Financial Institutions Group

Federal Deposit Insurance Reform

Earlier this year, Congress enacted the Federal Deposit Insurance Reform Act[1] (the Reform Act), which calls for significant changes to the federal deposit insurance framework. The Reform Act represents the culmination of nearly a decade of work by Congress, industry, the Federal Deposit Insurance Corporation (FDIC) and other banking agencies to renew and reform the deposit insurance system.

These changes will affect insured depository institutions and permit the FDIC to exercise greater authority and more discretion in how it operates the deposit insurance system. The most important changes from the Reform Act and the FDIC's implementing regulations to date include:

- Merging the Bank Insurance Fund (BIF) and the Savings Association Insurance Fund (SAIF) into a new fund, the Deposit Insurance Fund (DIF)
- Granting a one-time assessment credit totaling $4.7 billion to insured depository institutions that paid into the BIF and SAIF during the 1990s
- Increasing deposit insurance coverage to $250,000 for certain retirement accounts
- Providing that general deposit insurance coverage be indexed to inflation
- Creating a new risk-based assessment system that would distinguish among large, small and new institutions, and prescribing new procedural requirements for setting insurance assessments
- Permitting the FDIC Board of Directors (FDIC Board) to manage the insurance reserve ratio within an established range, rather than using a fixed statutory reserve ratio
- Providing for the distribution of dividends to be paid to insured depository institutions if the reserve ratio exceeds a certain level
- Providing for DIF restoration plans when the reserve ratio falls below the minimum designated reserve ratio

The Reform Act also requires the FDIC to prescribe implementing regulations by the November 5, 2006, statutory deadline. To date, the FDIC has proposed or finalized regulations in a number of areas, including rules on the one-time assessment credit, increased insurance coverage for employee benefits accounts, the new risk-based assessment system, the designated reserve ratio and the payment of dividends. Each of these regulations is discussed in further detail below.

Formation of the Deposit Insurance Fund

Prior to passage of the Reform Act, the FDIC utilized two separate insurance funds to insure banks and thrifts: the BIF and the SAIF, respectively. The two insurance funds were created by the Financial Institutions Reform, Recovery and Enforcement Act of 1989 (FIRREA)[2] in reaction to the threat to the insurance fund from the insolvency crisis in the savings and loan industry.

Over time, the rationale for maintaining two separate insurance funds has eroded. Banks and thrifts have become more similar to each other in their risk profiles and activities. The BIF and the SAIF have effectively come to provide nearly identical insurance coverage. As the number of thrifts has declined due to consolidation, the threat posed by the failure of these institutions to the insurance fund has lessened. But, the SAIF has also become smaller as fewer institutions contribute to it, making it more vulnerable to fund insolvency.

Accordingly, the Reform Act required the merger of the BIF and the SAIF into a new single fund, the DIF, which would insure both banks and thrifts collectively. The FDIC effectuated the merger on March 31, 2006.[3] The newly created DIF ended the first quarter of 2006 with a fund balance of $49.2 billion. This balance reflects an increase of approximately 1.2%, compared to the combined BIF and SAIF balances of $48.6 billion, as of December 31, 2005.[4]

Allocation of One-Time Assessment Credit to Certain Insured Depository Institutions

Under the Act, the FDIC is required to allocate a one-time assessment credit totaling approximately $4.7 billion among insured institutions to reflect the contributions they made to the BIF and the SAIF in the 1990s. [5] The one-time assessment credit will be allocated to each "eligible insured depository institution" based on the assessment base of the institution as of December 31, 1996. An "eligible insured depository institution" is defined by statute as an insured depository institution that "(i) was in existence on December 31, 1996, and paid a deposit insurance assessment prior to that date; or (ii) is a successor to any insured depository institution." The statute does not define "successor," but instead delegates that responsibility to the FDIC under its rulemaking authority, as discussed below.

