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September 22, 2006

Robert E. Feldman
Executive Secretary
Attention: Comments
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, D.C. 20429

Re: Deposit Insurance Assessments—Designated Reserve Ratio

Dear Sir or Madam:

The Independent Community Bankers of America (ICBA)[1] appreciates the opportunity to offer comments in connection with the FDIC's proposal to establish the Designated Reserve Ratio (DRR) for the Deposit Insurance Fund (DIF) at 1.25%. The FDIC's proposal is one of several proposals that the FDIC has recently issued to implement the Federal Deposit Insurance Reform Act of 2005 (Reform Act). Under the Reform Act, the FDIC must by regulation set the DRR for DIF within a range of 1.15% to 1.50% of estimated insured deposits.

ICBA's Position

ICBA strongly urges the FDIC to use the maximum flexibility it has under the Reform Act to build up DIF reserves to meet the DRR steadily and gradually over a three to five year period to avoid an unnecessary surge in assessment rates. While is it understandable that, other things being equal, the FDIC Board would want to reach its targeted reserve ratio as soon as possible, any sudden significant increase in assessment rates would be an unnecessary shock to the banking system and an impairment to bank's earnings and capital. **There should be a period of transition to allow banks to gradually use up their one-time assessment credits and to adjust to paying premiums again under the new risk-based assessment system.**

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[1]*The Independent Community Bankers of America represents the largest constituency of community banks of all sizes and charter types in the nation, and is dedicated exclusively to representing the interests of the community banking industry. ICBA aggregates the power of its members to provide a voice for community banking interests in Washington, resources to enhance community bank education and marketability, and profitability options to help community banks compete in an ever-changing marketplace.*

With nearly 5,000 members, representing more than 18,000 locations nationwide and employing over 265,000 Americans, ICBA members hold more than $876 billion in assets $692 billion in deposits, and more than $589 billion in loans to consumers, small businesses and the agricultural community. For more information, visit ICBA's website at www.icba.org.

INDEPENDENT COMMUNITY BANKERS of AMERICA The Nation's Voice for Community Banks℠
One Thomas Circle, NW Suite 400 Washington, DC 20005 ▪ (800)422-8439 ▪ FAX: (202)659-1413 ▪ Email:info@icba.org ▪ Web site:www.icba.org

One of the FDIC's rationales for setting the DRR at 1.25% is that it is midway between 1.15% and 1.35%, an important floor and ceiling under the Reform Act. Under that law, the FDIC must adopt a restoration plan when the reserve ratio falls below 1.15% and if the ratio exceeds 1.35%, the FDIC must begin paying a dividend. **However, ICBA is concerned that the FDIC Board will raise assessment rates for 2007 possibly as high as five basis points over the base schedule of rates in an effort to quickly reach a reserve ratio of 1.25%.[2]** For those 90% of insured depository institutions that are expected to be in Risk Category I, a five basis point increase would mean 2007 assessments of between 7 and 9 basis points. If assessments were established that high, most institutions would quickly burn through their one-time assessment credits within one year, contrary to what was intended under the Reform Act. Congress expected the credits to last several years to provide a cushion for, and recognize the contributions of, those institutions that built up the fund prior to 1997.

ICBA believes that there are many reasons for the FDIC to slowly build up DIF reserves and establish assessment rates close to the proposed base schedule of rates. First, economic growth is beginning to slow as higher interest rates continue to weigh on economic activity, particularly in the housing sector. A slower pace of home price appreciation is also expected to impede growth in consumer spending next year. **Slower economic activity will mean that insured deposit growth will slow, reversing the trend responsible for the recent decline in the reserve ratio.**

Second, the performance and health of the banking industry is exceptionally robust with strong asset quality, low charge-offs, and high capital and profitability. No insured institution has failed in two years, the longest period without a failure since the creation of the FDIC in 1933. **With five consecutive annual records of bank earnings and with DIF balances now reaching $50 billion, the risk exposure of the DIF is at an all-time low.** In fact, the FDIC has recently estimated potential losses for future failures to be within a range of from $1 million to $241 million. These estimates suggest that near-term losses to the DIF would not alter the reserve ratio.

Furthermore, there have been great improvements in risk management and supervisory practices since 1991 when the 1.25% target level was established. The enhanced regulatory powers that the FDIC has enjoyed since the Federal Deposit Insurance Corporation Improvement Act was implemented in 1991—including prompt corrective action, depositor preference and cross guarantee measures—not only has minimized bank failures but makes it less costly to resolve a bank failure. In response to risk-based examinations and recent proposals to revise the Basel capital accord to make it more risk-sensitive, bankers have made great strides towards improving their risk management tools and implementing them into their operations.

In adopting the Reform Act, Congress expected that the FDIC would pursue a steady, low premium policy to avoid premium volatility. Congress gave the FDIC the tools and flexibility the agency sought so that it could abandon the previous policy of pursuing a designated reserve

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[2] The FDIC has proposed a base schedule of rates of 2-4 basis points for institutions in Risk Category I, 7 basis points for Risk Category II, 25 basis points for Risk Category III, and 40 basis points for Risk Category IV. See the FDIC's proposal on risk-based assessments.

ratio without any consideration of factors such as the impact of high assessments on the banking industry. Under the Reform Act, even if the reserve ratio falls below 1.15%, the FDIC has up to five years to restore the reserve ratio to above that amount. We urge, therefore, that the FDIC determine that three to five years is an appropriate time frame for the DIF to achieve its proposed DRR.

Setting the DRR

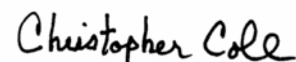
The FDIC's proposal provides little economic analysis or justification for establishing a DRR of 1.25%. Other than stating that the performance of the industry and the economy has been strong and citing a few statistics on economic growth, the FDIC has not sufficiently explained its economic rationale for why the DRR should be at 1.25% as opposed to something lower or higher. If the FDIC sets the DRR arbitrarily at 1.25% for now, it should conduct and publish a more thorough analysis of the DRR within the next two years. The arbitrary setting of the DRR at 1.25% is more reason that premiums should not be set artificially high to achieve the DRR quickly.

Conclusion

The FDIC should use the maximum authority and flexibility it has under the Reform Act to build up DIF reserves to meet the DRR steadily and gradually over the next three to five years. There should be a period of transition to allow banks to gradually use up their one-time assessment credits and to adjust to paying premiums again under the new risk-based assessment system. Establishing the assessment rates for the next several years close to the base schedule of rates would ensure a smooth transition to the new assessment system without unnecessarily impacting bank capital and earnings.

If you have any questions about our comments, please do not hesitate to contact me at 202-659-8111 or Chris.Cole@icba.org.

Sincerely,



Christopher Cole

Regulatory Counsel