7(b)(2)(E). This provision currently applies, but will cease to be operative when the BIF meets the DRR. This provision may again become operative if the reserve ratio *remains* below the DRR at some future time. The Board interprets the minimum assessment provision of section 7(b)(2)(E), which requires weighted average assessments of 23 basis points, as applying only when the reserve ratio *remains* below the DRR for at least a year.

Any time the reserve ratio goes below the DRR, the Board must either set rates 1) to restore the reserve ratio within one year or 2) in accordance with a recapitalization schedule not to exceed fifteen years. FDI Act, section 7(b)(3)(A). Because the Board has the discretion to determine the rate necessary to restore the reserve ratio to the DRR within one year, it is reasonable to conclude that the minimum assessment provision (which mandates the Board to set rates sufficient to provide revenue equivalent to that generated by an annual flat rate of .0023) would not apply until the reserve ratio stays below the DRR for at least one year. Moreover, it is unlikely that Congress intended such a drastic result if the DRR falls slightly below the target DRR, when a small adjustment in the assessment schedule for the following semiannual period could bring the fund back up to the DRR. In such a case, if the minimum assessment provision applied, the result would be

an enormous overcollection of assessment revenue which, as explained below, the FDIC lacks the authority to rebate.

#### D. Rebates

It appears, based on the statutory framework and legislative history of section 7 of the FDI Act, that the FDIC has not had authority to provide rebates since the permanent risk-based assessment system took effect on January 1, 1994. Prior to FDICIA, two provisions of section 7 expressly addressed rebates or assessment credits, section 7(d), Assessment Credits, and section 7(e), Refunds to Insured Depository Institutions.

In section 302(e)(3) of FDICIA, Congress removed the assessment credit provisions of section 7(d) of the FDI Act and at the same time established a rate-setting scheme requiring the Board to set rates to maintain the reserve ratio at the DRR. Pub. L. 102-242, 105 Stat. 2236, 2349. As is clear from the statutory history of assessment credits, such credits were intended as a means to provide flexibility to keep the fund balance from growing too large at a time when assessment rates were set in the statute and all institutions paid the same flat rate. See generally, S. Rep. No. 1269, 81st Cong., 2nd Sess. 1-2 (1950); *Cong. Rec.* H10648 *et seq.* (daily ed. July 19, 1950) (statement of Mr. McCormack); Federal Deposit Insurance Corporation, *The First Fifty Years* at 58-60, Wash., D.C. 1984. Because of the large number of bank failures in the mid-to-late 1980s, Congress gradually provided the FDIC with greater flexibility to determine the timing and amount of assessment rates. This culminated in the requirement in FDICIA that the FDIC implement a risk-based assessment system. FDICIA also provided the FDIC with the flexibility, after the DRR was reached, to set assessment rates to maintain the DRR.

#### 1. Statutory History of Section 7(d)

Section 7(d), 12 U.S.C. 1817(d), was enacted in the FDI Act in 1950. Public Law 797, Ch. 967, 64 Stat. 873. At that time all banks paid a flat assessment rate of 0.83 percent. Due to favorable economic circumstances, the fund had built up excess reserves, but the FDIC lacked the authority to return the excess funds to the industry. Congress adopted an assessment credit formula to credit to insured banks 60 percent of the fund's net assessment income and to transfer the remaining 40 percent to the Corporation's surplus (Permanent Insurance Fund). "The committee desires to emphasize that the formula thus provides a flexible method for

granting a reduction in the assessments paid by banks in normal years, and in bad years provides for payment of the full assessment if needed. This should reasonably protect the insurance fund in years of extraordinary losses." H. Rep. No. 2564, 81st Cong. 2nd Sess. (1950) reprinted in 1950 U.S.C.C.S. 3770. This formula returned net assessment revenues only; it did not extend to investment income.

The percentage of net assessment income rebated to insured banks was modified from time to time as warranted given the constraints of a statutory flat assessment rate system. In the Consumer Checking Account Equity Act of 1980, enacted as part of the Depository Institutions Deregulation and Monetary Control Act of 1980, Public Law 96-221, 94 Stat. 132, Congress tied the amount of the rebate to the status of the reserve ratio. If the reserve ratio was less than 1.10%, the amount transferred to the Corporation's capital account was required to be increased to an amount (not to exceed 50% of net assessment income) that would restore the ratio to at least 1.10%. If the reserve ratio exceeded 1.25%, the amount transferred to the capital account could be reduced by such amount that would keep the reserve ratio at not less than 1.25%; finally, if the reserve ratio exceeded 1.40%, the amount transferred to the capital account was required to be increased such that the reserve ratio would be not more than 1.40%. *Id.* at section 308(d).

