FDIC
Federal Deposit Insurance Corporation
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Division of Insurance and Research

November 19, 2019

MEMORANDUM TO: The Board of Directors

FROM: Diane Ellis
Director, Division of Insurance and Research

SUBJECT: Notice of Final Rulemaking Re: the Use and Remittance of Certain Assessment Credits

RECOMMENDATION

Staff recommends that the FDIC Board of Directors (Board) adopt and authorize publication of the attached final rulemaking (final rule). The final rule would amend the deposit insurance assessment regulations that govern the use of small bank credits and one-time assessment credits (OTACs) awarded to insured depository institutions (IDIs). Together, the credits total approximately $765 million. Small bank credits represent $764.5 million of the total and OTACs account for approximately $300,000.

In March 2016, the FDIC Board of Directors approved a final rule[1] (the 2016 final rule) that, among other things, implemented the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) requirement that the FDIC offset the effect of increasing the minimum reserve ratio of the Deposit Insurance Fund (DIF) from 1.15 percent to 1.35 percent on IDIs with less than $10 billion in assets (small IDIs).[2] Pursuant to the 2016 final rule, upon reaching the statutory minimum reserve ratio of 1.35 percent, small IDIs were awarded assessment credits for the portion of their assessments that contributed to the growth in the reserve ratio from 1.15 percent to 1.35 percent (small bank credits).[3] The FDIC's regulations currently provide that these small bank credits will be applied to quarterly deposit insurance assessments when the reserve ratio is at least 1.38 percent.[4]

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[1] 81 FR 16059 (Mar. 25, 2016).

[2] Pub. L. No. 111–203, 334(e), 124 Stat. 1376, 1539 (12 U.S.C. 1817 (note)).

[3] *See* 81 FR at 16065-16066.

[4] 12 CFR 327.11(c)(11)(i).

Concur:

Nicholas J. Podsiadly
General Counsel

As of June 30, 2019, the DIF reserve ratio reached 1.40 percent, exceeding the 1.38 percent threshold for the first time. As a result, the FDIC began to apply small bank credits to quarterly assessment invoices, beginning with IDIs' second quarter assessments. Under the final rule, such credits would continue to be applied as long as the DIF reserve ratio is at least 1.35 percent (instead of 1.38 percent, as currently provided). In addition, after small bank credits have been applied for three additional quarterly assessment periods (instead of seven, as proposed), the FDIC will remit the full amount of any remaining small bank credits in lump-sum payments to each IDI holding such credits in the next quarterly assessment period in which the reserve ratio is at least 1.35 percent. Finally, at the same time that any remaining small bank credits are remitted, the FDIC also will remit the nominal value of any remaining OTACs in lump-sum payments to each IDI holding such credits.

The primary objective of this rule is to make the application of small bank credits to quarterly assessments more predictable for IDIs with these credits, and to simplify the FDIC's administration of these credits, without materially impairing the FDIC's ability to maintain the required minimum reserve ratio of 1.35 percent. Staff recommends that the rule become effective upon publication in the *Federal Register* and that the rule have an application date of July 1, 2019 (the beginning of the third quarter assessment period).

BACKGROUND

Small Bank Assessment Credits

To offset the effect of increasing the minimum reserve ratio on small IDIs, the 2016 final rule provided small bank credits for the portion of regular assessments paid by small IDIs that contributed to the growth in the reserve ratio from 1.15 percent to 1.35 percent.[5, 6] Pursuant to the 2016 final rule, upon reaching the statutory minimum reserve ratio of 1.35 percent, small IDIs were awarded small bank credits. The regulations provided that these small bank credits would be applied to quarterly deposit insurance assessments when the reserve ratio is at least 1.38 percent.[7]

As of September 30, 2018, the DIF reserve ratio reached 1.36 percent, exceeding the statutorily required minimum reserve ratio of 1.35 percent. All IDIs that were small IDIs, including small IDI affiliates of large IDIs, at any time during the "credit calculation period"[8] were awarded a share of credits in January 2019.[9] The aggregate amount of small bank credits

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[5] Pub. L. No. 111–203, 334(e), 124 Stat. 1376, 1539 (12 U.S.C. 1817 (note)).

[6] *See* 81 FR 16059 (Mar. 25, 2016) and 83 FR 14565 (April 5, 2018) (making technical amendments to FDIC's assessment regulations, including an amendment clarifying that small bank credits will be applied in assessment periods in which the reserve ratio is at least 1.38 percent).

[7] 12 CFR 327.11(c)(11).

[8] The "credit calculation period" covers the period beginning July 1, 2016 (the quarter after the reserve ratio first reached or exceeded 1.15 percent) through September 30, 2018 (the quarter in which the reserve ratio first reached or exceeded 1.35 percent). *See* 12 CFR 327.11(c)(2).

