

**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 paragraph (a), removing paragraph (b), redesignating paragraph (c) as paragraph (d), and adding new paragraphs (b) and (c) 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 an institution specified in § 327.31(a) shall be the rate in the following Rate Schedules 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) *Rate adjustment; announcement—*  
 (1) *Semiannual adjustment.* The Board may increase or decrease Rate Schedule 2 set forth in paragraph (a) of this section up to a maximum increase of 5 basis points or a fraction thereof or a maximum decrease of 5 basis points or a fraction thereof (after aggregating increases and decreases), as the Board deems necessary to maintain the reserve ratio at the BIF designated reserve ratio. Any such adjustment shall apply uniformly to each rate in the schedule. In no case may such adjustments result in a negative assessment rate or in a rate schedule that, over time, is more than 5 basis points above or below Rate Schedule 2, nor may any one such adjustment constitute an increase or decrease of more than 5 basis points. 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 (b)(1)(i) of this section considering the risk profile of BIF members.

(2) In determining the amount of assessment revenue in paragraph (b)(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 the amount and basis for any adjustment thereto not later than 45 days before the invoice date specified in § 327.3(c) for the first quarter of the semiannual period for which the adjusted assessment schedule shall be effective.

(c) *Special provisions.* The following provisions apply only with respect to the first time the BIF designated reserve ratio is achieved after 1994:

(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;

(2) Notwithstanding the provisions of § 327.7(a)(3), if, as a result of the new rate schedule having gone into effect, an institution has overpaid its assessment, the Corporation shall provide interest on any such overpayment, as follows:

(i) For the first semiannual period of 1995, beginning on the date the new rate schedule goes into effect; and

(ii) For the second semiannual period of 1995, beginning on the date of the overpayment; and

(3) Notwithstanding the provisions of § 327.7(b)(3), the interest rate applicable to overpayments described in paragraph (c)(2) of this section shall be the arithmetic average of the overnight simple interest rates received by the Corporation on its U.S. Treasury investments for the period during which the Corporation held the overpayment amount.

\* \* \* \* \*

By order of the Board of Directors.

Dated at Washington, DC, this 8th day of August 1995.

Federal Deposit Insurance Corporation.

**Jerry L. Langley,**

*Executive Secretary.*

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**12 CFR Part 327**

**RIN 3064-AB59**

**Assessments; Retention of Existent Assessment Rate Schedule for SAIF-Member Institutions**

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

**ACTION:** Final rule.

**SUMMARY:** This final rule retains the existing assessment rate schedule applicable to members of the Savings Association Insurance Fund (SAIF). The effect of this final rule is that the SAIF assessment rates to be paid by depository institutions whose deposits are subject to assessment by the SAIF will continue to range from 23 cents per \$100 of assessable deposits to 31 cents per \$100 of assessable deposits, depending on risk classification.

**EFFECTIVE DATE:** This final rule becomes effective September 15, 1995.

**FOR FURTHER INFORMATION CONTACT:** James R. McFadyen, Senior Financial Analyst, Division of Research and Statistics, (202) 898-7027, or Valerie Jean Best, Counsel, Legal Division, (202) 898-3812, Federal Deposit Insurance Corporation, Washington, D.C. 20429.

**SUPPLEMENTARY INFORMATION:** The Board of Directors of the FDIC (Board) is retaining the existing assessment rate

schedule applicable to members of the SAIF. The order of discussion under this caption is as follows. The proposed rule to retain the existing assessment rate schedule for SAIF-member institutions is outlined in Section I. The final rule adopted by the Board through this rulemaking procedure is described in Section II. The statutory provisions governing SAIF assessment rates are summarized in Section III. Next, a detailed description of the problems confronting the SAIF is set forth in Section IV. The comment letters received in response to the proposed rule are analyzed under the caption "Comment Summary", and the FDIC's response to the comments is set forth under the caption "Adoption of Final Rule".

## Background

### I. Introduction; The SAIF Assessment-Rate Proposal

The Board has the legal authority to reduce SAIF assessment rates to a minimum average of 18 basis points until January 1, 1998. Beginning January 1, 1998, the minimum average rate must be 23 basis points until SAIF achieves its designated reserve ratio (DRR) of 1.25 percent of estimated insured deposits. Based upon the results of its semiannual review of the capitalization of the SAIF and of the SAIF assessment rates, the Board was inclined to retain the existing assessment rate schedule applicable to SAIF-member institutions for the second semiannual assessment period of 1995 so that capitalization of the SAIF is accomplished as soon as possible.

The FDIC wished to have the benefit of public comment before ending its review for the period, however. Therefore, on February 16, 1995, the Board published a proposed rule to retain the existing assessment rate schedule applicable to members of the SAIF.<sup>1</sup> The Board requested comment on all aspects of the proposed rule. At the same time, the Board published a proposed rule to decrease the assessment rate schedule for members of the Bank Insurance Fund (BIF) to a range of 4–31 basis points, depending on risk classification, when the reserve ratio of the BIF attains the minimum DRR of 1.25 percent of estimated insured deposits.<sup>2</sup>

The Board held a hearing at FDIC headquarters in Washington, D.C. on March 17, 1995 to provide opportunity for interested parties to express orally their views on the proposals to decrease assessment rates for members of the BIF

while retaining the 23–31 basis point assessment schedule for members of the SAIF. Every person or organization that requested an opportunity to testify was accommodated.

A total of twenty witnesses were heard by the full Board during the day-long hearing. They included the Savings Association Insurance Fund Industry Advisory Committee, the American Bankers Association, the Independent Bankers Association of America, America's Community Bankers, the National Association of Home Builders, several bank or thrift associations, individual bank and thrift executives, consumer organizations, a private sector attorney and an independent consultant. The written testimony of each witness as well as the hearing record were included in the FDIC's public comment file on the two proposals.

The public comment period for both proposals expired on April 17, 1995. The Board received a combined total of over 3,200 comment letters including testimony from the public hearing. After taking into account duplicate letters submitted by the same commenter, 2,891 comments were tabulated representing 2,310 individual BIF member respondents, 454 individual SAIF member respondents, 61 trade associations and 66 other individuals/organizations. Comments concerning the BIF proposal are discussed in a separate final rule governing BIF assessment rates published elsewhere in this **Federal Register**.

As detailed in the Comment Summary below, thrifts commenting on the SAIF proposal uniformly asked that the impending disparity between premiums assessed against the banking industry and the thrift industry be reduced or eliminated. A significant number of SAIF members stated, however, that a reduction in SAIF assessment rates to the minimum authorized by current law would not resolve the long-term challenges facing SAIF. They noted that, among other things, draws on the SAIF by the Financing Corporation (FICO) would continue to undermine the SAIF. Many of these commenters urged legislative action, stating that "the Congress must act decisively to defuse the coming crisis of the SAIF". The legislative initiatives suggested by the various commenters require Congressional action and were not part of the assessment-rate proposals. Nonetheless, these initiatives are included in the Comment Summary in an effort to present a complete review of the comments received by the FDIC and in recognition of the significant number of letters that offered comments on such initiatives.

### II. Description of Final Rule

After considering the comments received in response to the proposed rule and other relevant information, the Board has determined to retain the existing assessment rate schedule applicable to members of the SAIF. As a result of this action, the SAIF assessment rate to be paid by institutions whose deposits are subject to assessment by the SAIF will continue to range from 23 cents per \$100 of assessable deposits to 31 cents per \$100 of assessable deposits, depending on risk classification.

Despite the general good health of the thrift industry, the SAIF is not in good condition and its prospects are not favorable. The issues confronting the SAIF are discussed in detail under Section IV. To summarize, the SAIF is significantly undercapitalized. On March 31, 1995, the SAIF had a balance of \$2.2 billion, or about 31 cents in reserves for every \$100 in insured deposits. An additional \$6.6 billion would have been required on that date to fully capitalize the SAIF to its DRR of 1.25 percent of estimated insured deposits. At the current pace, and under reasonably optimistic assumptions, the SAIF would not reach the statutorily mandated DRR until at least the year 2002. Moreover, the SAIF became responsible for resolving failed thrifts on July 1, 1995. The failure of a single large SAIF-insured institution or several sizeable institutions or an economic downturn leading to higher than anticipated losses could render the fund insolvent. While the FDIC is not currently predicting such thrift failures, they are possible.