In section 208 of FIRREA, Congress specified certain flat annual assessment rates to be in effect through 1991, but provided the FDIC with authority to increase those rates as needed to protect the BIF and to raise the DRR from 1.25% to a maximum of 1.50% as justified by circumstances raising a significant risk of substantial future losses. In the event the Board increased the DRR above 1.25%, it was required to establish supplemental reserves for that increased revenue, the income from which was to be distributed annually to BIF members through an Earnings Participation Account. (This was the first time Congress provided any mechanism for returning to the industry any investment income.) In addition, to the extent the supplemental reserves were not needed to satisfy the next year's projected DRR, those amounts were to be rebated. FIRREA, section 208(4). Congress also barred any assessment credits until the DRR was achieved. When forecasts indicated the DRR would be achieved in the following year, the Board was required to provide assessment credits for that following year equal to the lesser of: (1) the amount necessary to

reduce the BIF reserve ratio to the DRR; or (2) 100 percent of the net assessment income to be received in that following year. *Id.*

In sections 2002 and 2003 of the Assessment Rate Act, Congress provided the FDIC with greater flexibility in both the timing and amount of assessment rates. It also eliminated the requirement that the investment income on the supplemental reserves be distributed annually to BIF members. Assessment Rate Act, section 2004. Because the Board did not increase the DRR above 1.25%, the provision authorizing Earnings Participation Accounts and supplemental reserves never became effective.

In FDICIA, Congress provided for establishment of a risk-based assessment system that, after the DRR was achieved, would provide the FDIC with much greater flexibility to set assessment rates. In 1990, Congress had already provided the FDIC with the authority to adjust assessment rates upward to ensure that the BIF received sufficient revenue. In FDICIA, Congress intended that same rate adjustment authority to operate in lieu of providing assessment credits in the event that the established rates resulted in collection of excess assessment revenue. Therefore, Congress eliminated the assessment credit provisions of section 7(d) in their entirety as being obsolete because the ability to adjust rates would take the place of a rebate mechanism.

The discussion of section 212(e)(3) in the Senate Report on S. 543 (which became the language of section 302(a) of FDICIA) describes Congress' intent:

Section 212(e)(3) replaces current section 7(d) with a new section 7(d) recodifying current section 7(b)(9). The deleted text, providing for assessment credits to insured depository institutions when deposit insurance fund reserve ratios exceed designated reserve ratios, is obsolete in light of the standards for establishing assessments set forth in new section 7(b)(2)(A)(i) [setting rates to maintain at the DRR]. Under section 7(b)(2)(A)(i), funds that, under current section 7(d), would have been rebated to insured depository institutions through assessment credits will now be rebated through reduced assessments.

138 Cong. Rec. S2073 (daily ed. Feb. 21, 1992).

This position finds further support in the language of section 104 of FDICIA (in effect December 19, 1991 through December 31, 1993) which required the Board to set rates to maintain the reserve ratio at the DRR when the reserve ratio equals or exceeds 1.25%. FDICIA, section 104(a) amending section 7(b)(1)(C) of the FDI Act. Clearly, Congress contemplated a

situation in which the reserve ratio would rise above the DRR, but nonetheless eliminated rebate authority. Thus, Congress appears to have intended the rate setting process to be the appropriate mechanism for adjustment.

## 2. Section 7(e) Does Not Provide Rebate Authority

An argument has been raised that section 7(e), 12 U.S.C. 1817(e), authorizes the FDIC to provide rebates of fund assets to keep the reserve ratio at 1.25%. Section 7(e) was enacted in 1950 in the Federal Deposit Insurance Act, along with section 7(d), assessment credits. Section 7(e) has been amended only once—in FIRREA, by changing “insured bank” to “insured depository institution”.

Section 7(e) provides that the FDIC:

(1) may refund to an insured depository institution any payment of assessment in excess of the amount due to the Corporation or (2) may credit such excess toward the payment of the assessment next becoming due from such bank and upon succeeding assessments until the credit is exhausted.

By its terms, the statutory language contemplates that such refunds or credits are to be made in respect of overpayments. The report accompanying the legislation describes section 7(e) as “expressly authoriz[ing] the Corporation to refund any overpayments of assessments or to credit such overpayments on future assessments”. H. Rep. No. 2564, 81st Cong., 2d Sess. (1950), reprinted in 1950 U.S.C.C.S. 3771. Because section 7(d) contained express authority to provide rebates, Congress appears to have intended in section 7(e) to provide the FDIC with alternative methods (refunds or credits) to correct computational errors or other forms of overpayments outside of the rebate context so that the FDIC could return funds which clearly did not belong to it.

Because section 7(d) providing assessment credits was adopted as part of the same legislation, an interpretation that section 7(e) also provides the same authority would mean that the provisions were redundant. Rather, each provision has independent meaning and purpose if section 7(d) is interpreted to provide the substantive authority to provide rebates, while section 7(e) grants the FDIC the discretion to choose the method of refunding overpayments, i.e., by either providing an assessment credit or a refund check. Moreover, section 7(e) has never been interpreted as providing rebate authority precisely because until January 1, 1994 when the statutory risk-based assessment system

became effective, that authority existed in section 7(d). Given the intent of the drafters as expressed in the section-by-section analysis of S. 543, that rebates will be provided through reduced assessment rates, an interpretation that section 7(e) provides rebate authority outside its historical context would seem to be contrary to Congressional intent.