The Reform Act provides that the one-time assessment credit shall be automatically applied to future assessments imposed on an institution with some limitations on the applicability of this credit. First, the credit may offset 100% of an institution's assessments due for 2007. However, in fiscal years 2008, 2009 and 2010, the credit may offset up to only 90% of the assessments that become due for those years. Furthermore, for institutions that exhibit financial, operational or compliance weaknesses ranging from moderately severe to unsatisfactory, or are not adequately capitalized,[6] the amount of any credit due may not exceed the average assessment rate of all institutions.

Proposed Rule–One-Time Assessment Credit

On May 18, 2006, the FDIC published for notice and comment a proposed rule that establishes the aggregate amount of the one-time credit, the institutions eligible to receive credits, the amount of each eligible institution's credit, and the qualifications and procedures governing the application of assessment credits.[7] Institutions may calculate their estimated one-time assessment credit with the assistance of a calculator on the FDIC website.[8]

One aspect of the proposed rule that has generated attention is the FDIC's definition of "successor," which the FDIC proposed to define as the resulting institution in a merger or consolidation involving an institution that was eligible for the one-time credit. The FDIC views this definition as being operationally viable and most consistent with the purpose of the one-time assessment credit, which is to recognize the contributions made by some insured depository institutions to capitalize the insurance funds.

Importantly, the FDIC requested comments on alternative definitions of "successor." First, drawing from traditional principles of corporate law, the FDIC invited comments on whether to include *de facto* merger transactions in the definition. For example, a *de facto* merger could be defined as "an eligible institution conveying all of its deposit liabilities and substantially all of its assets to a single acquiring institution, so long as the conveying institution subsequently terminated its deposit insurance."[9] While this definition would encompass a greater number of institutions that may be eligible for the credit, it also departs from the bright-line rule that a strict merger or consolidation rule would provide.

The FDIC has also solicited comment on whether the definition of successor should "follow the deposits," regardless of the means by which they were transferred. Under this approach, the FDIC may take into account the sale or transfer of deposits, and the credit may be applied on a pro rata basis or may be split between the parties to the deposit transfer transaction. However, one aspect that may make the "follow the deposits" approach unworkable and unfair is the absence of reliable data, as the FDIC does not routinely maintain detailed data on all deposit transfer transactions that would seem to be necessary to implement this system. Instead, information would have to be collected from the industry. Considering the passage of time and the consolidation of the industry, records may not have been retained, and institutions that saved their records would have a significant advantage over those that did not. Furthermore, if there was a chain of mergers and consolidations for a certain set of deposits, resolving one institution's credit may first require lengthy analysis and examination of other claims in the chain.

In some cases, there may not be a successor to an institution that is eligible for a credit. For example, if an otherwise eligible institution failed without a successor after December 31, 1996, but before the issuance of the final one-time assessment credit rule, that institution would not be eligible to receive a credit. In this situation where there is

no successor identified, the proposal states that the failed institution's credit would be redistributed among the eligible institutions.

Deposit Insurance Coverage Increased

Section 2103 of the Reform Act contains a number of provisions that increase deposit insurance coverage. Specifically, these provisions tie deposit insurance coverage to inflation, provide pass-through insurance for employee benefit plans and increase deposit insurance coverage for certain retirement accounts. Interim rules implementing these provisions were published on March 23, 2006, and became effective April 1, 2006.[10] A final rule was also published on September 12, 2006. [11]

First, Section 2103(a) establishes a new "standard maximum deposit insurance amount" that is tied to inflation. The statute provides that deposit insurance coverage will continue to be set at $100,000, but may be adjusted for inflation after March 10, 2010, and in five-year increments thereafter. The boards of directors for the FDIC and National Credit Union Administration (NCUA) are granted authority to jointly consider whether an adjustment is necessary. They are required to consider a number of statutory factors, including the overall state of the DIF and economic conditions affecting insured depository institutions, potential problems affecting the DIF, and whether an increase in coverage will cause the reserve ratio of the DIF to drop below 1.15% of estimated insured deposits. If the boards determine that an adjustment is necessary, then they will calculate a new standard maximum deposit insurance amount based on the product of $100,000 and a Personal Consumption Expenditures Chain-type Price Index published by the Department of Commerce for that year. Any new standard maximum deposit insurance amount would be published in the Federal Register and reported to Congress, and take effect on January 1 of the following calendar year.