The main source of income for the SAIF is assessments. A sizable portion of the SAIF's ongoing assessments is diverted to meet interest payments on obligations of the FICO. Reducing the minimum average rate to 18 basis points is presently projected to delay SAIF capitalization until 2005, and it would cause a FICO shortfall as early as 1996. Moreover, there will still be a significant differential between BIF and SAIF assessment rates even if the Board reduces the SAIF assessments to the minimum average allowed by statute.

### III. Statutory Provisions Governing SAIF Assessment Rates

#### A. Section 7 of the Federal Deposit Insurance Act

Section 7(b) of the Federal Deposit Insurance Act (FDI Act) governs the Board's authority for setting assessments for SAIF members. 12 U.S.C. 1817(b). Section 7(b)(1)(A) and (C) require that the FDIC maintain a risk-based

<sup>1</sup> 60 FR 9266 (Feb. 16, 1995).

<sup>2</sup> 60 FR 9270 (Feb. 16, 1995).

assessment system, setting assessments based on: (1) The probable risk to the fund posed by each insured depository institution taking into account different categories and concentrations of assets and liabilities and any other relevant factors; (2) the likely amount of any such loss; and (3) the revenue needs of the fund. Section 7(b)(2)(A)(iii) further directs the Board to impose a minimum assessment on each institution not less than \$1,000 semiannually. The Board must set semiannual assessments and the DRR for each deposit insurance fund independently. FDI Act section 7(b)(2)(B).

In general, the Board must set semiannual assessments for SAIF members to maintain the reserve ratio at the DRR or, if the reserve ratio is less than the DRR, to increase the reserve ratio to the DRR. FDI Act section 7(b)(2)(A)(i). The reserve ratio is the dollar amount of the fund balance divided by estimated SAIF-insured deposits. The DRR for the SAIF is currently 1.25 percent of estimated insured deposits, the minimum level permitted by the FDI Act. In setting SAIF assessments to achieve and maintain the DRR, the Board must consider the SAIF's 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. FDI Act section 7(b)(2)(D).

Before January 1, 1998, if the SAIF remains below the DRR, the total amount raised by semiannual assessments on SAIF members may not be less than the amount that would have been raised if section 7(b) as in effect on July 15, 1991 remained in effect. See FDI Act section 7(b)(2)(E) and (F). The minimum rate required by section 7(b) as then in effect was 0.18 percent.

Beginning January 1, 1998, all minimum assessment provisions applicable to BIF members also apply to SAIF members. Under these provisions, if the SAIF remains below the DRR, the total amount raised by semiannual assessments on SAIF members may not be less than the amount that would have been raised by an assessment rate of 0.23 percent. See FDI Act section 7(b)(2)(E).

In setting semiannual assessments for members of the SAIF, beginning January 1, 1998, if the reserve ratio of the SAIF is less than the DRR, the Board must set

semiannual assessments either, (a) at rates sufficient to increase the reserve ratio to the DRR within 1 year after setting the rates, or (b) in accordance with a schedule for recapitalization, adopted by regulation, that specifies target reserve ratios at semiannual intervals culminating in a reserve ratio that is equal to the DRR not later than 15 years after implementation of the schedule. FDI Act section 7(b)(3). Section 8(h) of the Resolution Trust Corporation Completion Act (RTCCA), Public Law No. 103-204, 107 Stat. 2369, 2388, amended section 7(b)(3) to allow the Board, by regulation, to amend the SAIF capitalization schedule to extend the date by which the SAIF must be capitalized beyond the 15-year time limit to a date which the Board determines will, over time, maximize the amount of semiannual assessments received by the SAIF, net of insurance losses incurred. FDI Act section 7(b)(3)(C).

Amounts assessed by the FICO against SAIF members must be subtracted from the amounts authorized to be assessed by the Board. FDI Act section 7(b)(2)(D).

In order to achieve SAIF capitalization, the Board adopted a risk-related assessment matrix in September 1992 (see Table 1) which has remained unchanged.

TABLE 1.—SAIF-MEMBER ASSESSMENT RATE SCHEDULE FOR THE FIRST SEMIANNUAL ASSESSMENT PERIOD OF 1995

[Basis points]

Capital group	Supervisory sub-group		
	A	B	C
Well Capitalized .....	23	26	29
Adequately Capitalized .	26	29	30
Undercapitalized .....	29	30	31

**B. Statutory Provisions Governing FICO Assessments**

FICO was originated by section 302 of the Competitive Equality Banking Act of 1987 (CEBA), Public Law 100-86, 101 Stat. 552, 585, which added section 21 to the Federal Home Loan Bank Act (FHLB Act).<sup>3</sup> FICO's assessment authority derives from section 21(f) of the FHLB Act, 12 U.S.C. 1441(f). As amended by section 512 of the Financial Institutions Reform, Recovery, and

Enforcement Act of 1989 (FIRREA), Public Law 101-73, 103 Stat. 183, 406, section 21(f) requires that FICO obtain funding for "anticipated interest payments, issuance costs, and custodial fees" on FICO obligations from the following sources, in descending priority order: (1) FICO assessments previously imposed on savings associations under pre-FIRREA funding provisions; (2) "with the approval" of the FDIC Board, assessments against SAIF member institutions; and (3) FSLIC Resolution Fund (FRF) receivership proceeds not needed for the Resolution Funding Corporation (REFCORP) Principal Fund.

Under section 21(f)(2), FICO assessments against SAIF members are to be made in the same manner as FDIC insurance assessments under section 7 of the FDI Act. The amount of the FICO assessment—together with any amount assessed by REFCORP under section 21B of the FHLB Act—must not exceed the insurance assessment amount authorized by section 7.<sup>4</sup> Section 21(f)(2) further provides that FICO "shall have first priority to make the assessment", and that the amount of the insurance assessment under section 7 is to be reduced by the amount of the FICO assessment. One important effect of the FICO assessment is to exacerbate any differential that may exist between BIF and SAIF assessment rates.

**IV. Problems Confronting the SAIF**

**A. Background: SAIF Assessment Rates**

As stated in the Board's proposal, in deciding against changes in the SAIF assessment rate, the Board has considered the SAIF's expected operating expenses, case resolution expenditures and income under a range of scenarios. The Board also has considered the effect of an increase in the assessment rate on SAIF members' earnings and capital. When first adopted, the assessment rate schedule yielded a weighted average rate of 25.9 basis points. With subsequent improvements in the industry and the migration of institutions to lower rates within the assessment matrix, the average rate has declined to 23.7 basis points (based on risk-based assessment categories as of July 1, 1995 and the assessment base as of March 31, 1995—see Table 2).

<sup>3</sup>Title III of CEBA, entitled the Federal Savings and Loan Insurance Corporation Recapitalization Act of 1987, directed the Federal Home Loan Bank Board to charter FICO for the purpose of financing the recapitalization of the FSLIC by purchasing FSLIC securities (and, subsequently, securities

issued by the FSLIC Resolution Fund as successor to FSLIC).

<sup>4</sup>The REFCORP Principal Fund is now fully funded and, accordingly, REFCORP's assessment authority has effectively terminated.

TABLE 2.—SAIF ASSESSMENT BASE DISTRIBUTION SUPERVISORY AND CAPITAL RATINGS IN EFFECT JULY 1, 1995 DEPOSITS AS OF MARCH 31, 1995 [In billions]

Capital group		Supervisory subgroup					
		A	A	B	B	C	C
Well Capitalized .....	Number .....	1,553	85.9%	138	7.6	25	1.4%
	Base .....	\$604.8	83.4%	\$58.0	8.0%	\$16.6	2.3%
Adequately Capitalized .....	Number .....	25	1.4%	31	1.7%	26	1.4%
	Base .....	\$17.4	2.4%	\$18.3	2.5%	\$6.9	1.0%
Under Capitalized .....	Number .....	0	0.0%	0	0.0%	10	0.6%
	Base .....	\$0.2	0.0%	\$0.0	0.0%	\$3.4	0.5%

“Number” reflects the number of SAIF members; “Base” reflects the SAIF-assessable deposits of SAIF members and of BIF-member Oakar banks.