In sum, the Board believes that the better interpretation of the statute is that the FDIC has no authority to grant rebates and that to do so would be in violation of the statute and contrary to the legislative history. As discussed above, this position is based on:

(1) the statutory history of sections 7(d) and (e); 2) the fact that Congress deleted the rebate authority in section 7(d); and (3) the legislative history indicating that Congress intended that lower rates would be the substitute for rebates.

## III. Proposed Assessment Rate Schedule

The Board proposes to set a new assessment rate schedule with a spread of 4 to 31 basis points (see Table 1). The Board further proposes to make adjustments to this schedule by an adjustment factor not to exceed 5 basis points.

The following definitions are used in the proposal:

**Assessment Schedule:** A set of rates based on the risk classification matrix with a spread of 27 basis points between the minimum rate which would apply to institutions classified as 1A and the maximum rate which would apply to institutions classified as 3C.

**Spread:** The difference between the minimum and maximum rate in any given assessment schedule.

**Adjustment Factor:** The maximum number of basis points or a fraction thereof by which the Board would be authorized to increase or decrease the proposed 4–31 basis point assessment schedule without going through the rulemaking process.

### A. Statutory Factors

As discussed in Section II, pursuant to sections 7(b)(1) and 7(b)(2)(A)(ii), the Board is required to take into consideration the following factors when setting risk-based assessments: the probability of loss, the amount of such loss, expected operating expenses, case resolution expenditures and income, the effect of assessments on members' earnings and capital, and any other factors that the Board may deem appropriate. These factors are discussed below.

### 1. Risk-Based Assessment Schedule

The fundamental goals of risk-based assessment rates are to reflect the risk posed to the insurance fund by insured institutions and to provide institutions with incentives to control risk taking. The maximum rate spread in the existing assessment rate matrix (see Table 1) is 8 basis points. Institutions rated 1A pay an annual rate of 23 basis points while institutions rated 3C pay 31 basis points. A concern is whether 8 basis points represents a sufficient spread for achieving these goals.

In the FDIC's proposal for the current risk-based premium system, the Board sought comment on whether the assessment rate spread embodied in the existing system, *i.e.*, 8 basis points, should be widened. Of the 96 commenters addressing this issue, 75 favored a wider rate spread. In the final rule, the Board expressed its conviction that widening the rate spread was desirable in principle, but chose to retain the proposed rate spread. The Board expressed concern that widening the rate spread while keeping assessment revenue constant, might unduly burden the weaker institutions which would be subject to greatly increased rates. However, the Board retained the right to revisit the issue at some future date. 58 FR 34357 (June 25, 1993).

The current assessment rate spread for BIF institutions has been criticized widely by bankers, banking scholars and regulators as overly narrow, and there is considerable empirical support for this criticism. Using a variety of methodologies and different sample periods, the vast majority of relevant studies of deposit insurance pricing have produced results that are consistent with the conclusion that the rate spread between healthy and troubled institutions should exceed 8 basis points.<sup>1</sup> While the precise estimates vary, there is a clear consensus from this evidence that the rate spread should be widened.

FDIC research likewise suggests that a substantially larger spread would be

necessary to establish an "actuarially fair" assessment rate system. Insurance premiums are actuarially fair when the discounted value of the premiums paid over the life of the insurance contract is expected to generate revenues that equal expected discounted costs to the insurer from claims made by the insured over the same period. A 1994 FDIC study used a "proportional hazards" model to estimate the expected lifetime of banks that were in existence as of January 1, 1993. The study estimated the actuarially fair premium that each bank must pay annually so that the cost of each bank failure to the FDIC would equal the revenue collected through insurance assessments. The estimates indicated a rate spread for 1A versus 3C institutions on the order of magnitude of 100 basis points.<sup>2</sup>

The Board is concerned also that rate differences between adjacent cells in the current matrix do not provide adequate incentives for institutions to improve their condition. Larger differences are consistent with historical variations in failure rates across cells of the matrix, viewed in connection with the preponderance of evidence regarding actuarially fair premiums.<sup>3</sup> The precise magnitude of the differences is open to debate, given the sensitivity of any estimates to small changes in assumptions and to selection of the sample period. However, the Board believes that larger rate differences between adjacent cells of the matrix are warranted.

The Board believes that the assessment rate matrix should be adjusted in the direction of an actuarially fair rate structure, as described above. Consistent with the results of the relevant studies on this topic, regardless of the sample period selected, the Board believes at this time that the highest-rated institutions pose a small but positive risk to the insurance fund and that the spread between the highest- and lowest-rated institutions should be widened.

The Board does not wish to adopt major changes in the assessment rate structure at this time. The proposed rate matrix retains the nine-cell structure. As noted above, in the final rule adopting the current assessment rate schedule, the Board expressed its conviction that

widening the rate spread was desirable but declined to do so because of the potential hardship for troubled institutions and possible additional losses for the insurance fund. The Board remains unwilling to increase the maximum rate other than by means of the adjustment factor discussed below, without further study regarding the proper insurance pricing structure for the industry.

