■ 2. Revise § 345.12(u)(1) to read as follows:

§ 345.12 Definitions.

* * * * *

(u) *Small bank*—(1) *Definition.* Small bank means a bank that, as of December 31 of either of the prior two calendar years, had assets of less than $1.109 billion. Intermediate small bank means a small bank with assets of at least $277 million as of December 31 of both of the prior two calendar years and less than $1.109 billion as of December 31 of either of the prior two calendar years.

* * * * *

Department of the Treasury

Office of Thrift Supervision

12 CFR Chapter V

■ For the reasons discussed in the joint preamble, 12 CFR part 563e is amended as follows:

PART 563e—COMMUNITY REINVESTMENT

■ 1. The authority citation for part 563e continues to read as follows:

Authority: 12 U.S.C. 1462a, 1463, 1464, 1467a, 1814, 1816, 1828(c), and 2901 through 2907.

■ 2. Revise § 563e.12(u)(1) to read as follows:

§ 563e.12 Definitions.

* * * * *

(u) *Small savings association*—(1) *Definition. Small savings association* means a savings association that, as of December 31 of either of the prior two calendar years, had assets of less than $1.109 billion. *Intermediate small savings association* means a small savings association with assets of at least $277 million as of December 31 of both of the prior two calendar years and less than $1.109 billion as of December 31 of either of the prior two calendar years.

* * * * *

Dated: December 16, 2008.

Julie L. Williams,

First Senior Deputy Comptroller and Chief Counsel.

By order of the Board of Governors of the Federal Reserve System.

Dated: December 16, 2008.

Robert deV. Frierson,

Deputy Secretary of the Board.

By order of the Board of Directors.

Dated at Washington, DC, this 16th day of December, 2008.

Federal Deposit Insurance Corporation.

Robert E. Feldman,

Executive Secretary.

Dated: December 11, 2008.

By the Office of Thrift Supervision.

John M. Reich,

Director.

[FR Doc. E8–30433 Filed 12–19–08; 8:45 am]

BILLING CODE 4810–33–P; 6210–01–P; 6714–01–P; 6720–01–P

FEDERAL DEPOSIT INSURANCE CORPORATION

12 CFR Part 327

RIN 3064–AD35

Risk Based Assessments

AGENCY: Federal Deposit Insurance Corporation (FDIC).

ACTION: Final rule.

SUMMARY: The FDIC is amending our regulations to increase risk-based assessment rates effective for the first quarter 2009 assessment period. This is in accordance with the Restoration plan for the DIF published on October 16, 2008, in the **Federal Register**.

DATES: The final rule will become effective on January 1, 2009.

FOR FURTHER INFORMATION CONTACT: Matthew Green, Chief, Fund Analysis and Pricing Section, Division of Insurance and Research, (202) 898–3670; and Christopher Bellotto, Counsel, Legal Division, (202) 898–3801.

SUPPLEMENTARY INFORMATION:

I. Background: Restoration Plan and Proposed Rule

Recent failures of FDIC-insured institutions caused the reserve ratio of the Deposit Insurance Fund (DIF) to decline from 1.19 percent as of March 30, 2008, to 1.01 percent as of June 30 and 0.76 percent as of September 30. The FDIC expects a higher rate of institution failures in the next few years compared to recent years, leading to a further decline in the reserve ratio. Because the fund reserve ratio fell below 1.15 percent as of June 30 and was expected to remain below 1.15 percent, the Reform Act required the FDIC to establish and implement a Restoration Plan to restore the reserve ratio to at least 1.15 percent within five years.

On October 7, 2008, the FDIC established a Restoration Plan for the DIF, published on October 16 (see 73 FR 61598). In the FDIC's view, restoring the reserve ratio to at least 1.15 percent within five years requires an increase in assessment rates. Since the current rates are already three basis points above the existing base rate schedule, a new rulemaking was required. Consequently, the FDIC Board of Directors adopted, also on October 7, 2008, a notice of proposed rulemaking with request for comments on revisions to the FDIC's assessment regulations (12 CFR part 327).[1] The rulemaking proposed that, effective January 1, 2009, current assessment rates would increase uniformly by 7 basis points for the first quarter 2009 assessment period. Effective April 1, 2009, the rulemaking proposed to alter the way in which the FDIC's risk-based assessment system differentiates for risk and set new deposit insurance assessment rates. Also effective on April 1, 2009, the proposal would make technical and other changes to the rules governing the risk-based assessment system. The proposed rule was published concurrently with the Restoration Plan on October 16, 2008 (see 73 FR 61560), with a comment period scheduled to end on November 17, 2008.

