NEWS RELEASE

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FDIC PROPOSES RULE TO IMPLEMENT "PROMPT CORRECTIVE ACTION" REQUIREMENTS

The FDIC Board of Directors has issued for public comment a rule that would implement Section 131 of the FDIC Improvement Act of 1991 (FDICIA), which requires regulators to take specified "prompt corrective action" when an insured institution's capital falls to certain levels.

Under the new law, restrictions and prohibitions on an FDIC-insured bank or thrift become more severe as the institution's capital level declines. The sanctions begin with measures such as restrictions on dividends and management fees, and culminate in the closing of institutions that are critically undercapitalized for a prescribed period.

The proposal, which the Board agreed to issue on June 23, applies primarily to state-chartered banks supervised by the FDIC and insured branches of foreign banks also supervised by the agency. However, the Federal Reserve Board, the Office of the Comptroller of the Currency and the Office of Thrift Supervision are in the process of adopting parallel prompt corrective action rules that would apply to depository institutions regulated by those agencies.

The FDIC proposal would amend the agency's capital regulation to define the five capital levels specified in the law. Those are:

- A "well-capitalized" institution would have at least 10 percent total capital to risk-weighted assets (including six percent in "Tier 1" or "core" capital), at least five percent Tier 1 capital to total assets (leverage ratio), and not be subject to a written order or directive from its primary regulator requiring it to maintain a higher level of capital.
- An "adequately capitalized" institution would meet all required minimum capital levels but not meet the definition of "well-capitalized." For banks,

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those minimum capital levels (when fully phased in at year-end 1992) will be eight percent total risk-based capital (including four percent Tier 1) and four percent leverage capital.

o An "undercapitalized" institution would fail to meet one or more of the required minimum capital levels as noted above but would be better capitalized than institutions in the two categories described below. Under FDICIA, an "undercapitalized" bank or thrift automatically is subject to restrictions on asset growth and is prohibited from making acquisitions, opening branches or engaging in new lines of business without prior approval of its regulator.

o A "significantly undercapitalized" institution would be defined as having a total risk-based capital ratio of less than six percent (or less than three percent Tier 1) or a Tier 1 leverage capital ratio of less than three percent. This institution would be subject to the same restrictions applying to "undercapitalized" institutions plus certain others, such as mandatory restrictions on bonuses and raises to senior executive officers.

o A "critically undercapitalized" institution would have Tier 1 leverage capital that is two percent or less of total assets. Institutions in this category would be subject to the same restrictions and prohibitions on "undercapitalized" and "significantly undercapitalized" institutions, plus other limitations.

At a minimum, regardless of its primary federal regulator, a "critically undercapitalized" institution under the new law must receive written approval from the FDIC before it can take actions that include: engaging in material transactions other than in the usual course of business; extending credit for highly leveraged transactions; amending its charter or bylaws; making material changes in accounting methods; paying excessive compensation or bonuses; and paying above-market interest rates on deposits.

A "critically undercapitalized" institution also can be placed in conservatorship or receivership if its capital level is not increased over a prescribed period.

Most FDIC-insured banks and thrifts would be considered well-capitalized or adequately capitalized under the proposed definitions. The FDIC estimates that, based on recent reports filed with the regulators, three percent of the nation's approximately 12,300 insured banks (with assets of about $232 billion) and 14 percent of the 2,000 insured thrifts (with assets of about $188 billion), have capital ratios that would fit into the three proposed categories for undercapitalized institutions. However, the actual number of banks and thrifts that would be subject to limitations for undercapitalized institutions would be higher because provisions of FDICIA allow the agencies to "downgrade" other institutions under certain circumstances.

For example, the restrictions for undercapitalized institutions may be applied to a bank or thrift that meets minimum capital requirements but otherwise is in a less-than-satisfactory condition, such as one that has significant asset quality problems. Also under the law, a bank or thrift is prohibited from paying management fees, dividends or other capital distributions if the payment would result in the institution entering the ranks of the undercapitalized.

The FDIC proposal also contains procedures for issuing and contesting "prompt corrective action" directives to institutions, including those requiring the dismissal of directors and senior executive officers, as well as those downgrading an institution.

Comments are due 45 days after the FDIC proposal appears in the Federal Register.

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