The primary source of funds for the SAIF is assessment revenue from SAIF-member institutions. Since the creation of the fund and through the end of 1992, however, all assessments from SAIF-member institutions were diverted to other needs as required by FIRREA.<sup>5</sup> Only assessment revenue generated from BIF-member institutions that acquired SAIF-insured deposits under section 5(d)(3) of the FDI Act (12 U.S.C. 1815(d)(3)) (so-called “Oakar” banks) was deposited in the SAIF throughout this period.

**B. The SAIF is Significantly Undercapitalized**

SAIF-member assessment revenue began flowing into the SAIF on January 1, 1993. However, the FICO has a priority claim on SAIF-member assessments in order to service FICO bond obligations. Under existing statutory provisions, FICO has assessment authority through 2019, the maturity year of its last bond issuance. At a maximum of \$793 million per year, the FICO draw is substantial, and is expected to represent 45 percent of estimated assessment revenue for 1995, or 11 basis points of the average assessment rate of 23.7 basis points.<sup>6</sup> The SAIF had a balance of \$2.2 billion (unaudited) on March 31, 1995. With primary resolution responsibility residing with the Resolution Trust Corporation (RTC), there have been few demands on the SAIF. The SAIF assumed resolution responsibility for failed thrifts from the RTC on July 1, 1995, however. In addition to assessment revenue and investment income, there are other potential

sources of funds for the SAIF as follows. First, the FDIC has a \$30 billion line of credit available from the Department of the Treasury (Treasury) for deposit insurance purposes, which to date has not been utilized. FDI Act section 14(a). The SAIF would have to repay any amounts borrowed from the Treasury with premium revenues, however. The FDIC would have to provide the Treasury with a repayment schedule demonstrating that future premium revenue would be adequate to repay any amount borrowed plus interest. FDI Act section 14(c).

Next, the RTCCA authorized the appropriation of up to \$8 billion in Treasury funds to pay for losses incurred by the SAIF during fiscal years 1994 through 1998, to the extent of the availability of appropriated funds. In addition, at any time before the end of the 2-year period beginning on the date of the termination of the RTC, the Treasury is to provide out of funds appropriated to the RTC but not expended, such amounts as are needed by the SAIF and are not needed by the RTC. To obtain funds from either of these sources, however, certain certifications must be made to the Congress by the Chairman of the FDIC. FDI Act sections 11(a)(6)(D), (E) and (J). Among these, the Chairman must certify that the Board has determined that:

- (1) SAIF members are unable to pay additional semiannual assessments at the rates required to cover losses and to meet the repayment schedule for any amount borrowed from the Treasury for insurance purposes under the FDIC’s line of credit without adversely affecting the SAIF members’ ability to raise capital or to maintain the assessment base; and
- (2) An increase in assessment rates for SAIF members to cover losses or meet any repayment schedule could reasonably be expected to result in greater losses to the Government.

It may require extremely grave conditions in the thrift industry in order for the FDIC to certify that raising SAIF

assessments would result in increased losses to the Government. Moreover, these funds cannot be used to capitalize the fund—that is, to provide an insurance reserve, which was the original purpose of requiring a 1.25 reserve ratio.

The RTC’s resolution activities and the thrift industry’s substantial reduction of troubled assets in recent years have resulted in a relatively sound industry as the SAIF assumes resolution responsibility. However, with a balance of \$2.2 billion, the SAIF does not have a large cushion with which to absorb the costs of thrift failures. The FDIC has significantly reduced its projections of failed-thrift assets for 1995 and 1996, but the failure of a single large institution or several sizeable institutions or an economic downturn leading to higher than anticipated losses could render the fund insolvent. The FDIC’s loss projections for the SAIF are discussed in more detail below.

**C. Condition and Performance of SAIF-Member Institutions<sup>7</sup>**

During the first quarter of 1995, SAIF-member institutions continued to improve asset quality and posted improved, though modest, earnings. SAIF members had a return on assets of 0.64 percent in the first quarter, up from 0.55 percent in the fourth quarter and 0.40 percent in the first quarter of 1994, when a few of the largest thrifts incurred substantial restructuring charges. Earnings improvement over the fourth quarter was due to lower loss provisions (down 18 percent) and reduced noninterest expense (down 10 percent). This helped offset lower net interest income caused by a narrowing of the average net interest margin, which fell to 2.97 percent from 3.12 percent in the fourth quarter. Increased competition for deposits, particularly in the West Region, raised interest expense

<sup>7</sup> Excluding one RTC conservatorship and one self-liquidating savings institution.

<sup>5</sup> From 1989 through 1992, more than 90 percent of SAIF assessment revenue went to the FRF, the REFCORP and the FICO.

<sup>6</sup> The FICO has an annual call on up to the first \$793 million in SAIF assessments until the year 2017, with decreasing calls for two additional years thereafter. With interest credited for early payment, the actual annual draw is expected to approximate \$780 million.

by 6.5 percent over the fourth quarter, while interest income was up only 1.7 percent.

Asset quality continued to improve in the first quarter, as noncurrent loans fell 4.2 percent from year-end 1994 and 28 percent from the level of a year ago. The inventory of foreclosed real estate fell even further, down 7.3 percent during the first quarter and 40 percent over four quarters. Although loss reserves have declined slightly over the past year, the drop in noncurrent loans resulted in a coverage ratio of 84 cents for each dollar of noncurrent loans, about the same as in December and 10 cents higher than in March 1994. Most major balance sheet categories, including total assets, loans and deposits, showed small declines during the first three months of 1995, although equity capital grew slightly, raising the equity-to-assets ratio to 7.88 percent.

As of March 31, 1995, there were 1,806 members of the SAIF, including 1,731 savings institutions and 75 commercial banks. On this date, there were 58 SAIF-member "problem" institutions with total assets of \$32 billion, compared to 83 institutions with \$63 billion a year earlier. No SAIF members failed during the first quarter of 1995.

This discussion has focused on the improving condition of the SAIF-member thrift industry, but any such discussion must mention the relatively weak economic conditions still confronting a large segment of the industry. Eighteen percent of all SAIF-insured deposits are concentrated in the nation's eight largest thrift institutions, all of which operate predominantly in California. This state, in general, has lagged behind most of the nation in recovering from the most recent recession, and many California thrifts have significant exposure in the weakest areas of southern California. Additionally, a few large institutions have suffered low earnings and still have relatively high levels of risk in their loan portfolios. Consequently, despite the improving health of the thrift industry, the SAIF still faces significant risk relative to the fund's current reserve level.

#### D. Impact of a Premium Differential

In a separate rule-making on August 8, 1995, the Board adopted a final rule amending the FDIC's regulation on assessments to establish a new assessment rate schedule for institutions whose deposits are subject to assessment by the BIF. Under the new schedule, BIF assessment rates range from 4 to 31 basis points, compared to a range of 23 to 31 basis points under

the former BIF schedule and the current SAIF schedule. Lower BIF rates were adopted because the BIF is believed to have recapitalized during the second quarter of 1995. Largely due to the FICO obligation, the SAIF is not expected to capitalize until 2002 (this projection is discussed below), and SAIF assessment rates cannot be lowered below the statutory minimum of 18 basis points.

Under the current BIF and SAIF assessment rate schedules, average SAIF rates are likely to remain about 20 basis points higher than average BIF rates for the next seven years, until the SAIF is capitalized. After capitalization, SAIF rates would continue to be at least 11 basis points higher until the FICO bonds mature in 2017 to 2019, assuming the Board sets SAIF assessment rates to cover FICO's needs.

If BIF members pass along their assessment savings to their customers, SAIF members may be forced to pay more for deposits or charge less for loans to remain competitive. For SAIF members, this could result in reduced earnings and an impaired ability to raise funds in the capital markets. Among the weakest thrifts, a 20-basis point differential could result in competitive pressures that cause additional failures. An analysis of over a five-year time span suggests that any such increase in failures attributable to an average 20-basis point differential is likely to be sufficiently small as to be manageable by the SAIF under current interest-rate and asset-quality conditions. Moreover, the analysis indicates that under harsher than assumed interest-rate and asset-quality conditions, these economic factors would have a significantly greater effect on SAIF-member failure rates than would an average 20-basis point premium differential.

