**REMARKS
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I appreciate the chance to come talk to you today about some of the important items on our agenda at the FDIC. Since I became Chairman, we've spent the past eight months shaping the FDIC and sharpening its focus.

During that time we have identified several important priorities for the Corporation. We must protect the deposit insurance system to ensure it works for the industry and the American people. We must make sure our management is effective and efficient so we retain the confidence of the Congress and the marketplace. And we must be a leader in the development of good banking policy.

I want to spend a little time today talking about our number one priority: A fundamental reform of the deposit insurance structure at the FDIC. We believe this reform effort is good policy, good business and in the interest of financial stability.

The FDIC currently holds funds - totaling $43 billion dollars - in trust for the American people. This money was paid by the banks and thrifts and these funds are the tangible symbol of the insurance contract between the industry, the federal government and the American people. We are proud of the role we play in making sure this covenant is kept.

To be honest, I wasn't sure if I should discuss this with you all today. So I decided to call John Douglas, who is sitting in the audience today, to get his thoughts. John, please stand up so everyone can see you. I had not met John, but 98 percent of what I had heard about him as the former General Counsel of the FDIC was positive, and, for a lawyer, that's almost unheard of.

John's advice was to talk about deposit insurance reform, so I will.

Before I get into the reforms, though, I want to spend a minute discussing just how important deposit insurance is to our banking and financial system.

This is a program that has been resoundingly successful in maintaining public confidence and preserving stability in our banking system. During the crisis of the 1980s and early 1990s, the FDIC and RTC resolved 2,362 failures of insured institutions involving more than $700 billion in assets. There were no bank runs, no panics, no disruptions to financial markets and no debilitating impact on overall economic activity. The last time we saw a banking crisis this bad was during the Great Depression. Yet, the outcomes were very different - in large part due to the presence of the FDIC and its stabilizing presence in the marketplace.

We in the United States sometimes fail to appreciate what a truly remarkable accomplishment this was, and we tend to undervalue the importance of federal deposit insurance when times are good.

Helen Boosalis, past president of the AARP, has an opinion on the subject. She believes the FDIC is, and I quote, "… precisely what a government program should be - one that not only has accomplished what it was designed to do, but has become for many a symbol of the very strength and safety of our nation." She was right. She went on to point out that "… the role of this program in protecting depositors should be preserved and strengthened." This is precisely what we intend to do. In fact, that's what our deposit insurance reform proposals are all about - strengthening and preserving this important system.

After a thorough review, we found several problems - technical or otherwise - in the law or in our own operating procedures that could pose problems - either for the effective management of deposit insurance or for the economy as a whole. We have come to the conclusion that a reform of the deposit insurance system is both necessary to strengthen the deposit insurance system and in the national interest.

The first question in many of your minds will be - Why do we need reform? And if you're a banker, I know what you're thinking. You're thinking - I don't see what's wrong with the system now. There's no crisis and we don't have to pay premiums for deposit insurance. Where's the problem?

It's true there is no crisis. The deposit insurance system generally works well. But it does have flaws and now - with the leadership of many in Congress - we have the opportunity to address them.

The deposit insurance system is supposed to protect depositors and help the economy by preventing bank panics and stabilizing the financial system. It's supposed to accomplish this without causing other problems. Specifically, it should not increase banks' appetite for risk. And, most of all, deposit insurance should never cost the taxpayers a dime.

If you buy these propositions, which I personally think are hard to argue with, and see how the present system stacks up - the need for reform becomes obvious. I'd like to talk today about three sets of problems we face.

First, there is the question of our fund structure. We have two deposit insurance funds, the Bank Insurance Fund and the Savings Association Insurance Fund. With industry consolidation over the past decade or so, the distinction between the two has become blurred. Further, there is the very real possibility that banks could face premiums while the thrift across the street does not - or vice versa. To solve these problems once and for all, the FDIC has recommended these funds be merged into one Deposit Insurance Fund.

