



### **CBAI's Case for Changing the FDIC Assessment Method**

On February 27, 2009, FDIC Chairman Sheila Bair stunned the banking world when she announced that the FDIC approved a plan to assess banks 20 cents per \$100 of domestic deposits this summer and, if needed, an additional 10 basis points this fall to replenish the deposit insurance fund (DIF).

At the urging of both CBAI and ICBA, outraged community bankers sent thousands of letters to the FDIC and members of Congress explaining how the assessment would devastate bank earnings, reduce financial support for the communities they serve, and undermine efforts to revive a flagging economy. Community bankers also objected to paying for the sins of Wall Street.

Chairman Bair addressed the assessment issue during the ICBA Convention in March. She made it clear that she understands community banker frustration with a financial crisis that community banks did not create. She acknowledged that the FDIC must come up with a better method of assessing insurance premiums, one that prices for risk. She concluded that steps must be taken to mitigate the systemic risk posed by "too big to fail" banks. It was music to our ears! She received thunderous applause from community bankers who welcomed the fact that someone from Washington had not forgotten them.

### **Debate over fairness**

Meanwhile, there has been considerable debate concerning how to fairly assess FDIC-insured institutions, and by late May the FDIC is expected to announce its final plan to replenish the DIF. Based on quotes from representatives of the big-bank groups, fairness is indeed in the eyes of the beholder.

ICBA and CBAI have urged the FDIC board to base assessments on total assets less tangible capital which would reduce the assessments for nearly all community banks and increase the assessments for the largest banks that caused the current financial and economic crisis. The ABA and its state affiliates, however, won't support this position. Instead, they want the FDIC to borrow to replenish the DIF. However, banks would still have to repay the debt with interest. Furthermore, the current assessment method unfairly burdens community banks with a disproportionate share of the cost. Statistical analyses support this position.

According to ICBA research, the ratio of domestic deposits to assets for community banks of less than \$1 billion in assets is about 79%, compared to just 47% for the nation's largest banks. To add perspective, ICBA's 5,000 members collectively hold \$1 trillion in assets, more than \$800 billion in deposits, and \$700 billion in loans. The nation's three largest banks total about \$5 trillion in assets. Deposits don't fail; bad assets are the root cause of most failures. Changing the assessment method from deposits to assets would result in fairer assessments that more accurately reflect institutional risk to the DIF. Additionally, banks should not be penalized for being well-capitalized, so the assessment should be based on assets minus tangible capital.

## How would assessing banks based on assets minus tangible capital affect assessments?

According to the ICBA study, 6,122 banks or 99.98% of banks with less than \$1 billion in assets would pay 10.59% of the total assessment if based on assets less tangible capital, compared to 16.13% if based on domestic deposits. The table below shows the share of the assessment that would be paid by different asset sizes under various assessment methods:

**Share of Assessments Paid by Asset Size**

Assessment Base	Less than \$1B	\$1B to \$10B	\$10B to \$100B	\$100BPlus
Domestic Deposits	16.13%	14.31%	20.84%	48.73%
Total Deposits	13.36%	11.98%	18.61%	56.05%
Assets	10.99%	10.82%	19.32%	58.87%
Assets Less Tangible Capital	10.59%	10.55%	19.19%	59.68%
Total Liabilities	10.87%	10.66%	19.30%	59.17%

*If the special assessment is based on assets minus tangible capital, ICBA calculates that a bank with a ratio of domestic deposits to assets of 58% would break even under both proposals. Since less than 2% of banks under \$1 billion in assets have a domestic deposits-to-assets ratio of 58% or less, the vast majority of community banks would pay a smaller share of the assessment under this proposal. **For banks with less than \$1 billion in assets, ICBA estimates that using assets-minus-tangible capital as the assessment base would save nearly \$1 billion in aggregate.***

It's easy to understand why the nation's largest banks, and their advocates, have not embraced the assets minus tangible capital method of assessing FDIC premiums. Doing so would shift the burden of funding DIF from community banks to the nation's largest banks.

CBAI has voiced its position to the FDIC and the Illinois congressional delegation. An adverse decision may reduce community bank earnings for years. The FDIC is scheduled to reach a final decision on the proposed special assessment on Friday, May 22.