A separate analysis focused on BIF and SAIF members in the 3C assessment categories (undercapitalized/supervisory subgroup C) that will be paying 31 basis points. These weaker institutions will be competing with a large group of BIF members in category 1A (well capitalized/supervisory category A) that will be paying only 4 basis points. The analysis assumed that the 3C institutions would have to absorb the entire 27-basis point differential in the form of higher interest paid or lower interest earned. The result was that apart from institutions that have already been identified by the FDIC's supervisory staff as likely failures, the wider spread is likely to have a minimal impact in terms of additional failures.

Nevertheless, the Board recognizes that a premium differential between BIF- and SAIF-insured institutions is likely to increase competitive pressures

on thrifts and impede their ability to generate capital both internally and externally.<sup>8</sup>

#### E. Assessment Rate Spread

Under the SAIF assessment rate schedule there is a spread of 8 basis points, from 23 basis points for institutions in category 1A to 31 basis points for institutions in category 3C. Under the newly adopted BIF assessment schedule, the spread for BIF members was increased from 8 to 27 basis points. This was accomplished by dropping the minimum, most favorable rate from 23 to 4 basis points. Thus, the weakest BIF members will incur no additional deposit insurance cost. In order to apply a similar 27-basis point spread to SAIF members, it would be necessary to raise the highest SAIF assessment rate to 45 to 50 basis points, based on a lowest rate of 18 to 23 basis points. Because 86 percent of SAIF members would continue to pay the lowest rate, the revenue benefit of a 27-basis point spread would be limited. However, analysis indicates that SAIF assessments ranging to 50 basis points, creating a premium differential of as much as 46 basis points, would greatly increase the expenses of SAIF members and likely would result in significant additional failures. While the Board recognizes that a spread of more than 8 basis points would better serve the goals of a risk-related premium system, given the minimum average of 18 basis points currently prescribed by law, a wider spread could only be implemented by raising rates for all but the strongest SAIF members, which likely would have adverse consequences for an undercapitalized SAIF. For these reasons, the Board chose to retain an assessment rate spread of 8 basis points for members of the SAIF.

#### F. The Ability of the SAIF to Fund FICO

Under law, SAIF assessments paid by BIF-member Oakar banks are deposited in the SAIF and are not subject to FICO draws.<sup>9</sup>

Further, SAIF assessments paid by any former savings association that: (i) Has converted from a savings association charter to a bank charter, and (ii) remains a SAIF member in accordance with section 5(d)(2)(G) of the FDI Act (12 U.S.C. 1815(d)(2)(G)) (a

<sup>8</sup> See "The Condition of the BIF and the SAIF and Related Issues," Testimony of Ricki Helfer, Chairman, FDIC, before the Subcommittee on Financial Institutions and Consumer Credit, Committee on Banking and Financial Services, U.S. House of Representatives, Attachment C entitled "Analysis of Issues Confronting the Savings Association Insurance Fund," March 23, 1995.

<sup>9</sup> See Notice of FDIC General Counsel's Opinion No. 7, 60 FR 7055 (Feb. 6, 1995).

so-called "Sasser" bank), are likewise not subject to assessment by FICO.<sup>10</sup> On March 31, 1995, BIF-member Oakar

banks held 26.8 percent of the SAIF assessment base, and SAIF-member

Sasser banks held an additional 7.2 percent (see Table 3).

TABLE 3.—PERCENTAGE DISTRIBUTION OF THE SAIF ASSESSMENT BASE

	Available to FICO (per-cent)	Not available to FICO			Total (per-cent)
		Oakar (per-cent)	Sasser (per-cent)	Subtotal (percent)	
12/89 .....	99.8	0.2	0.0	0.2	100.0
12/90 .....	95.8	3.9	0.3	4.2	100.0
12/91 .....	89.9	8.7	1.5	10.1	100.0
12/92 .....	85.9	10.3	3.8	14.1	100.0
12/93 .....	74.7	19.4	5.9	25.3	100.0
12/94 .....	67.3	25.4	7.3	32.7	100.0
3/95 .....	66.0	26.8	7.2	34.0	100.0

While the pace of Oakar acquisitions slowed as RTC resolution activity wound down, Oakar acquisitions may continue and become an even greater proportion of the SAIF assessment base.<sup>11</sup> This has the potential result of the SAIF having insufficient assessments to cover the FICO obligation at current assessment levels. The rate of Sasser conversions is difficult to predict and is partially dependent on state laws, but any future conversions would also decrease the proportion of SAIF assessment revenues available to FICO.

In addition to the growth of the Oakar/Sasser portion of the SAIF assessment base, the ability of the SAIF to fund FICO interest payments will be adversely affected by an ongoing premium differential. A differential is likely to create powerful incentives for SAIF-insured institutions to minimize their premium costs by reducing their SAIF-assessable deposits.<sup>12</sup> This can be accomplished in a number of ways despite the current moratorium on the conversion of SAIF-insured deposits to BIF-insured deposits. SAIF-insured institutions could reduce their SAIF deposits by shifting their funding to nondeposit liabilities, such as Federal Home Loan Bank advances and reverse repurchase agreements. Institutions could also reduce their funding needs by securitizing assets or by changing business strategies, such as choosing to become a mortgage bank. Lastly, SAIF-insured institutions and their parent companies could structure affiliate relationships that would facilitate the migration of deposits from a SAIF-

insured institution to a BIF-insured affiliate. At least a dozen organizations have already filed applications seeking to establish such affiliate relationships.

If a competitive imbalance attributable to a premium differential materializes, that is, if BIF members pass along their savings to their customers, a rapid acceleration in the shrinkage of the SAIF assessment base could begin soon thereafter. With two insurance funds providing essentially the same product at significantly different prices, it must be expected that purchasers will seek the lower price. Attempts to control this behavior through legislation or regulation are likely to be ineffective and may only result in companies finding less efficient means. A result of the expected shrinkage of the SAIF assessment base could be a default on FICO bonds. At current assessment rates, a SAIF assessment base of \$328 billion is needed to generate sufficient assessment revenue to cover the FICO draw of up to \$793 million per year. The FICO-available base, which excludes Oakar and Sasser deposits, was \$478 billion on March 31, leaving a "cushion" of \$150 billion. This cushion could quickly be depleted if the strategies described above are successful, possibly causing a FICO default. A legislated reversal of the Oakar/Sasser exemption would only defer a FICO shortfall because the existence of a significant, prolonged premium differential is likely to result in continued erosion of the SAIF assessment base.

G. Failed-Asset Estimates for the SAIF

Among the factors that affect the ability of the SAIF to capitalize and to meet the FICO assessment are the number of thrift failures and the dollar amount of failed assets going forward.

Estimates of failed-institution assets are made by the FDIC's interdivisional Bank and Thrift Failure Working Group. In July 1995, the Working Group estimated failed thrift assets of \$100 million for the second half of 1995, \$2 billion for 1996 and \$2 billion for the first half of 1997. The estimate of \$100 million for the second half of 1995 represented a sharp decline from the \$3 billion estimated by the Working Group in November 1994. The \$2 billion estimate for 1996 was unchanged. In the estimation process, failed assets for the first twelve months of the two-year period are based on the FDIC's projected failure of specific institutions. Estimates for the second twelve months are derived from the FDIC's longer-term loss experience. For loss projections beyond mid-year 1997, the assumed failed-asset rate for the SAIF was 22 basis points, or about \$2 billion per year.

In the FDIC's projections, banks and thrifts were assumed to face similar longer-run loss experience. The BIF's historical average failed-asset rate from 1974 to 1994 was about 45 basis points. However, a lower failure rate than the recent historical experience of the BIF was assumed because the thrift industry is relatively sound following the RTC's removal of failing institutions from the system, and the health and performance of the remaining SAIF members has improved markedly. As of March 31,

<sup>10</sup> *Id.*

<sup>11</sup> SAIF-assessable deposits held by BIF-member Oakar banks will continue to grow at the same rate as the Oakar bank's overall deposit base. Under section 5(d)(3) of the FDI Act, as amended by the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA), such deposits are adjusted annually by the acquiring institution's

overall deposit growth rate (excluding the effects of mergers or acquisitions).