Accordingly, FDIC staff currently are undertaking a comprehensive reevaluation of the risk-based assessment rate matrix, and will present recommendations to the Board in the near future. Any proposed changes to the risk-based assessment rate structure that may result from this process will be addressed in a separate future notice of proposed rulemaking.

In the interim, the Board believes that the proposed assessment schedule represents an equitable set of rate adjustments. It widens the rate spread between the lowest- and highest-rated institutions, consistent with the implications of the best empirical evidence on this issue and with the Board's previously stated conviction. Moreover, the rate differences between adjacent cells in the matrix are widened, providing additional incentive for weaker institutions to improve their condition and for all institutions to avoid excessive risk-taking. This is consistent with the Board's desire to create adequate incentives via the assessment rate structure to encourage behavior that will protect the deposit insurance fund against excessive losses.

### 2. Expected Operating Expenses and Case Resolution Expenses and Income

Operating expenses are projected to be approximately \$260 million for the second half of 1995 (See Table 2). Case resolution expenditures or "insurance losses" for the second half of 1995 are projected to be \$130 million. If the 1994 loss experience of \$70 million per semiannual period (estimated) continues in 1995, losses may be lower than the projected amount. Insurance losses in 1994 were less than one-quarter of the historical average, relative to insured deposits, and baseline assumptions indicate that losses will begin to revert toward the norm in 1996 (see Tables 2-4). See additional discussion of loss assumptions in Section III.B, below.

### 3. Impact on Earnings and Capital

Because assessment rates for most BIF members will decline, the impact on earnings and capital will be positive. Lower assessment costs will reduce expenses by approximately \$4.6 billion

<sup>1</sup> For a representative sampling of academic studies on this issue, see Estimating the Value of Federal Deposit Insurance, The Office of Economic Analysis, Securities and Exchange Commission (1991); Berry K. Wilson, and Gerald R. Hanweck, A Solvency Approach to Deposit Insurance Pricing, Georgetown University and George Mason University (1992); Sarah Kendall and Mark Levonian, A Simple Approach to Better Deposit Insurance Pricing, Proceedings, Conference on Bank Structure and Competition, Federal Reserve Bank of Chicago (1991); R. Avery, G. Hanweck and M. Kwast, An Analysis of Risk-Based Deposit Insurance for Commercial Banks, Proceedings, Conference on Bank Structure and Competition, Federal Reserve Bank of Chicago (1985).

<sup>2</sup> See, Gary S. Fissel Risk Measurement, Actuarially Fair Deposit Insurance Premiums and the FDIC's Risk-Related Premium System, FDIC Banking Review (1994), at 16-27, Table 5, Panel B. Single-copy subscriptions of this study are available to the public free of charge by writing to FDIC Banking Review, Office of Corporate Communications, Federal Deposit Insurance Corporation, 550 17th Street, N.W., Washington, D.C. 20429.

<sup>3</sup> *Id.*, at Tables 2 and 5.

per year. Based on the industry's year-end 1993 average tax rate of 31.5 percent, there will be an after-tax impact on profits of approximately \$3.15 billion per year. BIF members may pass some portion of the cost savings on to their customers through lower borrowing rates, lower service fees, and higher deposit rates. Their ability to do so will be affected by factors such as the level of competition faced by banks.

#### 4. Other Factors—Consideration of the Impact on the SAIF of Decreased BIF Rates

A question has been raised concerning whether the Board may take into consideration the impact on SAIF in setting BIF rates. Based on recent projections, the BIF is expected to recapitalize between May 1 and July 31, 1995. By contrast, recent projections show that the SAIF will not recapitalize until 2002 because assessments to cover interest payments on bonds issued by the Financing Corporation (FICO) divert about \$780 million per year, or about 45 percent of total SAIF assessment revenue. In addition, the SAIF assessment base has been shrinking since the SAIF was created in 1989. The FICO will continue to divert SAIF assessments for interest payments on FICO bonds until 2019 when the bonds mature.

Section 7(b)(2)(A)(ii) of the FDI Act requires the Board to consider certain factors in setting assessment rates, one of which is "any other factors that the Board of Directors may deem appropriate". Section 7(b)(2)(B) of the FDI Act requires the Board to set semiannual assessments for members of each fund "independently" from semiannual assessments for members of the other insurance fund. Read together, these provisions do not specifically prohibit Board consideration of the impact of BIF rates on SAIF members as long as the rates are set independently.

However, section 7(b)(2)(A)(i) requires the Board to set rates to maintain the BIF reserve ratio. If the Board were to take into consideration the impact on the SAIF when it set BIF rates and, as a result, the reserve ratio continued to increase in excess of the DRR, it might be considered a violation of the statute. By contrast, an increase in the reserve ratio due to revenue generated from the minimum assessments and maintaining a risk-based assessment system would not be a violation because those provisions are mandated by the statute.

