An Update on Emerging Issues in Banking

FDIC Notifies Banks that Higher Insurance Premiums Are Possible

March 1, 2002

The Board of Directors of the FDIC today alerted insured institutions to the possibility of higher deposit insurance premiums in the second half of 2002. The higher premiums–if they prove necessary–would likely affect only those banks and thrifts with deposits insured by the Bank Insurance Fund (BIF), and the amount of any such increase would be at most 5 basis points of BIF-assessable deposits per annum.

The FDIC Board also considered, and rejected, seeking public comment on possible premium rate increases of more than 5 basis points in the second half of the year.

The BIF balance for year-end 2001 stood at $30.6 billion (unaudited), which includes the effect of a $1.75 billion reserve for calendar-2002 insurance losses. BIF-insured deposits at year-end 2001 are about $2.41 trillion. Based on these figures, the ratio of the BIF to its insured deposits is expected to fall to 1.27 percent at year-end 2001.

The FDIC is required to maintain a BIF balance of at least 1.25 percent of BIF-insured deposits (the "Designated Reserve Ratio," or DRR). If the BIF falls below the DRR, the FDIC must collect premiums sufficient to restore the shortfall within a year after the higher premiums are set, or it must collect premiums of at least 23 basis points.

The FDIC Board must notify insured institutions of any increase in premiums for the second half by May 15, 2002. In 1996 the Board reserved for itself, by regulation, the option to increase premiums by as much as 5 basis points at any one time.[1] Larger premium increases require the Board to solicit public comment.

Based on the information presently available, higher premiums would not be needed in the second half of the year. In today's economic climate, however, predictions are difficult and actual outcomes have the potential to deviate significantly from expected or most likely outcomes, both for the economy generally and for individual companies.

The FDIC will use the time between now and May 15 to analyze any additional information that becomes available. There remains a possibility that such new information would require the Board to exercise its discretion to increase premiums by up to 5 basis points.

Table 1 shows the ranges for insured deposit growth and insurance losses that the staff presented to the Board, and the impact on the year-end 2002 BIF reserve ratio assuming no increase in premiums. The 2 percent to 6 percent range for annualized insured deposit growth is within the range suggested by recent experience. The $100 million to $2.8 billion range for insurance losses is subject to the most uncertainty, but is consistent with recent increases in the number and assets of problem banks (for information about recent bank performance see the *Preliminary Bank Earnings Report*.

Table 1

BIF Ratio Projections Depend on Insurance Losses and Insured Deposit Growth *	
December 31, 2002 Projected Losses = $100M to $2.8B	
2% annual deposit growth	6% annual deposit growth
Low: 1.17%	Low: 1.12%
High: 1.28%	High: 1.23%

* Assumes BIF fund balance as of 12/31/01 of $30.6 billion and BIF-insured deposits of $2.41 trillion, resulting in a BIF ratio of 1.27 percent.

If insured-deposit growth and insurance losses fall within these ranges, the year-end 2002 BIF reserve ratio would be between 1.12 percent and 1.28 percent if premiums are not increased in the second half.

[1] Deposit insurance premiums are assessed against adjusted domestic deposits.