<sup>12</sup> "The Condition of the SAIF and Related Issues," Testimony of Ricki Helfer, Chairman, FDIC, before the Committee on Banking, Housing, and Urban Affairs, U.S. Senate, Attachment A entitled "The Immediacy of the Savings Association Insurance Fund Problem", July 28, 1995. "The

Condition of the SAIF and Related Issues," Testimony of Ricki Helfer, Chairman, FDIC, before the Subcommittee on Financial Institutions and Consumer Credit, Committee on Banking and Financial Services, U.S. House of Representatives, Attachment A entitled "The Immediacy of the Savings Association Insurance Fund Problem," August 2, 1995.

1995, 86 percent of all SAIF-member institutions were in the best risk classification of the FDIC's risk-related premium matrix.

One of the purposes of the FDICIA was to minimize losses to the insurance funds. FDICIA increased regulatory oversight and emphasized capital. Specifically, FDICIA requires the closing of failing institutions prior to the full depletion of their capital, limits riskier activities by institutions that are less than adequately capitalized, and establishes audit standards and statutory time frames for examinations. The law also requires the implementation of risk-related assessments, which have provided effective incentives for institutions to achieve and maintain the highest capital and supervisory standards. In light of these provisions, the high levels of thrift failures and insurance losses experienced over the past decade must be tempered when considering the industry's near-term future performance.

#### H. Projections for the SAIF

The FDIC currently projects that, under reasonably optimistic assumptions, the SAIF is not likely to reach the statutorily mandated DRR of 1.25 percent until 2002. Also, projections indicate the fund will not encounter problems meeting the FICO obligation through 2004. It is important to note that the baseline assumptions underlying these projections foresee shrinkage in the non-Oakar portion of the SAIF assessment base of 2 percent per year. If thrifts react aggressively to the premium differential and reduce their SAIF-assessable deposits, as discussed in Section IV.F, substantially greater shrinkage may occur. Under higher rates of shrinkage, the SAIF is likely to capitalize sooner than 2002 because a lower level of insured deposits would require a smaller fund to meet the DRR; however, FICO interest payments could soon be imperiled.

As stated earlier, the Board has the authority to reduce SAIF assessment rates to a minimum average of 18 basis points until January 1, 1998, at which time the average rate would rise to 23 basis points until capitalization occurs. Projections made under this scenario (and using the other baseline assumptions) indicate that the SAIF would capitalize in 2005, or three years later than under the existing rate schedule. Perhaps more importantly, reduction of the SAIF assessment rate to 18 basis points is expected to cause a FICO shortfall in 1996.

### Comment Summary

#### I. Comments Regarding SAIF Assessment Rates

##### A. General Comments

Approximately 111 commenters said that the SAIF rate should be decreased to 18 basis points; an additional 108 commenters urged that the differential between BIF members and SAIF members be limited to 5 basis points, regardless of the rates prescribed. With regard to the potential 19 basis point differential between BIF-members and SAIF-members, one large savings association stated:

Such a differential is significant in a narrow margin business such as home mortgage lending, which is the primary business of most SAIF members. This differential when leveraged at 20 to 1 will result in the BIF members producing 4 percent greater returns on equity than the SAIF members for the same business.

This savings association suggested that some SAIF members would try to overcome any disadvantage a differential may pose by reducing their costs, while others may attempt to increase revenue through potentially risky investments which could increase SAIF losses. Most commenters urging a reduction in SAIF rates were SAIF members.

Many commenters did not offer comments concerning the particular rate at which the minimum SAIF assessment rate should be set. Rather, the vast majority of SAIF-affiliated commenters simply commented that a disparity between SAIF rates and BIF rates would harm the thrift industry and asked that the premium differential be reduced or eliminated: "If disparity must exist, make it minimal". These comments are discussed in more detail later in this summary.

In contrast, approximately 67 commenters (64 BIF members, 2 SAIF members, 1 trade group, and 1 other) said that the SAIF assessment rate should not be decreased below the current minimum rate of 23 basis points. The following comment is typical of those who supported maintaining SAIF assessment rates at current levels: "[T]he current level of assessments \* \* \* has not posed problems for the capital or earnings of thrifts. Most thrifts are healthy today".

While expressing alarm as to the impending disparity, many SAIF-members did not specifically oppose the proposed reduction in BIF rates. For example, one large savings association stated: "[The savings association] supports the revised assessment schedule that is proposed for BIF

members but believes that the effect of the resulting substantial SAIF/BIF premium differential could overwhelm the currently healthy savings institutions and render the SAIF insolvent".

##### B. Impact of an Assessment Rate Differential

Comments from SAIF-insured institutions focused on the competitive disadvantage inherent in the proposed premium differential. Approximately 133 commenters argued that capital will flow away from savings associations if a disparity in the rates were permitted; over 300 argued that savings associations will be at a disadvantage competitively if rates were disparate; more than 90 commenters claimed that a disparity would mean fewer funds for home buyers. Over 80 commenters argued that a rate disparity would cause the SAIF assessment base to shrink. One thrift expressed its concerns as follows:

The impending disparity between BIF and SAIF deposit insurance premiums will bring about the gradual demise of the thrift industry. The significant competitive disadvantage to SAIF members will cause a natural migration of deposits to BIF-insured institutions and an erosion of the SAIF's premium assessment income. Lower profits will make it increasingly difficult for savings institutions to raise capital in the marketplace, eventually contributing to a rise in thrift failures. The SAIF will be faced with a dwindling deposit assessment base, fixed obligations to the FICO bond holders, and waning capitalization levels of its members.

\* \* \* \* \*

The thrift industry today is profitable, well-managed, and well-capitalized. It provides consumer and financial services in more than 12,500 offices nationwide, and it employs 217,600 people. Thrifts specialize in home financing and hold \$649 billion in mortgage loans and securities. The thrift industry plays an important role in the U.S. economy; it does not deserve the fate which awaits it if Congress does not promptly address the premium disparity issue.

Many thrifts compared the proposed premium disparity to an additional 15 percent tax on thrifts' earnings. One letter said the differential would raise the effective tax rate for savings associations to 60 percent, compared to about 30 percent for banks and zero for credit unions. Another stated that thrifts would be hurt because depositors are almost solely focused on yields and would not hesitate to move their funds if their savings institutions could not pay competitive interest rates on deposits.

Approximately 215 commenters argued that savings associations had a competitive advantage in the 1970s with the interest-rate advantage accorded

thrifts under Regulation Q. They indicated that banks had been able to survive in such an environment of disparate rates and that savings associations should also be able to survive. Under such a differential, thrifts "certainly did not get all of the deposit dollars and they certainly would not lose all of them now," stated one letter. Another claimed: "Nineteen basis points is hardly an unbridgeable competitive gulf." A state trade association for bankers agreed that the premium differential would undoubtedly cause some savings associations competitive problems, but noted that banks and savings associations already compete with a number of financial firms that do not currently pay deposit premiums and cited credit unions as an example. A number of other letters also downplayed the competitive disadvantage of a premium disparity by arguing that thrifts already compete with nondeposit competitors such as securities firms, mutual funds, mortgage bankers, insurance companies and finance companies that do not pay any deposit-insurance premium.

Of particular interest were those comments submitted by holding companies that control both BIF-member banks and SAIF-member thrifts, as well as comments submitted by institutions that were obligated to pay assessments to BIF and SAIF as a result of participating in a transaction pursuant to the so-called "Oakar" provisions (12 U.S.C. 1815(d)(3)). One holding company that owned both a BIF member and a SAIF member wrote:

To the extent that the rate differential is a Government imposed cost, there is a significant advantage to the bank and a real disadvantage to the thrift that has nothing to do with the way either the bank or the thrift handles its own business or cares for the customer. This will be the effect of the disparity of premium rates, resulting in fewer thrifts to pay insurance premiums, potential FICO bond defaults and, in the end, a more expensive solution will be imposed to resolve a crisis much larger than at present, and banks will be forced to participate in the expense of solving that problem. Therefore, if we want to talk fairness, this is where fairness begins and ends: it is not fair to anyone to impose a more expensive solution later when much less is needed if we act now and can offer a quid pro quo to the banks for their participation.