Section 2103(b) provides pass-through insurance coverage for the deposits of any employee benefit plan. Prior to the passage of the Reform Act, the deposits of participants in employee benefit plans were generally insured on a pro-rata basis based on the interests of each participant in the plan, unless the institution holding the deposits was not permitted to accept brokered deposits. Pass-through insurance coverage was available in such cases only if the institution satisfied applicable capital standards and had notified the depositor that coverage was available at the time of accepting the deposits. The Reform Act simplifies this regime by providing pass-through coverage for deposits of any employee benefit plan and permitting only well- or adequately capitalized institutions to accept such deposits.[12]

The Reform Act also increased deposit insurance coverage for certain retirement accounts from $100,000 to $250,000, with adjustments for inflation over time. The types of accounts subject to this increase in coverage include individual retirement accounts, eligible deferred compensation plan accounts and individual account plan accounts of the Employee Retirement Income Security Act, as well as any plan described in section 401(d) of the Internal Revenue Code.[13] However, accounts such as Coverdell education savings accounts, health and medical savings accounts, and accounts established under section 403(b) of the Internal Revenue Code are not eligible to receive increased insurance coverage.[14]

In response to the increase in deposit insurance coverage for certain retirement accounts, the federal banking agencies have changed certain deposit-related reporting revisions for the June 30 and subsequent 2006 Call Reports.[15] These revisions affect the reporting of the number and amount of deposit accounts, fully insured brokered deposits and, for banks with $1 billion or more in total assets, the estimated amount of uninsured deposits.

New Ways of Setting Insurance Assessments

The Reform Act and the FDIC's proposed rules modify the way insurance assessments are established by creating a new risk-based assessment system that distinguishes among large, small and new institutions. Furthermore, the Reform Act and the proposed rules prescribe a number of changes related to the procedures governing insurance assessments, including amended recordkeeping requirements for insured depository institutions, increased penalties for late or unpaid assessments, and a statute of limitations for claims arising out of overpayment or underpayment of assessments.[16]

Risk-Based Assessments for Large, Small and New Institutions

Under the statute, the FDIC Board has discretion to set insurance assessments in amounts it determines to be necessary and appropriate, as long as it does not exclude large banks from the lowest risk-based assessment category solely because of size. The statute also sets forth a list of factors that the FDIC Board must consider when setting assessments, including estimated operating expenses of the DIF, estimated case resolution expenses and income of the

DIF, projected effects of payment of assessments on capital and earnings of insured depository institutions, risk factors, and other factors the FDIC board deems appropriate.

Proposed Rule–Risk-Based Assessment System

In the past, the FDIC has been prohibited from charging assessments to well-managed and well-capitalized institutions when the DIF is at or above the designated reserve ratio. However, the Reform Act eliminated this prohibition and granted to the FDIC Board the discretion to price deposit insurance according to risk for all insured institutions regardless of the level of the fund reserve ratio. Accordingly, on July 24, 2006, the FDIC published a proposed rule that would restructure the current risk-based assessment system by improving risk differentiation among institutions and making the system more sensitive to risk.[17] Specifically, the rule proposes to create different risk-based assessment frameworks for smaller and larger institutions that are well capitalized and well managed, establish a common risk framework for all other insured institutions and establish a base assessment rate schedule. The FDIC also developed an assessment rate calculator for well-capitalized and well-managed institutions that provides estimates of assessment rates under the new risk-based assessment system.[18]