#### B. Need for Decreased Rates

As discussed in Section II, management of the reserve ratio is necessarily imprecise because the

factors affecting this ratio cannot be predicted with certainty. Changes in the reserve ratio are primarily a function of assessment revenues, investment income, operating expenses and insurance losses resulting from bank failures.

The BIF is expected to recapitalize between May 1 and July 31, 1995. It is unlikely that the BIF will recapitalize prior to the second quarter of 1995 because, after declining from 1992 through mid-year 1994, there are indications that insured deposits have begun to increase.

Other than the revenues that may be necessary to achieve and maintain the DRR of 1.25% in the second half of 1995, projections indicate that the BIF will require little or no assessment income to cover losses and expenses for that period. Investment income is expected to approach \$500 million for the second half of the year. As noted above, for the same period insurance losses are projected to be \$130 million, and operating expenses are projected to be approximately \$260 million. Thus, based on current projections, investment income alone should suffice to cover BIF obligations unrelated to the reserve ratio in the second half of 1995.

The proposed assessment rate schedule is the current, nine-cell matrix with assessment rates ranging from 4 basis points per year for the highest-rated institutions to 31 basis points for the lowest-rated institution (see Table 1, Proposed Rate Schedule). For purposes of maintaining the reserve ratio at 1.25%, the relevant fact is that the estimated 4.5 basis point average assessment rate resulting from this matrix will produce approximately \$1.1 billion of annual revenue for the BIF in the short run. If the proposed matrix takes effect at or near the beginning of the second semiannual period in 1995, the reserve ratio will reach nearly 1.3% by year-end, under current assumptions concerning insurance losses, operating expenses, insured deposit growth, and other relevant factors.

However, the staff's baseline assumptions imply that an average assessment rate of 4 to 5 basis points is necessary to maintain the BIF reserve ratio at 1.25% over a 5–7 year horizon (see Tables 2–4). While the baseline assumptions for insurance losses may be characterized as relatively pessimistic given current economic conditions, it is important to recognize that such conditions are rare in the banking industry's recent history. For 1994, the ratio of insurance losses to estimated insured deposits was approximately one-half of 1 basis point (estimated). This ratio had not previously fallen

below 1 basis point in any year since 1980, averaging 16 basis points for the 1981–93 period and exceeding 30 basis points in three of those years. Therefore, the staff's baseline loss assumptions may be considered rather optimistic relative to recent historical experience.

The proposed matrix would yield assessment revenue sufficient to finance losses equal to the 60-year annual average, nearly 4 basis points of estimated insured deposits, with a margin to absorb losses that moderately exceed the average. In view of the recent experience reviewed above, the staff believes this to be the minimum amount necessary to maintain the DRR consistently over the near-term future.

Given the increasing degree of competition faced by insured institutions, the increasing opportunities for risk-taking as a result of rapid financial innovation, and the increased variability of interest rates as well as other prices due to the globalization of markets and other factors, the staff believes that the loss experience in the banking industry is unlikely to revert to pre-1980 norms. Rather, the average yearly loss ratio is likely to exceed the 60-year average going forward, with large year-to-year variability.

Prudence requires that the Board be provided with the flexibility to adjust assessment rates in a timely manner in response to changing conditions. Accordingly, the Board proposes to increase or decrease the proposed assessment schedule by an adjustment factor of up to 5 basis points or fraction thereof. The adjustment factor is the maximum amount by which the Board could adjust the assessment rate schedule without going through an additional notice and comment rulemaking process. Such adjustments could only be made to the assessment schedule in its entirety, not to individual risk classification cells. Nor could the spread of 27 basis points be changed by means of the adjustment factor. Accordingly, by means of the adjustment factor, the Board could adjust the proposed assessment schedule of 4–31 basis points to a maximum assessment schedule of 9–36 basis points and a minimum assessment schedule of 0–27 basis points.

This adjustment factor would provide the Board with the flexibility to raise a maximum additional \$1.2–\$1.4 billion in the near term without undertaking a rulemaking. An adjustment factor of 5 basis points appears modest when viewed historically, as the loss-to-insured deposits ratio has been quite variable; the standard deviation was 8.6 basis points for the 1933–93 period and



11.7 basis points for 1983–93. In view of the currently favorable banking environment, however, a 5 basis point adjustment factor should be sufficient to maintain the DRR in the short run.

#### IV. Application and Adjustment of Proposed Assessment Rate Schedule

##### A. Summary

The proposal would establish (1) the manner in which the new schedule of assessment rates set forth in Section III, will be applied in the semiannual period during which the DRR is achieved, and (2) a process for adjusting the proposed rate schedule (within prescribed parameters) to maintain the reserve ratio at 1.25% without the necessity of notice and comment rulemaking procedures for each adjustment. In conformity with the statutory directives, the proposed assessment schedule would not become effective unless and until the DRR is, in fact, achieved. Once effective, however, the proposed rate would apply to the remainder of the semiannual period after the DRR is achieved and to semiannual periods thereafter.