This holding company recommended that the Board champion legislation that would merge the funds but, at the same time, provide the banking industry with a quid pro quo for the additional cost that would be placed on it. It suggested that regulatory relief from the burdens of data gathering, retention and

reporting could provide significant savings to offset what would otherwise be deposit insurance premium savings. It also suggested that the remaining RTC funds be used to capitalize the SAIF.

A bank holding company that acquired failed thrifts from the RTC commented that a premium disparity would force its thrift to pay less interest to its depositors and/or increase the charge on borrowers, make it more difficult for its thrift to provide home loans or lend to small businesses, and threaten its thrift's ability to participate in low and moderate income housing programs. Another bank holding company with both bank and thrift subsidiaries commented that banks should not be forced to pay for FICO but that any remaining RTC funds should be used to reduce FICO obligations. Another such holding company suggested a 3-basis point surcharge on BIF members, dropping the SAIF rate to 15 basis points and merging the funds when SAIF became fully capitalized.

#### C. Need for Immediate Action

Many commenters suggested that if immediate steps were not taken to eliminate the impending disparity between SAIF and BIF rates, the ultimate cost to SAIF and FICO would be higher. One federally-chartered savings association wrote:

The shrinkage of the deposit base of savings institutions since FIRREA has already called into question whether the business can recapitalize itself given the tax being imposed by the FICO obligation. The creation of a significant premium disparity will bring about new and ever creative ways to avoid or reduce the impact of the high cost alternative. I do not believe that the premium disparity will wreak widespread destruction over the savings institution industry. It will, however, cause the business to disappear and hasten the day of reckoning for the SAIF.

A holding company stated:

We believe that leaving solutions to these problems for another day will be most harmful to both banks and thrifts and to the country as a whole and certainly more expensive to resolve than if the issues are faced now and resolved.

Many commenters suggested that if SAIF rates remained high, SAIF members would find other means to shift deposits out of SAIF. One holding company commented:

[We believe that a] solution needs to be found and implemented at once, that delay is costly in solving this problem and that delay encourages business to channel its talent and resources towards "artificial restructuring" such as Great Western's proposal (which makes business sense only because of the anticipated disparity in premium costs for deposit insurance), rather than towards true business reorganizations

that have lasting value to the business and our nation as a whole.

Approximately 293 institutions suggested that there was no immediate SAIF problem, implying that there was no urgent need to capitalize SAIF. For example, a trade association said: "[T]he S&L industry and SAIF are in much better shape than anyone could have imagined only two years ago. The S&L industry is profitable and increasingly well capitalized". It suggested that the SAIF situation be carefully monitored through Congressional oversight hearings and other mechanisms. One banker said: "If and when the SAIF fund is in jeopardy or the FICO payment cannot be made, call us". A few bankers suggested implementing the proposed assessments and waiting two years to see if, in fact, a differential materializes and whether it adversely impacts thrifts. However, it seems likely that some cost differential would materialize between banks and thrifts because, among bankers indicating a likely use for their premium savings, they most frequently mentioned paying higher interest on deposits and/or charging lower rates for loans. Other possible uses included augmenting capital to fund growth, technology updates and higher dividends to shareholders.

A few bankers saw it as inevitable that some of the cleanup costs borne by thrifts will be shifted to the banking industry. "My fellow bankers would probably hang me for even suggesting we pay," wrote one banker who recommended using excess RTC funds to reduce FICO by one-half, adding 1 or 2 basis points to the proposed BIF rates to be used toward FICO and leaving SAIF rates at current levels until FICO is paid and SAIF capitalized. Another banker offered to pay an additional 1½ to 2½ basis points toward SAIF and FICO if other financial service providers did the same. The taxation of credit unions was frequently mentioned as a potential source of funding.

A number of BIF-affiliated commenters noted that the Board should not take into account a potential differential between BIF and SAIF when setting BIF assessment rates. A large trade association for bankers noted, however, that the Board is permitted to consider the effect of SAIF assessments on the earnings and capital of thrift members.

## II. Suggested Legislative Initiatives

### A. Summary

As indicated above, SAIF members uniformly agreed that the impending disparity would harm their industry. Many commenters affiliated with SAIF-



members argued that the SAIF rate should be lowered to the statutory minimum average of 18 basis points, and others argued that the SAIF rate should be lowered to within 5 basis points of the BIF rates. A significant number of such commenters noted, however, that reducing or eliminating the disparity would not be a final solution, noting that FICO draws would continue to undermine SAIF. Some commenters predicted another insurance fund crisis which would "cause irreparable damage to the entire industry which already has lost significant market share to less regulated non-bank competitors". Many of these commenters urged legislative action. A thrift trade association wrote:

The [FDIC] is charged with the management of both BIF and SAIF and with the responsibility of seeing to it that neither fund becomes a burden on the taxpayers of America. For this reason, it is incumbent on the FDIC board to promptly recommend to the Congress a course of action that will mitigate the effects of the premium differential and achieve competitive parity between all insured institutions as soon as possible.

#### B. "Fairness" Arguments

In an apparent attempt to explain why SAIF members alone should not bear the burden of recapitalizing SAIF, approximately 159 commenters (10 BIF members, 134 SAIF members, 4 trade associations, and 11 other organizations/individuals) argued that savings associations in operation today were no more responsible than BIF members for the condition of SAIF. One holding company commented:

While none of the existing thrifts today caused the S&L crisis of the last decade any more than did the banks, the banks were promised premium relief once BIF was adequately capitalized at 1.25 percent. However, going forward, there is no moral issue about having deposit insurance available at the same rate to thrifts and to banks even though in the past failed thrifts cost much more than failed banks.

Some commenters criticized earlier legislative policy concerning SAIF funding. One trade association for bankers wrote:

In 1989 when SAIF was created, Congress authorized two types of supplemental funding from the Treasury—a backup funding for SAIF premiums and payments to maintain a minimum fund balance. The requirement under prior law was that the Treasury capitalize the SAIF at \$8.8 billion by fiscal 1999. Treasury never requested these authorized funds. The RTC Completion Act repealed this authorization. But it is important to note that in 1989, the government promised to contribute \$8.8 billion to the SAIF and then five years later

reversed itself. This is unfair to the thrift industry.

A thrift holding company added that FICO bonds were issued with non-callable provisions, which precluded refinancing of these obligations in the recent low interest rate environment. It argued: "We believe that this oversight in the FICO bond provisions and the lack of supplemental funding by the Treasury for the SAIF, support an argument that the recapitalization of the SAIF should be borne by the government and not SAIF members."

A large savings association referenced the additional payments from Treasury contemplated by FIRREA, and suggested that these "safety net payments" were intended to balance the additional burdens imposed on the thrift business by FIRREA (on top of the FICO burden imposed in 1987). It described these added burdens to be "confiscating the thrift industry's \$2.5 billion investment in the retained earnings of the Home Loan Banks, diverting an added \$3.1 billion in premiums to REFCORP and FRF, and requiring the Home Loan Banks each year to pay \$300 million in interest on REFCORP bonds." The savings association argued that if the original FIRREA payments had been carried out, the Treasury would have paid \$5.3 billion into SAIF over the five year period from fiscal year 1993 through fiscal year 1997 and the fund would have reached its reserve target of 1.25 percent in early 1998 based on FDIC assumptions regarding future losses and deposit growth.

Approximately 949 commenters (922 BIF members, 1 SAIF member, 12 trade associations, and 14 other organizations/individuals) stated as a general principle that the banking industry should not pay for SAIF problems. Bankers stated that they solved their own problem by recapitalizing the BIF and did not cause the problems now confronting the SAIF. They were adamant about not using BIF funds to capitalize or otherwise assist the SAIF even though this was not part of the assessment rate proposals. "The SAIF should paddle their own boat", commented one banker, which succinctly expressed the views of others that SAIF members should continue to pay higher premiums until their fund is capitalized.