Under the current system, an institution's assessment rate depends upon its "risk category"—one of nine different risk classifications that takes into account both capital levels and supervisory ratings. First, an institution is placed into one of three capital groups: "1" if well capitalized, "2" if adequately capitalized and "3" if undercapitalized. Second, an institution is placed into one of three supervisory subgroups—labeled A, B and C—based generally on the institution's CAMELS rating. Subgroup A consists of financially sound institutions with few or minor weaknesses, while Subgroup B is composed of institutions that exhibit weaknesses that could result in deterioration of the institution and increased risk to the insurance fund. Subgroup C consists of institutions that pose a substantial risk of loss to the insurance fund unless corrective action is taken.[19] The highest-rated and least-risky institutions are assigned to risk category "1A," while the lowest-rated and riskiest institutions are assigned to category "3C."

In creating a new risk-based assessment system, the FDIC proposes to consolidate the existing nine risk categories into four and rename them as Risk Categories I, II, III and IV. The FDIC notes that not all of the existing nine categories are necessary and some categories contain few, if any, institutions. The FDIC rule would consolidate the sparsely populated categories with others based on similarity of failure rates. Risk Category I would replace category 1A of the current system and would contain all well-capitalized institutions—currently 95% of all insured institutions.

All institutions in Risk Categories II, III and IV would be treated similarly for assessment purposes. However, small, large and new institutions in Risk Category I would be evaluated under different criteria. In its proposal, the FDIC defines a large institution as an institution that has $10 billion or more in assets, while a small institution is defined as an institution with less than $10 billion in assets. Institutions that were established within the last seven years would be treated as "new institutions."

All new institutions in Risk Category I, regardless of size, would be treated similarly and would be assessed the maximum rate applicable to Risk Category I institutions. For small institutions within Risk Category I, the FDIC proposes to utilize weighted versions of the institution's CAMELS ratings and certain financial ratios from its call report to determine the small institution's individualized assessment rate. To determine the insurance score and assessment rate for a large institution in Risk Category I, the FDIC proposes to combine its CAMELS component ratings with its long-term debt issuer ratings and, for an institution with $10–$30 billion in assets, its call report financial ratios, as well. Based on this data, large institutions would then be grouped together and placed into one of six "buckets" within Risk Category I, and would thereby be assigned an assessment rate that corresponds to one of these six buckets.

One criticism of the proposal is that large institutions do not receive an individualized assessment rate, as small institutions do, resulting in a system where large institutions may be subject to different assessment rates than those charged to smaller institutions with similar risk profiles. Whereas the risk-based assessment rate for a small institution is calculated by using a mathematical formula, the assessment rate for a large institution depends upon in which bucket it is placed. Minor changes in a large institution's financial ratios could impact this placement and may result in fluctuating and unpredictable assessment rates.

Perhaps as a way to mitigate concern over the large institution assessment system, the FDIC included in its proposal an assessment rating assignment evaluation and review process, whereby the FDIC would "establish a variety

of controls to ensure consistent and well-supported pricing decisions."[20] The FDIC would consult with institutions' primary federal regulators before finalizing assessment rate assignments, and any adjustments to assignments would be fully supported and documented. Additionally, the overall distribution of large institution assessment rate assignments would be subject to additional review under the assessment request for review procedures currently set forth in the FDIC regulations.[21]

The FDIC also proposes to adopt a new base schedule of assessment rates that is tied to the new Risk Category system. Institutions in Risk Category I would be charged an assessment rate ranging from two to four basis points. All institutions in Risk Categories II, III and IV would be charged assessment rates of 7, 25 and 40 basis points, respectively. These rates may fluctuate from those proposed in the base schedule, and the FDIC proposes that it continue to be allowed to adjust all rates uniformly by five basis points higher or lower than the base rates, without having to undergo a notice-and-comment rulemaking.

Due to the extensive changes proposed, the FDIC invited comment from the public on all aspects of this rule. The FDIC intends to have the rule finalized by the November 5, 2006, statutory deadline.