On November 7, 2008, the FDIC Board approved an extension of the comment period until December 17, 2008, on the parts of the proposed rulemaking that would become effective on April 1, 2009. The comment period for the proposed 7 basis point rate increase for the first quarter of 2009, with its separate proposed effective date of January 1, 2009, was not extended and expired on November 17, 2008.

This final rule will implement a uniform increase to current rates for the first quarter 2009 assessment period only. The FDIC will issue another final rule early in 2009, to be effective April 1, 2009, to change the way that the FDIC's assessment system differentiates for risk, to set new assessment rates beginning with the second quarter of 2009, and make certain technical and other changes to the assessment rules.

II. The Final Rule: Assessment Rate Schedule for the First Quarter of 2009

The final rule raises the current rates uniformly by 7 basis points for the quarterly assessment period beginning January 1, 2009 only. The higher assessments would be reflected in the fund balance as of March 31, 2009, and collected on June 30, 2009. Rates for the first quarter of 2009 are shown in Table 1 as follows:

[1] At the same meeting, the Board set the Designated Reserve Ratio of the DIF at 1.25 percent for 2009.

TABLE 1—ASSESSMENT RATES FOR THE FIRST QUARTER OF 2009

	Risk category				
	I *		II	III	IV
	Minimum	Maximum			
Annual Rates (in basis points)	12	14	17	35	50

* Rates for institutions that do not pay the minimum or maximum rate would vary between these rates.

III. Factors Considered in Setting First Quarter 2009 Assessment Rates

Summary

The FDIC expects that the economic downturn and continuing troubles in the housing and construction sectors, financial markets, and commercial real estate will prolong the challenging operating environment that banks and thrifts face. Losses experienced by many large institutions in recent quarters are likely to spread to a growing number of small institutions. The percentage of the industry that is unprofitable is expected to remain high, primarily due to asset quality problems. These troubles lead the FDIC to project an increase in failures and higher losses to the insurance fund compared to recent years. The insurance fund balance and reserve ratio are likely to decline further before increased assessment revenue can begin to offset the effects of higher losses.

Since the October proposed rulemaking, the FDIC has updated its projections through the first quarter of 2009 of losses and other factors affecting the reserve ratio. The FDIC bases its updated near-term loss projections on analysis of specific troubled institutions, analysis of recent and expected loss rates given failure, as well as the stress analyses of the effects of housing price declines and an economic slowdown underlying the projections included in the October proposed rulemaking.

The FDIC also assumes that insured deposits would increase at an annual rate between 5 and 6 percent through March of next year. (Insured deposits include only those under the basic limit of $100,000 and $250,000 for retirement accounts.) [2] For the four quarters ending September 30, 2008, insured deposits rose 7.1 percent. Over the 5-year period ending in September, insured deposits rose at an average annual rate of 5.9 percent.

Table 2 shows projected reserve ratios for the fourth quarter of 2008 and first quarter of 2009 for alternative insured deposit growth assumptions. At 5 or 6 percent insured deposit growth, the reserve ratio would fall from 0.76 percent in the third quarter of 2008 to 0.61 percent at the end of the year. It would rise slightly to 0.63 percent (assuming 5 percent insured deposit growth) or 0.62 percent (with 6 percent growth) in the first quarter of 2009 due to the increase in assessment rates adopted in the final rule. In the absence of the rate increase, the reserve ratio would end the first quarter at 0.60 percent (with 5 or 6 percent insured deposit growth).