[9] If a small IDI acquired another small IDI through merger or consolidation during the credit calculation period, the acquiring small IDI's regular assessment bases for purposes of determining its credit base included the acquired

awarded is $764.5 million. As of June 30, 2019, the DIF reserve ratio reached 1.40 percent, exceeding the 1.38 percent threshold for the first time. As a result, for the second quarter assessment period, the FDIC applied $319.7 million of small bank credits to offset IDIs' assessments. After applying credits for the second quarter of 2019, $444.8 million in small bank credits remain.[10]

One-Time Assessment Credits

The Federal Deposit Insurance Reform Act of 2005 (FDI Reform Act) required the FDIC to provide one-time assessment credits (OTACs) to IDIs that existed on December 31, 1996, and paid a deposit insurance assessment prior to that date, or that were successors to such an institution.[11, 12] In October 2006, the FDIC adopted a final rule implementing the OTAC requirement.[13] The FDIC began to apply OTACs to offset an IDI's quarterly deposit insurance assessments beginning with the first assessment period of 2007. As of June 30, 2019, only two IDIs have outstanding OTACs totaling approximately $300,000. The FDIC estimates that the application of the OTACs could continue for more than 13 years.

Notice of Proposed Rulemaking

On August 29, 2019, the FDIC published in the *Federal Register* a notice of proposed rulemaking (NPR) to amend the deposit insurance assessment regulations that govern the use of small bank credits and OTACs by certain IDIs.[14] Under the NPR, the FDIC would continue to apply small bank credits if the reserve ratio falls below 1.38 percent, as long as it does not fall below the statutory minimum reserve ratio of 1.35 percent. The FDIC proposed to remit the full nominal value of any remaining small bank credits after such credits had been applied for eight quarterly assessment periods. At the same time that any remaining small bank credits are

IDI's regular assessment bases for those quarters during the credit calculation period that were before the merger or consolidation. *See* 12 CFR 327.11(c)(5).

[10] In January 2019, aggregate credits of $764.7 million were awarded to 5,381 institutions. As of June 30, 2019, due to mergers, IDI failures, and voluntary liquidations, 5,215 remaining institutions had credits totaling $764.5 million. Since then, the FDIC has applied $319.7 million of small bank credits, reducing the aggregate amount of remaining small bank credits to $444.8 million.

[11] The FDI Reform Act was included as Title II, Subtitle B, of the Deficit Reduction Act of 2005, Pub. L. No. 109-171, 2107(a), 120 Stat. 4, 18 (12 U.S.C. 1817(e)(3)).

[12] By statute, the aggregate amount of credits equaled the amount that would have been collected if the FDIC had imposed a 10.5 basis point assessment on the combined assessment base of the Bank Insurance Fund and the Savings Association Insurance Fund as of December 31, 2001. *See* 12 U.S.C. 1817(e)(3)(B). Individual shares were required to be based on the ratio of the institution's assessment base on December 31, 1996, to the aggregate assessment base of all eligible IDIs on that date. *See* 12 U.S.C. 1817(e)(3)(A).

[13] 12 CFR 327 Subpart B (327.30 *et seq.*).

[14] *See* 84 FR 45443 (August 29, 2019).

remitted, the FDIC also proposed to remit the full nominal value of any remaining OTACs to IDIs holding such credits.

The FDIC sought comment on every aspect of the NPR, including alternatives. The FDIC received two comments on the NPR, both from trade associations. Both commenters generally supported the rule and agreed that the proposal would result in more predictable application of credits to quarterly assessments and would simplify the FDIC's administration of the DIF. One commenter supported remitting the full balance of any remaining small bank credits after small bank credits have been applied for four quarterly assessment periods, noting that the FDIC should "return the credit funds as expeditiously as is feasible" and that "[t]he credits will serve a better purpose when disbursed to these banks where these funds can support the institutions' lending and liquidity."[15]

DISCUSSION OF THE FINAL RULE

Application of Small Bank Credits when Reserve Ratio is at least 1.35 Percent

FDIC staff recommends that the Board adopt and authorize publication of the attached final rule to amend the deposit insurance assessment regulations so that small bank credits would continue to be applied if the reserve ratio falls below 1.38 percent, as long as it does not fall below the statutory minimum reserve ratio of 1.35 percent. Staff believes that the changes will reduce the likelihood that the application of small bank credits would be suspended due to small variations in the reserve ratio. In particular, the rule lessens the likelihood that small bank credits would be applied in a quarter when the reserve ratio is at or above 1.38 percent and then immediately suspended in the next quarter if the reserve ratio falls below 1.38 percent. The rule is expected to result in more stable and predictable application of small bank credits to quarterly assessments, permitting IDIs to better budget for their assessment cash flow, and could benefit certain IDIs that might realize the full value of their credits at an earlier date.