Other Changes to the Insurance Assessment System

In addition to creating a new risk-based assessment system, the Reform Act implemented a number of other, largely procedural, changes to the assessment system. Section 2104(c) increases penalties that insured depository institutions must face due to late or unpaid assessments. The Reform Act generally provides for penalties of up to 1% of the assessment amount due for each day the assessment goes unpaid. If an insured depository institution fails to pay an assessment due to a dispute with the FDIC over the amount of the assessment, then it is excepted from any penalties as long as it deposits security with the FDIC as a substitute for payment until the dispute is resolved. Furthermore, the FDIC may modify or remit payment of a penalty if an insured depository institution has a good cause for the delay of payment.[22]

The Reform Act also establishes a statute of limitations for actions related to insurance assessments. For overpayment of an assessment, an insured depository institution has three years from the date the assessment was due to file a claim against the FDIC. Similarly, if an insured depository institution underpays an assessment, the FDIC has three years after the date the assessment was due to file a claim against the institution. Lastly, if an insured depository institution makes a false or fraudulent statement to evade an assessment, the Reform Act makes clear that the three-year statute of limitations does not begin until the date of discovery of such statement.

Proposed Rule–Assessments

On May 18, 2006, the FDIC proposed additional changes to its assessment regulations that would make the deposit insurance system react more quickly and more accurately to variations in an institution's risk profile.[23] Specifically, the proposed rule would provide for elimination of the float deduction, assessment collection after each quarter end, changes in the computation of an institution's assessment base, elimination of prepayment and double payment options, and changes to procedures to request review and revision of quarterly invoices. If adopted, these provisions will become effective January 1, 2007.

The most substantial change proposed in this rule is the elimination of the float deduction. Currently, institutions are permitted to adjust their current assessment base by applying a float deduction, which takes into account deposits that are reported for assessment purposes that were created by deposits of checks or other cash items that the institution did not yet receive. The float deduction reduces double counting of deposits. The FDIC is proposing to eliminate the float deduction because current estimated float calculations are arbitrary, and requiring an "actual float" calculation is too burdensome. Furthermore, legal and technological changes in the payment systems—such as Check 21—have accelerated check clearing, reduced float and made float deductions theoretically obsolete.

In the proposal, the FDIC seeks a number of comments from institutions on float, such as how much float remains in the payment system, how accurate present float deductions are, and how burdensome it would be to calculate actual float. Furthermore, the FDIC seeks comment on two alternative proposals. First, the FDIC asks whether institutions would favor a system in which actual float would be incorporated into calculating the assessment base. While this would more accurately reflect an institution's assessment base, calculation of actual float would require an institution to track these transactions and may therefore be too burdensome. Second, the FDIC asks whether it should retain the existing float

deduction. While the deduction does not accurately measure float for most institutions, it has been in place for over 40 years and institutions are accustomed to this measurement.

Another major proposed change concerns the timing of when assessments are collected. Currently, deposit insurance assessments are collected in advance on a semiannual basis in two installments—one at the beginning of the assessment period and one at the middle of the assessment period. Under the proposal, the FDIC would instead begin collecting assessments in arrears at the end of the quarter for which the institution was insured. The FDIC invites comment on whether to maintain the current process of collecting premiums in advance or to adopt the proposed system of collecting assessments in arrears.

An additional proposed change is intended to ensure that any changes in an institution's supervisory or capital group categories be reflected in a more timely manner. Currently, any changes in these ratings impact an institution's assessment rate and are reflected in the next semiannual assessment period. Under the proposal, any changes in these ratings would be reflected upon their occurrence. For example, under the proposed system, if an institution received a change in its CAMELS rating, any effect on insurance risk classification would change as of the date of the examination or when the institution was notified of the rating change.