Now I'm going to talk about some of the other important problems reform would solve. Today's system is largely a reaction against the high premiums we charged in the late 1980s and early 1990s to rescue the industry from the bank and thrift crisis. Once the crisis had passed, Congress prevented the FDIC from charging the vast majority of banks and thrifts for their deposit insurance during good times. However, when the funds fall below certain levels - usually during tough economic times - the FDIC must charge steep premiums on the industry. I'm a former banker. Believe me, it doesn't make any sense to increase the financial burden on banks and thrifts when they are least able to bear it and limit credit availability when the economy most needs it. This is directly contrary to the purpose of deposit insurance.

These statutes also prevent the FDIC from charging appropriately for risk during good economic times. Right now, even though every bank poses some insurance risk, 92 percent of them pay nothing for deposit insurance. There are two things wrong with this. First, the premiums that most banks pay don't really depend on risk. This encourages some banks to pursue their riskier lines of business, something my new friends in Washington call moral hazard. It also means that safe banks unnecessarily subsidize risky banks. That's not fair.

A second problem is that new deposits enter the system without paying. Essentially, the banks that were around in the early 1990's endowed the funds, and newcomers are not asked to pay the ongoing costs of the deposit insurance system. More than 900 new banks and thrifts have never paid for deposit insurance. I know this firsthand because I chartered a bank in Texas in the late 1990s and we never paid a dime. Others have grown significantly without paying additional premiums. This imbalance is a sore spot with many in the industry and they have consistently asked us to do something about it.

To solve both the structure and the new entrant problems, the FDIC has asked for greater flexibility in managing a merged fund. That means several things. First, the FDIC should have the discretion to set the target size for the fund and determine how quickly to bring it back toward the target. This would include the discretion to give assessment credits or cash rebates if the fund grows too large, and levy surcharges if the fund shrinks too small. We are not seeking unfettered discretion, though. We are not opposed to guiding principles and reporting requirements and we expect to be held accountable by the industry, the Congress and the public. We would prefer, however, that the Congress not set automatic triggers or hard targets, because they can create the kinds of problems we see in the present system.

The FDIC also needs greater discretion to charge based on risk. Every good insurance company charges riskier customers more. This would make the system fairer for safer banks. In my view, pricing properly for risk would require only minor adjustments to the FDIC's current assessment system.

Some banks understandably worry that changing the assessment system could make it too subjective. Our plan is to rely as much as possible on objective indicators to distinguish and price for risk more accurately within our least-risky premium category. Before using any additional indicator, though, we would thoroughly analyze it to make sure it had statistical value as a measure of risk. And, finally, nothing would happen without input from the industry and the public

Now let's discuss the industry's question about the imbalances that exist between those that paid in the early 1990s and those that have paid little or nothing. Giving a one-time assessment credit is a good way to deal with this problem. Our analysis estimates a one-time credit would let the safest banks offset premiums for several years, assuming present conditions persist and that credits are based on past contributions, as we have recommended.

I know what you're thinking - all this is very well, but what's the bottom line? What will it cost my bank? I will tell you this: the point of the FDIC's proposed reforms is not to increase assessment revenue from the industry, but to distribute the assessment burden more evenly over time and more fairly across insured institutions. Doesn't it make sense to charge two or three basis points over time rather than nothing for five years then a sudden disruptive 23 basis point charge? I believe our approach makes sense economically and - again, as a former banker - I can assure you it makes good business sense.

But what does it mean specifically? It means that, if the conditions we have seen for the last several years were to continue, the safest banks and thrifts that paid to build up the funds on balance would be no worse off than they are under the present system. Riskier banks, fast growers, and new entrants would bear more of the assessment burden in the short term. It also means that, if conditions worsen, the safest banks would be better off than they are under the present system, since their premiums during a downturn would be lower.

I know that some banks are very concerned about the costs of the FDIC's reform proposals. I can tell you that in many cases their fears are being generated by unfounded assumptions about how the new system would work. For example, I've heard some bankers say that they believe if the FDIC had greater discretion to manage the funds, it would simply set the target at the highest possible level and peg the fund ratio there. This is ridiculous. Nothing in the FDIC's history suggests we would do that.