For semiannual periods after that period in which the DRR is achieved, the proposed rate would be adjusted semiannually up or down by the adjustment factor of up to and including 5 basis points as necessary to maintain the target DRR at 1.25%. The semiannual assessment schedule, and any adjustment thereto, would be adopted by the Board in a resolution which reflects consideration of the statutory factors upon which it is determined. The Board would announce the semiannual assessment schedule not later than 45 days prior to the November 30 and May 30 quarterly invoice dates, and the adjusted rates would first be reflected in those invoices.

##### B. Semiannual Period During Which DRR Is Achieved

Section 7(b)(2)(E) provides that:

The Corporation shall design the risk-based assessment system for any deposit insurance fund so that, if the \* \* \* reserve ratio of that fund remains below the designated reserve ratio, the total amount raised by semiannual assessments on members of that fund shall be not less than the total amount that would have been raised if—

- (i) section 7(b) as in effect on July 15, 1991 remained in effect; and
- (ii) the assessment rate in effect on July 15, 1991 [23 basis points] remained in effect.

Based on the language of this section as well as its legislative history, the Board believes that it has no authority to decrease the assessment rates paid by BIF members until after the reserve ratio has, in fact, reached the DRR, regardless

of projections for BIF recapitalization. Section 7(b)(2)(E) indicates that the Board may not lower BIF assessment rates in anticipation of meeting the DRR during the upcoming semiannual period. If the Board were to decrease the rates based on projections for BIF recapitalization, the reserve ratio would “remain” below the DRR at the time of the Board’s action and the minimum assessments provisions of section 7(b) would continue to apply.

This interpretation is consistent with Congressional intent that the FDIC maintain a minimum assessment rate of 23 basis points for BIF members until the fund achieves its DRR. In connection with the Senate Banking Committee’s consideration of whether to establish a maximum assessment for BIF members, the Committee stated, “[t]he Committee is *firm* in its view that the 23 basis point premium rate now in effect [during the second semiannual period of 1991] should not be reduced until the BIF achieves its designated reserve ratio.” [Emphasis added.] S. Rep. No. 167, 102d Cong., 1st Sess., 30 (1991). The Committee believed that, “So long as BIF reserves remain insufficient to cover demands on the BIF as they arise, taxpayers will be at risk” and passed a bill which “encourages the FDIC to begin rebuilding the BIF by restricting the FDIC’s discretion to delay recapitalization.” *Id.* at 29.

If section 7(b)(2)(E) were further interpreted to mean that the FDIC must wait to reduce BIF rates until the beginning of the semiannual period after the DRR was reached, the FDIC would have collected far in excess of the revenue required to maintain the reserve ratio at the DRR with no mechanism for rebating the excess amounts. This is particularly the case if the BIF recapitalizes early in the semiannual period, as is indicated by current projections. If this provision were interpreted in this manner, the vast majority of the assessment revenue collected would not be needed to maintain the BIF at the DRR.

Although the Board must set semiannual assessments for BIF members, the FDI Act is silent as to when assessments must be announced or set and expressly allows the Board to prescribe the manner and time of assessment collections. See FDI Act, sections 7(b)(2)(A); 7(b)(3) and 7(c)(2)(B).<sup>4</sup> 12 U.S.C. 1817(b)(2)(A); 1817(b)(3) and 1817(c)(2)(B). Thus, the

Board may set semiannual assessment rates to take effect after the DRR has been achieved.

The reserve ratio is the dollar amount of the BIF fund balance divided by the estimated insured deposits of BIF members. Although data for the fund balance is accounted for on a monthly basis, the amount of estimated insured deposits is based on data from the quarterly reports of condition (call reports). Because current projections indicate that the BIF will recapitalize early in the July–December semiannual period, the amount of estimated insured deposits would be determined by the information on the June call reports which are due on July 30 (or for some institutions, August 14). Due to the customary time lag involved in verifying the information from the call reports, it is probable that the determination that the DRR has been achieved will not be made until mid-September. Moreover, because the fund balance is determined only on a monthly, rather than daily basis, the date on which the Board ascertains that the DRR has been attained must necessarily be the last day of the month.

Because the Board cannot lower assessment rates until it is certain that the DRR has been attained, the May 30 quarterly invoice and, very likely, the August 30 quarterly invoice will reflect the pre-DRR rate of approximately 6 basis points (one-quarter of the annual assessment rate of 23 basis points). The June 30 direct debit of the amount specified on the May 30 invoice will proceed as planned. However, in the event it is determined that the DRR has been attained before the September 30 direct debit occurs, the Board proposes to promptly notify BIF members that the September 30 direct debit will be modified to reflect the new assessment rate.

Because the proposed 4–31 basis point assessment rate would apply from the first day of the month after the DRR was achieved for the remainder of the semiannual period, it is likely that some BIF members will have overpaid their semiannual assessments. For example, if the DRR is determined to have been achieved on July 31 and the 4–31 basis point rate becomes effective on August 1, a portion of the assessment paid for the July–September quarter would constitute an overpayment. In such a case, pursuant to section 7(e) of the FDI Act, the FDIC is permitted to refund any assessment overpayment or to credit the overpayment toward the next assessment due until the overpayment amount is exhausted.