The FDIC also proposes to change the way in which an institution's assessment base is calculated. Currently, an institution's assessment base is determined by its quarter-end deposit balance as of a specific date. This measurement only captures a balance on a single day and may not accurately reflect an institution's typical deposit level. Instead, the FDIC proposes to instead use an average daily balance over the quarter in an effort to give a more accurate and timely picture of an institution's deposits. The proposal requires institutions with $300 million or more in deposits to use the average daily balance method, while smaller institutions, with less than $300 million, have the option of using either the average daily balance or the quarter-end balance method. Any institution that switches to the average daily balance system, either voluntarily or because it is required, cannot switch back to the quarter-end balance system.

Fixed Reserve Ratio Replaced with Reserve Range

Prior to passage of the Reform Act, the FDIC was required to utilize a statutory designated reserve ratio of at least 1.25% in deciding whether to assess deposit insurance premiums. The Reform Act replaces this target-designated reserve ratio with a reserve range of 1.15–1.5% of estimated insured deposits. While the FDIC Board is still required to designate a reserve ratio, it now has the discretion to designate a reserve ratio within a specific range and may designate one that falls below the previous statutory minimum of 1.25%. In designating a reserve ratio within the statutory range, the FDIC is required to consider a number of statutory factors, including present and future risk of losses to the DIF (including historic experience) and potential and estimated losses from insured depository institutions; economic conditions generally affecting insured depository institutions, any sharp adjustments in the assessment rates, and other factors the board deems appropriate. Additionally, in designating a reserve ratio, the FDIC Board is required to include with its proposed designation a thorough analysis of the data and projections on which a new ratio would be based.

Proposed Rule–Designated Reserve Ratio of 1.25%

In a recently published rule, the FDIC continued to set the designated reserve ratio for the DIF at 1.25% of estimated insured deposits.[24] Although it has the discretion to set a different reserve ratio as long as it falls within the reserve range, the FDIC decided to maintain the current ratio, citing the strong performance of the economy and banking industries, the lack of bank failures during the past two years, the greater likelihood of premium stability if the designated reserve ratio is maintained, and historical experience that a designated reserve ratio of 1.25% has worked well under varying economic conditions.

Dividends

The Reform Act requires the FDIC to implement a system for paying out dividends to insured depository institutions if the reserve ratio of the DIF exceeds 1.5%.[25] If the reserve ratio is greater than 1.35% but less than 1.5%, a dividend that is equal to 50% of the excess shall be declared and paid to insured depository institutions.

The FDIC Board's distribution of dividends would be based on a number of statutory factors, including an institution's relative contribution to the DIF; an institution's assessment base on December 31, 1996, as it compares to the assessment base of all eligible insured depository institution's on that date; the total amount of assessments paid on or after January 1, 1997, to the DIF; the portion of assessments paid by an institution (or any predecessor) that reflects higher levels of risk assumed by the institution; and any other factors the FDIC deems appropriate.

The Reform Act also provides that the FDIC Board may suspend or limit dividends if it determines in writing that a significant risk of loss to the DIF exists over the next year, and the losses will be sufficiently high to justify finding that the distribution of dividends should be suspended. Factors that the FDIC Board is required to consider under the Reform Act include national and regional conditions impacting institutions, potential problems affecting institutions or specific group of institutions, and anticipated failures and contingent liabilities of the FDIC.

Proposed Rule–Dividends

Under the Reform Act, the FDIC is required to issue regulations that address the methods for calculation, declaration and payment of dividends, and administrative appeals of individual dividend amounts. The proposed rule[26] amends 12 C.F.R. Part 327 and covers the initial two-year period of payment of dividends from the DIF, with a sunset date of December 31, 2008. If this two-year interim rule is adopted, the FDIC would undertake a second rulemaking in 2007 to explore alternative methods for distributing future dividends after the initial two-year period.

In determining whether to declare a dividend, the proposal states that the FDIC Board will use complete data as of the prior year-end for the reserve ratio and will announce its determination by May 15 of each year. At that time, the FDIC Board may determine that (i) no dividend will be declared because the reserve ratio is less than 1.35%; (ii) a dividend will be declared; or (iii) a dividend would be required except in circumstances that warrant limitation or suspension of a dividend. Notification of a dividend would occur as soon as practicable after May 15, and would be provided in a special notice or in an institution's next assessment invoice.