Some bankers commented that banks and thrifts operate in separate industries, and there is no rationale for asking one to assist the other ("\* \* \* no different than asking a cow man to bail out a broke sheep farmer under the guise that both raise livestock"). Others see banks and thrifts as competitors in

the same industry and similarly see no reason to assist a competitor ("\* \* \* like asking General Motors to bail out Chrysler"). A few letters contended that the banking industry has already paid dearly for the savings and loan crisis of the 1980s through an increased regulatory burden. A number of bankers cited higher interest rates paid by thrifts with which they compete, and a few letters included newspaper clippings of advertisements placed by thrifts. "If they can afford to pay higher interest rates for deposits", wrote one banker, "they can afford to bear the burden to recapitalize SAIF".

Thrifts countered along the following lines: "The simple fact is today's thrift institutions are now being punished for the savings and loan cleanup of the 1980s. While this may be emotionally gratifying for some, it makes little sense from an economic perspective".

#### C. Use of RTC Funds

Over 250 commenters (179 BIF members, 60 SAIF members, 9 trade associations, and 8 other organizations/individuals) urged that RTC funds be made available to SAIF for capitalization purposes; over 90 (9 BIF members, 65 SAIF members, 9 trade associations, and 9 organizations/individuals) urged that the RTC funds be made available to SAIF on a contingent basis to rescue SAIF from future losses.

The solution most frequently recommended by thrifts (and their primary trade group) involved having the FICO burden shared proportionately by BIF and SAIF, using excess RTC funds to cover losses in institutions identified as problems as of year-end 1997 and reducing the SAIF differential to 5 basis points until the SAIF is capitalized. These measures would require Congressional action, but as an interim measure, the FDIC was urged to reduce the SAIF premium to 18 basis points, the minimum average SAIF rate allowed under current law. Variations on this proposal included lowering the DRR to 1 percent, although a few writers asked that this ratio be raised to as high as 1.50 percent for BIF and SAIF.

#### D. One-time Special Assessment Against SAIF Members

Approximately 11 BIF members and 10 SAIF members, as well as 2 trade groups, urged that a one-time assessment be imposed against SAIF members. In opposition to such a proposal, one large thrift holding company asserted that the thrift industry had already paid sufficient deposit premiums since FIRREA to have capitalized the SAIF but of the \$9.5

billion in premiums paid, only \$2.4 billion went into SAIF. It argued: "Any substantial up front assessment on thrifts is not only unfair, it is counterproductive in the sense that it could precipitate even greater losses to the insurance fund". At the same time, however, it indicated that if its preferred method of recapitalizing SAIF—using RTC funds—proved insufficient to reach the 1.25 percent ratio, a variety of means might be considered to fill the gap, including the use of borrowed funds, a "one-time assessment or a temporarily higher premium". It stated that such methods would have to be structured so as to minimize the impact on the earning capacity of the thrift business.<sup>13</sup>

#### E. Merge the BIF and the SAIF

Merging the BIF and the SAIF was frequently suggested (approximately 121 commenters, including approximately 6 trade groups) and was seen by some as inevitable and possibly less expensive today than "four or five years down the road". As one thrift executive wrote: "The consumer views deposit insurance as coming from one source—backed by the U.S. Government". A state trade association representing thrifts supported the merging of the two funds "as the only solution that will assure that all institutions of equal risk profiles will pay the same premium for federal deposit insurance".<sup>14</sup>

One thrift holding company supporting merger of the funds if the remaining RTC funds were not available submitted the following comment:

The original distinction between commercial banks and savings institutions has significantly blurred over the last decade \* \* \*. In addition, most, if not all, of the tax and regulatory "advantages" which benefitted savings institutions in the past have been eliminated or significantly curtailed. Likewise, the Federal Home Loan Bank system, which was an exclusive province of savings institutions, is now being embraced as a significant competitive benefit by an increasing number of commercial banks. Any portion of a weakened federal deposit insurance fund will have adverse consequences on the entire banking industry in the public's perception.

Another thrift urged that the funds be merged with the FICO interest

<sup>13</sup> In conjunction with this proposal, it suggested that RTC be extended for two years to cover any failures of thrifts currently under its supervisory watch.

<sup>14</sup> In light of the political sensitivity to such a merger, this trade association wrote that it could support a package of changes which contained all of the following: (1) A sharing of the FICO obligation proportionately between BIF and SAIF; (2) Use of excess RTC funds as a backstop against near-term losses; and (3) A reasonable SAIF premium differential to be paid until such time as the SAIF reaches the mandated reserve ratio.

obligations to be borne by the new fund as a whole and noted:

Effecting this merger will enable the government to keep its promise to the American people and will avoid using taxpayer funds either to capitalize the SAIF today, or to bail it out several years from now. If deposit insurance premiums for both banks and thrifts were kept at their current levels, a combined fund could reach full capitalization at 1.25% within approximately 20 months after the merger \* \* \*. Thus banks and thrifts would experience very little delay in seeing their premiums reduced.

A California savings association argued that even after SAIF is fully capitalized, the fund would be unsound because the SAIF has too much geographic concentration in California. It urged that the funds be merged to generate sufficient geographic spread.

Some suggested that SAIF members could pay a one-time assessment (80 basis points was mentioned) to capitalize the SAIF prior to a merger of the funds. The premium differential could then be reduced to 5 basis points or less or eliminated altogether. A savings banker suggested that thrifts be allowed to record the special assessment as a credit against the tax bad debt reserve in order to lessen the immediate impact on tax revenues. A variety of writers, including banks, thrifts and an industry watchdog group, questioned the need for a separate thrift charter once the funds have been merged.

Over 775 commenters, including approximately 10 trade groups, argued against a merger of the insurance funds. Many of those opposing a merger of the funds essentially argued that the banking industry should not be required to participate in an economic solution which would benefit their competition. For example, a state trade association representing banks argued that "for decades S&Ls enjoyed a lax regulatory environment, significant tax breaks, and a mandated competitive advantage". It said: "Asking banks to shoulder the bailout burden of a key competitor because a long time competitive advantage will be reversed is unfair and inappropriate, particularly when banks are not responsible for the problems of the thrifts".

One large trade association opposing a merger of the funds wrote: "The looming premium differential will prompt thrifts to continue to look for loopholes to leave SAIF, further exacerbating the SAIF/FICO problem. However, merging the funds or delaying the banks' premium reduction is not the answer". This trade association expressed support for using the remaining authorized and appropriated funds for the RTC to capitalize the SAIF

and/or defease the FICO bond obligation. It suggested various ways to use the remaining RTC monies for SAIF/FICO, such as: (1) Transferring the remaining RTC funds to SAIF, leaving the principle intact, but investing the funds so as to generate sufficient interest earnings to pay FICO bond interest of up to \$793 million; (2) using the remaining RTC funds to capitalize SAIF, which they claimed would leave ample funds to address the FICO problem; (3) using the RTC funds only to defease the FICO obligation thereby enabling SAIF to capitalize at the current assessment rates by 1998.

#### F. FICO Issues

Over 200 commenters urged that BIF members share in FICO assessments, with the majority of these urging that BIF members share proportionately. Over 200 commenters urged that RTC funds be used to defease FICO and a few commenters urged that the \$8 billion from RTCCA be used as well. Over 70 commenters urged that premiums paid by Oakar and Sasser institutions should be used for FICO bond interest payments. It was recognized, however, that such a change in the law would be of limited benefit to SAIF. A large banking trade group commented:

Using Oakar and Sasser premiums for FICO bond interest, however, would slow the recapitalization of the SAIF. To address this problem, the Congress could also extend the recapitalization schedule of SAIF, giving FDIC more leeway to reduce SAIF premiums.

One large thrift suggested that if the FICO burden were spread over all SAIF and BIF members equally, the cost would be approximately 2 basis points per institution. It suggested that bank deposit premiums should not be increased to absorb such an additional cost. Rather, the FICO charge should be deducted from any BIF premium paid. In contrast, a bank trade group argued: "Such payments would merely protect FICO bondholders. \* \* \* Tapping BIF funds for uses other than protection of BIF depositors would set a very dangerous precedent".