Section 7(e) applies in the case of “any payment in excess of the amount

<sup>4</sup> Section 7(b)(1)(A) was amended in FDICIA to permit the FDIC to establish “and, from time to time, adjust the assessment rates \* \* \*”. FDICIA, section 104(b). This provision was in effect from December 19, 1991 until January 1, 1994 when the risk-based assessment provisions became operative.



due". The FDIC has interpreted this provision to apply case-by-case to an overpayment by an individual institution caused by a computation error or revisions to the institution's reported assessment base. Because individual institutions would have overpaid the amount that actually was due once the proposed rate became effective, section 7(e) should also be applicable in this situation.

On the other hand, if the DRR is not achieved, no action would be required because the existing collection process would simply remain in effect. In such a case, the September 30 direct debit of the amount specified on the August 30 quarterly invoices would go forward. If the DRR were to be reached, for example, on September 30, the proposed rate would nonetheless take effect at that point for the remainder of the July–December semiannual period.

In the event the FDIC collects more assessment revenue from an institution than is required for the July–December semiannual period, a refund of the overpayment, with interest from the time the DRR is achieved, would be provided. The FDIC intends to provide any such refund electronically using the ACH facility, but may do so by check. The same routing transit numbers and accounts used for the direct debit collection would be used for electronic refunds.

#### *C. Semiannual Periods After the DRR Is Achieved*

The 4–31 basis point assessment schedule would continue to apply to semiannual periods commencing with the semiannual period after the DRR has been achieved (presumably January 1996). However, to enable the Board to maintain the reserve ratio at the target DRR in future semiannual periods, the proposal would authorize the Board to adjust (by resolution) the proposed assessment schedule by an adjustment factor of up to and including 5 basis points or fraction thereof. By this means the Board proposes to limit its discretion to adjust rates within a range of 5 basis points. As noted above, such adjustments could only be made to the assessment schedule in its entirety, not to individual risk classification cells. Nor could the spread of 27 basis points be changed by means of the adjustment factor. Accordingly, by means of the adjustment factor, the Board could adjust the proposed assessment schedule of 4–31 basis points to a maximum assessment schedule of 9–36 basis points and a minimum assessment schedule of 0–27 basis points. Thus, for example, if the rate for 1A banks was 4 basis points, no matter how many times

the assessment schedule were adjusted up or down, the rate for 1A banks could never go above 9 basis points without going through the notice and comment rulemaking process. Finally, if financial conditions warranted a change beyond the maximum amount of the adjustment factor, the Board would make such adjustments through the notice and comment rulemaking process.

The adjustment factor for any particular semiannual period would be determined by (1) the amount of assessment income necessary to maintain the reserve ratio at 1.25% (taking into account operating expenses and expected losses) and (2) the particular risk-based assessment schedule that would generate that amount considering the risk composition of the industry at the time. The Board proposes to adjust the assessment rate schedule every six months by the amount, up to and including the maximum adjustment factor of 5 basis points, necessary to maintain the reserve ratio at the DRR. Such adjustments will be adopted in a Board resolution that reflects consideration of the statutory factors. These include expected operating expenses, projected losses, the effect on BIF members' earnings and capital and any other factors the Board determines to be relevant to the BIF. The resolution will be adopted and announced at least 45 days prior to the invoice date for the first quarter of the semiannual period in which the rate will take effect (*i.e.*, November 30 and May 30 invoice dates). Those invoices would then first reflect the adjusted assessment rate schedule.

#### **V. Request for Comment**

The Board invites comments on all aspects of the proposal.

#### **VI. Paperwork Reduction Act**

No collections of information pursuant to section 3504(h) of the Paperwork Reduction Act (44 U.S.C. 3501 *et seq.*) are contained in this notice. Consequently, no information has been submitted to the Office of Management and Budget for review.

#### **VII. Regulatory Flexibility Act**

The Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*) does not apply to a rule of particular applicability relating to rates, wages, corporate or financial structures or reorganizations thereof. *Id.* at 601(2). Accordingly, the statute does not apply to the proposed changes in the assessment rate schedule, the structure of that schedule and future adjustments thereto. In any event, to the extent an institution's assessment is

based on the amount of its domestic deposits, the primary purpose of the Regulatory Flexibility Act, that agencies' rules do not impose disproportionate burdens on small businesses, is fulfilled.

#### **List of Subjects in 12 CFR Part 327**

Assessments, Bank deposit insurance, Banks, Banking, Financing Corporation, Savings associations.

For the reasons stated in the preamble, the Board proposes to amend part 327, as amended at 59 FR 67153 effective April 1, 1995, 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, 1441b, 1817–1819.

2. Section 327.8 is amended by adding a new paragraph (i) to read as follows:

#### **§ 327.8 Definitions.**

\* \* \* \* \*

(i) As used in § 327.9, the following terms have the following meanings:

(1) *Adjustment factor.* The maximum number of basis points by which the Board may increase or decrease Rate Schedule 2 set forth in § 327.9(a).