I'm in North Carolina. I decided to play a little to the hometown crowd to help clarify how the credit system would work. North Carolina has a nice cross-section of banks, new and old, large and small, that fairly represents the spectrum of institutions across the nation. So we did our analysis on institutions in your state and I've brought some copies of our analysis if any of you want to pick it up after my remarks.

Here's what we found. Using the formula in the deposit insurance reform bill pending before the House of Representatives, we computed the amount of the credit for every insured institution chartered in North Carolina. We found that, under reasonable assumptions, the typical bank would not have to pay premiums for three to six years. Six years is a long time.

I stress that these results for the North Carolina banks are not unique. The formula for determining the initial assessment credit works the same way for every institution in America. After looking at our numbers, if any institutions are uncertain about the approximate credit they would receive initially under the new system, they should contact the FDIC (Don Inscoe, e-mail address dinscoe@fdic.gov) and we will be happy help you with the calculation.

Another concern I've heard expressed by bankers is that our assessment proposal needlessly complicates the system - I would argue that the above data suggest that our proposal would correct an imbalance in the system that the banks themselves insist needs to be corrected. In my view, the burden is on those expressing the concern to propose a simpler alternative that addresses the problem as effectively.

I've been at the FDIC about six months now. I arrived with a banker's natural skepticism about these reforms, but it didn't take long for me to become convinced. The reforms make too much sense.

I think Congress, too, is becoming convinced. Bills have been introduced in both the House and the Senate that take a number of major steps forward. Both give the FDIC significantly more discretion in managing the insurance fund, provide for risk-based premiums, provide for steady assessments over time, and allow for assessment credits to correct the imbalance between the late entrants and the banks that capitalized the FDIC funds in the early 1990s.

We are not alone. Both the Treasury and the Federal Reserve Board have testified in strong support of our framework for changing the way deposit insurance is paid for.

While we appreciate this support, we recognize that they have a concern with the issue of coverage.

Because there is some disagreement in the industry about this issue, it tends to get all the attention. Everybody and his brother - from Chairman Greenspan to Secretary O'Neil to a columnist at the Wall Street Journal have expressed their concerns about higher coverage.

But let's take a minute and look at the issue. The coverage level is fixed in law at $100,000 dollars per insured account, and the real value of deposit insurance is declining over time due to inflation. It has been 22 years since the coverage limit was last increased. Right now, the real value of the 1980 $100,000 dollar level is $47,000 dollars. A declining limit means declining protection for depositors. If you believe as we do that deposit insurance has value, this should be a subject of concern.

Our recommendation is simple: we are recommending that the coverage limit be indexed from the present level of $100,000 to ensure the value of deposit insurance in the economy doesn't wither away over time. In real terms, this does not expand coverage. It simply holds it steady over time.

We have, however, recommended that Congress consider a higher limit for retirement accounts. In this day and age, $100,000 is not a lot of money to save for retirement. Middle-income families routinely save much more. There is some precedent for this - prior to 1980, retirement accounts were insured at two-and-a-half times the overall level.

So coverage - while important - should be kept in context. We believe the problems in the coverage area could be solved with some relatively minor changes. And frankly, the issue of coverage is in many ways a political issue for Congress to decide.

And they are deciding. We are pleased that a bill is moving in the House of Representatives and we hope Senator Sarbanes will hold a hearing on deposit insurance reform this spring. I am confident we will enact a good deposit insurance reform bill this year.

That's not to say we don't have issues here and there - and I will soon detail our comments in a letter to members of the House Financial Services Committee.

The only one I'll mention here is a provision in the House bill that gives us significant pause. It would end the FDIC's current practice of deducting our loss reserve from our overall fund balances for assessment purposes. This is bad accounting and we strongly oppose it.

We have a few other concerns with some of the particulars of the approach contained in the House bill, but I do not want to overstate them. The bill contains many features that would significantly improve the system, and I look forward to working with the leaders in Congress to address these concerns.

Let me conclude by stating we at the FDIC take our charge very seriously. We are here to protect your bank deposits, to protect financial stability and to protect the deposit insurance funds. We will be vigilant in this effort and we will continue to make the case that reforming the system will enhance our ability to do our job and perform our mission.

Thank you again for the opportunity to speak. I'd welcome the chance to answer any questions you might have.

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