The rule also changes the assessment regulations to allow for the recalculation of small bank credits applied each quarter as a result of subsequent amendments to quarterly regulatory reports.[16]

Remittance of Credits after Four Quarterly Assessment Periods

In response to comments, under the final rule, the FDIC will remit the remaining balance of any small bank credits in lump-sum payments to each IDI holding credits after such credits have been applied for four quarterly assessment periods, rather than after eight periods as proposed in the NPR, as long as the reserve ratio is at least 1.35 percent. Based on current data and projections, remitting the full balance of any remaining small bank credits after four quarterly assessment periods will not materially impair the FDIC's ability to maintain the

[15] See comment submitted from the American Bankers Association, https://www.fdic.gov/regulations/laws/federal/2019/2019-assessments-3064-af16-c-002.pdf.

[16] Quarterly regulatory reports include Consolidated Reports of Condition and Income and quarterly Reports of Assets and Liabilities of U.S. Branches and Agencies of Foreign Banks.

adequacy of the DIF reserve ratio. At the same time that any remaining small bank credits are remitted, the FDIC also will remit any remaining OTACs to IDIs holding such credits.

Staff believes that adopting a maximum duration for the use of small bank credits and OTACs will accelerate the time at which IDIs would receive the benefit of such credits and will permit more efficient administration of the DIF on a going-forward basis. These benefits will not have an impact on the long-term adequacy of the DIF because the total amount of credits awarded will not change.

Proposed Effective Date and Application Date

Under the Administrative Procedure Act, "[t]he required publication or service of a substantive rule shall be made not less than 30 days before its effective date, except as otherwise provided by the agency for good cause found and published with the rule."[17] Under the final rule, the amendments to the FDIC's deposit insurance assessment regulations will be effective immediately upon publication in the *Federal Register*. The FDIC finds good cause that the publication of this final rule can be less than 30 days before its effective date because IDIs would benefit from more stable and predictable application of small bank credits before the final rule would otherwise become effective.

As of June 30, 2019, the DIF reserve ratio exceeded the 1.38 percent threshold for the first time. As a result, the FDIC applied small bank credits to offset IDIs' assessments for the second quarter of 2019. Because the FDIC invoices for quarterly deposit insurance assessments in arrears, invoices for the subsequent assessment period (i.e., the third quarterly assessment period of 2019) will be made available to IDIs in December 2019, with a payment date of December 30, 2019. To address any possibility that the reserve ratio may decrease below 1.38 percent as of September 30, 2019 (the end of the third quarterly assessment period) and cause the suspension of small bank credits, the FDIC will apply the final rule beginning with the third quarterly assessment period of 2019. This application date will provide certainty to IDIs with small bank credits that the final rule will apply to the third quarterly assessment period of 2019, and that the FDIC will apply small bank credits even if the DIF reserve ratio is less than 1.38 percent (but at least 1.35 percent) for that assessment period.

Expected Effects

The final rule will not change the total amount of credits awarded, but it could affect when the FDIC will apply credits. Based on quarterly regulatory report data as of June 30, 2019, the aggregate amount of small bank credits awarded to IDIs, $764.5 million, represented less than one basis point of the reserve ratio. Furthermore, the FDIC applied approximately 42 percent of the aggregate amount of small bank credits during the second quarter assessment period of 2019 (the first time that small bank credits were eligible to be applied). The application of small bank credits in future quarters is projected to represent increasingly smaller portions of the reserve ratio. The largest expected subsequent quarterly effect will be approximately one-third of a basis point of the reserve ratio. Therefore, the application of small

[17] 5 U.S.C. 553(d)(3).

bank credits in any one quarter will not be sufficient on its own to cause the reserve ratio to fall below 1.35 percent in future quarters.

Using the same data, staff currently estimates that 4,982 IDIs (or 95.5 percent) will exhaust their individual shares of small bank credits within four assessment periods of application, leaving 233 with residual small bank credits available for immediate remittance. The FDIC estimates that these IDIs will hold an aggregate of $6.2 million in credits. Under the final rule, the FDIC will remit the remaining individual small bank credit balances in a lump-sum payment.

Similarly, the final rule also will require the FDIC to remit the outstanding balances of OTACs. As of June 30, 2019, two IDIs held OTACs totaling approximately $300,000, and staff estimates that approximately $275,000 in OTACs will remain after three more quarters of application. Under the final rule, at the same time that the FDIC remits the remaining balances of small bank credits (after four quarters of use), the FDIC also will remit the remaining individual OTAC balances to each of these two IDIs in a lump-sum payment.

Conclusion

Staff recommends that the Board approve the attached final rule, with an effective date upon publication of the rule in the Federal Register, and with an application date of July 1, 2019.

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