The statute requires that any dividend be awarded in proportion to the 1996 assessment base ratio on an institution or its predecessor. The statute does not define "predecessor," though the FDIC proposal would define predecessor as an institution that combined with another institution through a merger or consolidation and did not survive as an entity. The FDIC adopted this definition under the theory that it parallels its definition of "successor" as proposed in the one-time assessment credit rule.

The FDIC seeks comment on whether this definition of predecessor is too limited—specifically, if the definition should also include an institution that combined with another through a *de facto* merger (a transaction that is not technically a merger or consolidation but mirrors the results of such transactions). Furthermore, comments are sought on whether this definition should parallel the definition of successor in the one-time assessment credit rule or any alternative definitions of successor that may be adopted.

This proposed rule also incorporates review procedures for an institution that disagrees with the computation of its 1996 assessment base ratio or computation of the dividend. An institution would have 30 days from the date of the invoice stating the dividend amount to request review. In requesting a review, the proposed rule requires that submission be made to the FDIC Division of Finance and that the request include supporting documentation and identification of all other institutions that may be affected by granting the review. These identified institutions would receive copies of the filings and have an opportunity to comment thereon. The proposal also explains that the FDIC would have the ability to temporarily freeze the distribution amount while the dividend is in dispute.

DIF Restoration Plans

The Reform Act requires the FDIC to adopt a DIF restoration plan when the reserve ratio falls below the minimum designated reserve ratio set by the FDIC Board. The statute requires the FDIC to establish a plan that would increase the reserve ratio to meet or exceed the minimum amount specified before the end of the five-year period following implementation of the plan. As part of the restoration plan, the FDIC may also restrict the application of assessment credits. Within 30 days of establishing the DIF restoration plan, the FDIC would be required to publish in the Federal Register a detailed analysis of factors considered and the basis for the actions taken with regard to plan.

Looking Ahead–Future Assessment Rates

The FDIC Board convened a meeting on May 9, 2006, and voted to keep assessment rates charged to insured banks and thrifts at the same rate for the second half of 2006. However, next year and in subsequent years, the FDIC Board will need to maintain the reserve ratio within the range established under the Reform Act, and thus, the FDIC has cautioned that it is likely that banks will begin to see increased assessment rates going forward.

These probable increases in assessment rates stem from two major factors: increased deposit growth, and limited revenue

in the next few years due to the use of assessment credits. Statistics from the FDIC indicate that insured deposit growth has pushed the reserve ratio down from 1.31% at year-end 2004 to 1.25% at year-end 2005, and 1.23% in March 2006. The FDIC staff's best estimate for the year-end 2006 reserve ratio is 1.20%.[27] Additionally, as institutions begin to use their assessments credits in the next few years, revenue into the insurance fund will be limited and the reserve ratio may continue to drop. In light of limited revenue and increasing deposit growth, the FDIC Board has stated it may have to impose substantial assessment rate increases to maintain a reserve ratio within the statutory range.

Conclusion

The statutory changes and implementing regulations required by the Reform Act will help to make the federal deposit insurance framework react more quickly to changing economic and industry conditions, reflect changes in an institution's risk profile, and incorporate operational and procedural systems that measure more accurately an institution's assessment base. This article has outlined the complex set of changes called for in the Reform Act and the FDIC's actions to date to implement these reforms. As the FDIC continues to publish rules and implement the changes required by the Reform Act, it is certain that there will be further debate over how to best implement these reforms.