#### G. Other Approaches

Other recommended alternatives included reducing BIF rates to 15 basis points and putting the excess assessment in a "secondary reserve" account, such as existed under FSLIC at one time, which would pay interest to BIF members but would also be used to defray SAIF expenses; transferring the net worth of mutual thrifts to SAIF; and merging the SAIF with the credit union insurance fund.

### III. Miscellaneous Comments

#### A. Spread From 23 Basis Points to 31 Basis Points

The Board received few comments in response to its question as to whether the current spread of 8 basis points from the lowest to the highest assessment rates should be retained for SAIF members.

#### B. Transactions Which Would Have the Effect of Allowing Deposits to Shift From One Insurance Fund to the Other

Over 300 BIF-member institutions and 6 trade associations commented that steps should be taken to prohibit transactions which would have the effect of allowing deposits to shift from the SAIF to the BIF, thereby depleting the SAIF. Approximately 42 BIF-member institutions stated that exit and entrance fees should be assessed against transactions which would have the effect of allowing deposits to shift from the SAIF to the BIF (assuming that such transactions were not otherwise subject to exit and entrance fees). A bank trade group commented that, among other options for recapitalizing SAIF, policy makers should consider prohibiting thrifts from chartering banks for the purpose of exiting SAIF; declaring such institutions to be Sasser institutions that remain SAIF-insured; or requiring such institutions to pay the equivalent of exit/entrance fees and continue contributing to FICO.

Thrifts and their trade associations, however, noted that when significant costs are involved on an ongoing basis, institutions and their advisors would spend their time, energy and talent to find ways to avoid these ongoing costs and noted that this could leave Oakar banks and slow-moving thrifts without any relief. They suggested that methods already existed whereby depositors at a thrift could be encouraged to move their deposits to an existing bank affiliate while the thrift would service the deposits (*i.e.*, agent branches).

#### C. Comments Regarding Oakar Transactions

Seven BIF-members contended that the SAIF-assessable deposits held by BIF-member Oakar banks should be assessed at a lower rate than that imposed against SAIF member institutions (apparently to reflect the fact that FICO's assessment authority does not extend to such banks). Other commenters want banks and holding companies that acquired SAIF-insured institutions, and thereby benefited from the savings and loan bailout to continue to be liable to SAIF (although this is already the case because these acquirers

pay SAIF premiums on the acquired deposits).

#### Adoption of Final Rule

As indicated above, the FDIC has determined to retain the existing assessment rate schedule applicable to members of the SAIF. The Board fully understands and appreciates the concerns raised in the comment letters concerning the impending rate differential. Most of the solutions suggested by SAIF-affiliated commenters require Congressional action, however, and are beyond the scope of this rulemaking procedure. Nonetheless, the FDIC agrees with these commenters that the difficulties facing the SAIF can only be addressed comprehensively through Congressional action. Therefore, after extensive analysis of the relevant issues, the FDIC has informed Congress of the FDIC's strong support for a proposal developed on an interagency basis for resolving the problems of the SAIF.<sup>15</sup>

The proposal has three components to address the immediate, pressing financial problems of the SAIF: (1) The SAIF would be capitalized through a special up-front cash assessment on SAIF deposits; (2) the responsibility for the FICO payments would be spread proportionally over all FDIC-insured institutions; and (3) the BIF and the SAIF would be merged as soon as practicable, after a number of additional issues related to the merger are resolved. In addition to the three components of the proposal, the FDIC and the Office of Thrift Supervision also recommend making unspent RTC funds available as a kind of reinsurance policy against extraordinary, unanticipated SAIF losses to limit the potential future costs to taxpayers from the existing full faith and credit guarantee of the U.S. Government that the SAIF enjoys. This proposal is further explained in the Testimony of Ricki Helfer, Chairman, FDIC, on The Condition of the SAIF and Related Issues, before the Committee on Banking, Housing, and Urban Affairs, U.S. Senate, July 28, 1995, and before the Subcommittee on Financial Institutions and Consumer Credit, Committee on Banking and Financial Services, U.S. House of Representatives, August 2, 1995. The proposal is consistent with many of the suggestions

<sup>15</sup>The Condition of the SAIF and Related Issues, Testimony of Ricki Helfer, Chairman, FDIC, before the Committee on Banking, Housing, and Urban Affairs, U.S. Senate, July 28, 1995. The Condition of the SAIF and Related Issues, Testimony of Ricki Helfer, Chairman, FDIC, before the Subcommittee on Financial Institutions and Consumer Credit, Committee on Banking and Financial Services, U.S. House of Representatives, August 2, 1995.

made by commenters in response to this final rule.

The FDIC further recognizes that a differential is likely to increase competitive pressures and impede thrifts' ability to generate capital both internally and externally. At this time, however, the FDIC must decline to reduce the minimum average SAIF assessment rate to 18 basis points. As detailed in Sections II and IV above, the SAIF is grossly undercapitalized. At the end of the first quarter of 1995, the SAIF had a balance of \$2.2 billion, or only 0.31 percent of insured deposits. That balance was less than 7 percent of the assets of SAIF-insured "problem" institutions. At the current pace, and under reasonably optimistic assumptions, the SAIF is unlikely to reach the minimum reserve ratio of 1.25 percent until the year 2002. Even though the SAIF is grossly undercapitalized, a sizable portion of the SAIF's ongoing assessments is, by law, diverted to meet interest payments on obligations of the FICO. On July 1 the SAIF assumed responsibility from the RTC for paying the costs arising from any new failures of thrift institutions. These problems are exacerbated by several additional factors, including the shrinkage of the SAIF assessment base since the SAIF was created in 1989. Given the fund's relatively low balance and the transfer of resolution authority from the RTC to the SAIF on July 1, the FDIC believes that the SAIF must be built as quickly as possible to its mandated reserve level.

Having determined not to reduce the SAIF rate to the statutory minimum average of 18 basis points, one other way to maintain parity between SAIF members and BIF members would be to retain the BIF assessment rate schedule at 23-31 basis points. Few SAIF-affiliated commenters specifically urged such action, however. In contrast to the SAIF, the \$23.2 billion BIF balance at the end of the first quarter was 1.22 percent of BIF-insured deposits and 70 percent of the assets of BIF-insured "problem" institutions. The BIF probably reached the 1.25 minimum reserve ratio during the second quarter of this year, although the FDIC cannot confirm this fact until the Call Reports for the second quarter have been received and analyzed. For the reasons set forth in the BIF rule published elsewhere in this **Federal Register**, the FDIC has determined to establish a new assessment rate schedule of 4 to 31 basis points for BIF members.

#### 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.

**Regulatory Flexibility Analysis**

The Board hereby certifies that the final 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 final 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 final rule. Therefore, the provisions of that Act regarding an initial and final regulatory flexibility analysis (*Id.* at 603 and 604) do not apply here.

**Riegle Community Development and Regulatory Improvement Act of 1994**

Section 302(b) of the Riegle Community Development and Regulatory Improvement Act of 1994 (RCDRIA), 12 U.S.C. 4802(b), requires that all new regulations and amendments to regulations prescribed by a Federal banking agency which impose additional reporting, disclosures, or other new requirements

on insured depository institutions shall take effect on the first day of a calendar quarter. This provision was designed to assist institutions by establishing a consistent date for complying with new regulations so that institutions would be more regularly informed of new rules and be able to effectuate necessary training, software, and other operational modifications in an orderly manner. However, this final rule does not impose such additional or new regulatory requirements, rather it retains the existing assessment rate schedule for SAIF-member institutions. The FDIC has therefore determined that section 302 of RCDRIA does not apply to this final rule.

**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, a portion of part 327 of title 12 of the Code of Federal Regulations is republished as set forth below:

**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 (d)(1) of § 327.9 as redesignated from paragraph (c)(1) elsewhere in this issue of the **Federal**

**Register** is republished for the convenience of the reader as set forth below:

**§ 327.9 Assessment rate schedules.**

\* \* \* \* \*

(d) *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 sub-group		
	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 8th day of August, 1995.  
 Federal Deposit Insurance Corporation.  
**Jerry L. Langley,**  
*Executive Secretary.*  
 [FR Doc. 95–20172 Filed 8–15–95; 8:45 am]  
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