(2) *Assessment schedule.* The set of rates based on the assessment risk classifications of § 327.4(a) with a difference of 27 basis points between the minimum rate which applies to institutions classified as 1A and the maximum rate which applies to institutions classified as 3C.

3. Section 327.9 is amended by revising paragraphs (a) and (b), by redesignating paragraph (c) as paragraph (e) and adding new paragraphs (c) and (d) to read as follows:

#### **§ 327.9 Assessment rate schedules.**

(a) *BIF members.* Subject to § 327.4(c), the annual assessment rate for each BIF member other than a bank specified in § 327.31(a) shall be the rate in the Rate Schedules below applicable to the assessment risk classification assigned by the Corporation under § 327.4(a) to that BIF member. Until the BIF designated reserve ratio of 1.25 percent is achieved, the rates set forth in Rate Schedule 1 shall apply. After the BIF designated reserve ratio is achieved, the rates set forth in Rate Schedule 2 shall apply. The schedules utilize the group and subgroup designations specified in § 327.4(a):

## RATE SCHEDULE 1

Capital group	Supervisory subgroup		
	A	B	C
1 .....	23	26	29
2 .....	26	29	30
3 .....	29	30	31

## RATE SCHEDULE 2

Capital group	Supervisory subgroup		
	A	B	C
1 .....	4	7	21
2 .....	7	14	28
3 .....	14	28	31

(b) *BIF recapitalization schedule.* The following schedule indicates the stages by which the Corporation seeks to achieve the BIF designated reserve ratio of 1.25 percent. The schedule begins with the semiannual period ending December 31, 1991 and ends on the earlier of the semiannual period ending June 30, 2002 or the date on which the BIF designated reserve ratio is achieved:

Semi-annual period	Target reserve ratio (per-cent)
1991.2 .....	-0.36
1992.1 .....	-0.28
1992.2 .....	-0.01
1993.1 .....	0.03
1993.2 .....	0.06
1994.1 .....	0.08
1994.2 .....	0.09
1995.1 .....	0.15
1995.2 .....	0.21
1996.1 .....	0.28
1996.2 .....	0.34
1997.1 .....	0.42
1997.2 .....	0.50

Semi-annual period	Target reserve ratio (per-cent)
1998.1 .....	0.59
1998.2 .....	0.67
1999.1 .....	0.76
1999.2 .....	0.85
2000.1 .....	0.94
2000.2 .....	1.03
2001.2 .....	1.12
2001.2 .....	1.21
2002.1 .....	1.25

(c) *Rate adjustment; announcement—*

(1) *Semiannual adjustment.* The Board may increase or decrease Rate Schedule 2 set forth in paragraph (a) of this section semiannually by an adjustment factor of up to and including 5 basis points or fraction thereof as the Board deems necessary to maintain the reserve ratio at the BIF designated reserve ratio. In no case may such adjustment result in a negative assessment rate. The adjustment factor for any semiannual period shall be determined by:

(i) The amount of assessment revenue necessary to maintain the reserve ratio at the designated reserve ratio; and

(ii) The assessment schedule that would generate the amount of revenue in paragraph (c)(1)(i) of this section considering the risk profile of BIF members.

(2) In determining the amount of assessment income in paragraph (c)(1)(i) of this section, the Board shall take into consideration the following:

- (i) Expected operating expenses;
- (ii) Case resolution expenditures and income;
- (iii) The effect of assessments on BIF members' earnings and capital; and
- (iv) Any other factors the Board may deem appropriate.

(3) *Announcement.* The Board shall:

- (i) Adopt the semiannual assessment schedule and any adjustment thereto by means of a resolution reflecting consideration of the factors specified in paragraph (c)(2)(i) through (iv) of this section; and

- (ii) Announce the semiannual assessment schedule and any adjustment thereto not later than 45 days before the invoice date specified in § 327.4(c) for the first quarter of the semiannual period for which the adjusted assessment schedule shall be effective.

(d) *Special provisions.* The following provisions apply only for the first semiannual period after January 1, 1995 in which the BIF designated reserve ratio is achieved:

(1) Notwithstanding the provisions of § 327.3(c)(2) or § 327.3(d)(2), the Corporation may modify the time of the direct debit of the assessment payment which next occurs after the Board determines that the designated reserve ratio has been achieved; and

(2) Notwithstanding the provisions of § 327.7(a)(3), if the designated reserve ratio is achieved at the end of a month which is not the end of a quarter and, as a result, an institution has overpaid its assessment, the Corporation shall provide interest on any such overpayment beginning on the date the designated reserve ratio was achieved.

\* \* \* \* \*

By order of the Board of Directors.

Dated at Washington, D.C., this 31st day of January 1995.

Federal Deposit Insurance Corporation.

**Robert E. Feldman,**

*Acting Executive Secretary.*

[FR Doc. 95-3670 Filed 2-15-95; 8:45 am]

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