NOTES

1. Pub. L. No. 109-171, 120 Stat. 9 (Feb. 8, 2006). Congress also passed *The Deposit Insurance Reform Conforming Amendments Act of 2005*, Pub. L. 109-173, 119 Stat. 3601 (Feb. 14, 2006), which contains necessary technical and conforming changes to implement deposit insurance reform.
2. Pub. L. No. 101-73 (Aug. 9, 1989).
3. *Revisions to Reflect the Merger of the Bank Insurance Fund and the Savings Association Insurance Fund*, 71 Fed. Reg. 20,524 (Apr. 21, 2006).
4. Press Release, FDIC Reports First Quarter 2006 Financial Results for the Deposit Insurance Fund (June 19, 2006), available at http://www.fdic.gov/news/news/press/2006/pr06061.html.
5. *The Federal Deposit Insurance Reform Act of 2005*, Pub. L. No. 109-171 § 2107(a) (Feb. 8, 2006).
6. An insured depository institution is "adequately capitalized" if it meets the required minimum level for each relevant capital measure. 12 U.S.C. § 1831o(b)(1)(B).
7. *One-Time Assessment Credit*, 71 Fed. Reg. 28,809 (May 18, 2006) (proposing to amend 12 C.F.R. part 327).
8. See http://www.fdic.gov/deposit/insurance/reform.html.
9. 71 Fed. Reg. at 28,813.
10. *Deposit Insurance Regulations; Inflation Index; Certain Retirement Accounts and Employee Benefit Plan Accounts*, 71 Fed. Reg. 14,629 (Mar. 23, 2006).
11. *Deposit Insurance Regulations; Inflation Index; Certain Retirement Accounts and Employee Benefit Plan Accounts*, 71 Fed. Reg. 53,547 (Sept. 12, 2006).
12. An insured depository institution is "well capitalized" if it significantly exceeds the required minimum level for each relevant capital measure, and is "adequately capitalized" if it meets the required minimum level for each relevant capital measure. 12 U.S.C. § 1831o(b)(1)(A), (B).
13. 71 Fed. Reg. 14,629.
14. 71 Fed. Reg. at 53,549.
15. *Effect of the Federal Deposit Insurance Reform Act on the Consolidated Reports of Condition and Income*, 71 Fed. Reg. 38,401 (July 6, 2006). For detailed guidance on the Call Report revisions and filing instructions, also see the "FFIEC Supplemental Instructions for June 2006 Call Report Forms" provided with FDIC FIL-54-2006 (June 27, 2006).
16. *The Federal Deposit Insurance Reform Act of 2005*, Pub. L. No. 109-171 § 2104 (Feb. 8, 2006).
17. *Assessments*, 71 Fed. Reg. 41,909 (July 24, 2006).
18. See http://www.fdic.gov/deposit/insurance/initiative/index.html.
19. Institutions with CAMELS ratings of 1 or 2 are generally placed in Supervisory Group A, institutions with CAMELS rating of 3 are placed in Supervisory Group B, and institutions with CAMELS ratings of 4 or 5 are placed in Supervisory Group C.
20. 71 Fed. Reg. 41,909, 41924.

21 12 C.F.R. § 327.4(d).

22. See *Penalty for Failure to Timely Pay Assessments*, 71 Fed. Reg. 40,938 (July 19, 2006) (proposing to amend 12 C.F.R. § 308.132 in conformity with the provisions of the Reform Act).

23 *Assessments*, 71 Fed. Reg. 28,790 (May 18, 2006) (proposing to amend 12 C.F.R. part 327).

24 *Deposit Insurance Assessments–Designated Reserve Ratio*, 71 Fed. Reg. 41,973 (July 24, 2006).

25 *The Federal Deposit Insurance Reform Act of 2005*, Pub. L. No. 109-171 § 2107(a) (Feb. 8, 2006).

26 *Dividend Requirements,* 71 Fed. Reg. 28,804 (May 18, 2006).

27 "The Deposit Insurance Reform Act of 2005: Proposed Rules Implementing the One-Time Assessment Credit, FDIC Dividends, and Related Assessment Issues," presentation made by FDIC staff to the District of Columbia Bar Association (July 24, 2006).

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