# Banking and Finance Law Daily Wrap Up,TOP STORY—Proposal would align small bank insurance deposit assessments with risk,(Jun. 16, 2015)

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Proposed changes to the way of assessing deposit insurance for established small banks would revise the methodology to estimate the probability of failure within three years to ensure that banks that take on greater risks will pay more for deposit insurance. The proposed rule would affect banks with less than $10 billion in assets that have been insured by the Federal Deposit Insurance Corporation for at least five years. “The proposed pricing method for small banks would do a better job of recognizing risks before they become losses and would help ensure that banks that take on greater risks pay more for deposit insurance than their less risky counterparts,” FDIC Chairman Martin J. Gruenberg said.

Gruenberg also noted in a statement at the FDIC Board meeting that the proposal is revenue neutral, “so that it would not change the aggregate amount that the FDIC expects to collect from small banks. It would only change the allocation of premium costs based on the risk profiles of banks.” To help banks understand the potential effect of the proposed rule, the FDIC has published an online assessment calculator that will allow institutions to estimate their assessment rates under the proposal.

**Risk differentiation.** The FDIC feels that it no longer needs to rely on a model based on the probability that a bank with a CAMELS composite rating of 1 or 2 will be downgraded to a CAMELS composite rating of 3, 4, or 5 within 12 months. Instead, the FDIC can base small bank deposit insurance assessments on a statistical model that estimates a bank’s probability of failure directly.

The FDIC said that the statistical model on which the proposed changes for small banks in 12 CFR 327—Assessments are based allows the system to better capture risk when the risk is assumed, rather than when the risk has already resulted in loss. The FDIC would update the financial measures used in the financial ratios method to be consistent with the proposed statistical model.

The FDIC would eliminate risk categories for small banks (other than new small banks and insured branches of foreign banks) and apply the model to all established small banks. Because CAMELS ratings can incorporate information that the model cannot, the FDIC proposes to apply minimum or maximum initial base assessment rates that will depend on a bank's CAMELS composite rating.

The FDIC is proposing that the new assessment system go into operation the quarter after the reserve ratio of the Deposit Insurance Fund reaches 1.15 percent. At that time, under the initial base assessment rate schedules adopted by the Board in 2011, initial base assessment rates will fall automatically from the current 5-basis-point-to-35-basis-point range to a 3-basis-point-to-30-basis-point range.

**Comments.** There is a 60-day comment period after publication in the *Federal Register*. The FDIC sought comment on whether:

- there are other variables, besides the eight included in the statistical model and proposal, that both predict the likelihood of bank failure with statistical significance and do not have perverse incentive effects;
- there are variables that can be shown to predict likely losses given failure with statistical significance;
- the upper end of the assessment rate range should decline from 35 basis points to 30 basis points as proposed or whether higher assessment rates should continue to apply to the riskiest banks.

MainStory: TopStory DepositInsurance FinancialStability