TABLE 2—PROJECTED RESERVE RATIOS

[September 30, 2008 reserve ratio = 0.76 percent]

Quarter ending	Annualized insured deposit growth *			
	4%	5%	6%	7%
12/31/2008	0.61%	0.61%	0.61%	0.60%
3/31/2009 (without rate increase)	0.60%	0.60%	0.60%	0.59%
3/31/2009 (with 7 b.p. rate increase)	0.63%	0.63%	0.62%	0.62%

* Assumes assessable (domestic) and insured deposits increase at the same rate. Estimated insured deposits do not include those resulting from the temporary coverage limit increase to $250,000 under the Emergency Economic Stabilization Act of 2008, or those non-interest bearing transaction deposits covered by the Temporary Liquidity Guarantee Program.

The rates adopted in the final rule for the first quarter of 2009 will raise almost as much assessment revenue as the rates that would become effective beginning April 1, 2009 under the October proposed rulemaking. Combining the updated near-term projections above with the longer-term projections included in the October proposed rulemaking and the proposed assessment rates effective April 1, the FDIC expects that the reserve ratio will reach 0.69 percent by the end of 2009. By the end of 2013—the last year of the Restoration Plan—the reserve ratio is projected to reach 1.21 percent, allowing for a margin for error in achieving the 1.15 percent threshold if the FDIC's assumptions do not hold.[3] However, the FDIC will update its longer-term projections for the insurance fund before adopting a final rule on assessment rates and risk-based pricing changes that would take effect in the second quarter of next year.

The FDIC recognizes that there is considerable uncertainty about its projections for losses and insured deposit growth, and that changes in assumptions about these and other factors could lead to different assessment revenue needs and rates. Under the terms of the Restoration Plan, the FDIC must update its projections for the insurance fund balance and reserve ratio at least semiannually while the plan is in effect and adjust rates as necessary. In the event that losses

[2] Estimated insured deposits do not include those resulting from the temporary coverage limit increase to $250,000 under the Emergency Economic Stabilization Act of 2008, or those non-interest bearing transaction deposits covered by the Temporary Liquidity Guarantee Program.

[3] In the October proposed rulemaking, the FDIC's best estimate of the cost of failures over the six years from 2008 through 2013 was about $40 billion and its projected 2013 ending reserve ratio was 1.26 percent. Combining updated near-term loss estimates with the longer term forecasts from October, total failures costs for 2008–13 are now projected to exceed $42 billion, contributing to a lower projected reserve ratio for 2013.

exceed the FDIC's best estimate or insured deposit growth is more rapid than expected, the Board will be able to adjust assessment rates.

Analysis

In setting assessment rates, the FDIC's Board of Directors has considered the following factors as required by statute:

(i) The estimated operating expenses of the Deposit Insurance Fund.

(ii) The estimated case resolution expenses and income of the Deposit Insurance Fund.

(iii) The projected effects of the payment of assessments on the capital and earnings of insured depository institutions.

(iv) The risk factors and other factors taken into account pursuant to section 7(b)(1) of the Federal Deposit Insurance Act (12 U.S.C. 1817(b)(1)) under the risk-based assessment system, including the requirement under section 7(b)(1)(A) of the Federal Deposit Insurance Act (12 U.S.C. 1817(b)(1)(A)) to maintain a risk-based system.

(v) Other factors the Board of Directors has determined to be appropriate.[4]

The factors considered in setting assessment rates are discussed in more detail below.

Case Resolution Expenses (Insurance Fund Losses)

A higher rate of failures is likely to cause the insurance fund balance and reserve ratio to decline at least through the end of 2008 before increased assessment revenue can begin to offset the effects of increased losses. The economic downturn and continuing troubles in the housing and construction sectors, financial markets, and commercial real estate will prolong the challenging operating environment that banks and thrifts face going into 2009. Losses experienced by many large institutions in recent quarters are likely to spread to a growing number of small institutions. The percentage of the industry that is unprofitable is expected to remain high, primarily due to asset quality problems.

The FDIC's updated near-term projections relied heavily on supervisory analysis of specific troubled institutions. Recent and expected loss rates given failure and stress analyses of the effects of housing price declines and an economic slowdown in specific geographic areas on loan losses and bank capital also served as a basis for insurance fund loss projections.

