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[FDIC Proposes to Implement Dodd-Frank Act Changes to Deposit Insurance Assessments](#)

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The Federal Deposit Insurance Corporation recently issued a proposed rule that would implement the directive of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) to revise the risk-based scheme for deposit insurance assessments. The new assessment system would generally be based on an institution's total liabilities (total assets less tangible capital) instead of its domestic deposits and would take effect for the quarter beginning April 1, 2011.

The FDIC's current risk-based system calculates an initial base assessment rate (IBAR) for each bank and thrift. The IBAR depends upon which of four risk categories the institution is assigned based on examination ratings, Call Report or Thrift Financial Report (TFR) data and certain other supervisory information. The IBAR can then be lowered due to calculations related to the institution's amount of long-term unsecured debt or raised as a result of a formula measuring its reliance on secured liabilities or brokered deposits. Those adjustments are designed to more accurately assess the risk the particular institution poses to the Deposit Insurance Fund. The final assessment rate for each institution under the current system is then applied to that institution's total domestic deposits (subject to some specified exclusions). The current IBAR scale ranges from 12 basis points for the least risky institutions to 45 basis points for the riskiest. With the possible adjustments, the range expands to 7 to 77.5 basis points.

As directed by the Dodd-Frank Act, the proposed rule would revise the FDIC's assessment system to tie the risk-based assessment rate to each institution's "average consolidated total assets" for the assessment period less its "average tangible equity." The FDIC's proposal generally requires the calculation of an institution's total assets as is now done for the Call Report or TFR, except that daily asset balances over the assessment period would be averaged for assessment purposes. The proposed rule would define "tangible equity" as Tier 1 capital for purposes of the deduction from total average assets and would generally require a monthly average over the assessment period. Institutions with less than \$1 billion in assets as of March 31, 2011, could choose instead to use the end-of-quarter Tier 1 capital balance. However, once an institution reports consolidated total assets of \$1 billion or more for two consecutive quarters, it would be required to use monthly averaging.

In conjunction with the change in assessment base required by the Dodd-Frank Act, the FDIC is also proposing possible changes to the adjustments to the IBAR. The proposal would eliminate the adjustment for secured liabilities because those liabilities will be subject to assessment under the new system.

Inasmuch as the FDIC believes that the issuance of long-term debt by depository institutions reduces the Deposit Insurance Fund's losses in the event of default (since unsecured debtholders are likely to be cut back or lose their money entirely in a liquidation), the proposal increases the potential assessment reduction for unsecured debt to account such being subject to assessment. However, noting that unsecured long-term debt issued to another depository institution does not provide the same reduction in risk, the proposal would apply a new adjustment for the assessment rate of an institution that holds unsecured long-term debt issued by another depository institution. That assessment adjustment would consist of an increase of 50 basis points for every dollar of such debt held. The proposal would also

modify the definition of long-term unsecured debt by excluding Tier 1 capital. The brokered deposit adjustment would be retained but scaled to the new assessment base through a ratio of domestic deposits to the new assessment base.

The FDIC's proposal indicates that the Dodd-Frank Act changes to the assessment system are intended to be revenue neutral. The proposed assessment schedule is lower than the existing one because the new assessment base will be broader than the current assessment base of domestic deposits. The schedule, as proposed, would range from 5 basis points for the least risky institutions to 35 basis points for the riskiest. The revised possible adjustments would expand the range to 2.5 to 45 basis points. The proposal provides for further reductions in the rate schedule as the Deposit Insurance Fund reserve ratio increases to meet specified thresholds.

At the same time that it issued the Dodd-Frank Act proposed rule, the FDIC issued a proposed rule amending its April 2010 proposal that would have established a separate risk-based assessment system for institutions with more than \$10 billion in assets and for other large, highly complex institutions. That proposal, which would have established a scorecard approach for calculating assessments for large institutions, was the subject of an earlier Financial Institutions Alert (FDIC Proposes Revisions to Risk-Based Assessment System for Large Insured Depository Institutions and Adjustments to Assessment Range for All Insured Institutions). The amended proposed rule is largely a result of the changes required by the Dodd-Frank Act and also incorporates comments received in response to the initial proposed rule. The FDIC is accepting comments on the proposed rules for 45 days following publication in the Federal Register.

The Dodd-Frank Act's changes to the FDIC's assessment system are thought to benefit community banks at the expense of larger institutions because larger institutions typically have had greater access to non-deposit funding sources that were not assessed. The open question is whether, as a result of the revised assessment system, larger institutions will adjust their business strategies to emphasize deposits, thereby intensifying competition for deposit products.

For more information about these issues, please contact the author(s) of this Legal Alert or your existing firm contact.

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