The FDIC estimates that failures in all of 2008 will cost the insurance fund $18.9 billion. After taking into account a projected year-end 2008 contingent loss reserve for anticipated failures, insurance fund loss provisions for 2008 are currently projected to total $30.4 billion.[5] For the fourth quarter, failures are expected to cost $4.8 billion and loss provisions are estimated at $7.7 billion.[6] The fund is also projected to incur another $1.1 billion in loss provisions during the first quarter of next year.

Before considering the final rule on changes to risk-based pricing rules and assessment rates beginning the second quarter of 2009, the FDIC will update its long-term stress analyses and other factors and assumptions underlying its projections of losses in 2009 and over the five-year Restoration Plan horizon.

Operating Expenses and Investment Income

Operating expenses are projected to average close to $300 million per quarter in the fourth quarter of 2008 and first quarter of 2009.

The FDIC projects that its investment contributions (investment income and realized gains on the sale of securities, plus or minus unrealized gains or losses on available-for-sale securities) will average $309 million per quarter in the fourth quarter of this year and first quarter of next year. The FDIC is investing new funds in overnight investments and short-term Treasury bills to accommodate increased bank failure activity. The FDIC generally expects that these investments will earn lower rates than the longer-term securities that they are replacing, particularly given the consensus forecast of a near-term decline in Treasury rates, and will therefore result in less interest income to the fund.[7]

Assessment Revenue, Credit Use, and the Distribution of Assessments

The FDIC expects that assessment revenue in 2008 will total about $3.0 billion: $4.4 billion in gross assessments charged less $1.4 billion in credits used. Fourth quarter revenue is projected at about $1.0 billion. By the end of 2008, the projections indicate that only 4 percent of the original $4.7 billion in credits awarded will be remaining. Under the statutory provisions governing the Restoration Plan, the FDIC has the authority to restrict credit use while the plan is in effect, providing that institutions may still apply credits against their assessments equal to the lesser of their assessment or 3 basis points.[8] The FDIC concluded not to restrict credit use in the Restoration Plan. The FDIC projects that the amount of credits remaining at the time that the proposed new rates go into effect will be very small and that their continued use would have very little effect on the assessment rates necessary to meet the requirements of the plan.[9]

The FDIC projects that the 7 basis point uniform increase in rates adopted in the final rule for the first quarter of 2009 will result in first quarter assessment revenue of just over $2.3 billion, about $1.2 billion more than in the absence of a rate increase. The FDIC derived its assessment revenue projections by assigning each insured institution to an assessment rate based on the current rate schedule for the fourth quarter and the rate schedule adopted in the final rule for the first quarter of next year. It then adjusted each institution's assessment for any remaining credits. For the fourth quarter of 2008, the FDIC estimated an industry average rate of approximately 6.4 basis points, increasing to approximately 13.4 basis points in the first quarter of 2009.

Estimated Insured Deposits

The FDIC believes that it is reasonable to plan for annual insured deposit growth of between 5 and 6 percent through the first quarter of next year. Over the 12 months ending September 30, 2008, estimated insured deposits

[4] Section 2104 of the Reform Act (amending section 7(b)(2) of the Federal Deposit Insurance Act, 12 U.S.C. 1817(b)(2)(B)). The risk factors referred to in factor (iv) include:

(i) The probability that the Deposit Insurance Fund will incur a loss with respect to the institution, taking into consideration the risks attributable to—

(I) Different categories and concentrations of assets;

(II) Different categories and concentrations of liabilities, both insured and uninsured, contingent and noncontingent; and

(III) Any other factors the Corporation determines are relevant to assessing such probability;

(ii) The likely amount of any such loss; and

(iii) The revenue needs of the Deposit Insurance Fund.

Section 7(b)(1)(C) of the Federal Deposit Insurance Act (12 U.S.C. 1817(b)(1)(C)).

[5] The $30.4 billion 2008 loss provision is derived by adding $18.9 billion for the cost of failures, $11.5 billion for the contingent loss reserve, and another $0.1 billion adjustment for failures in earlier years, then subtracting the $0.1 billion year-end 2007 contingent loss reserve.

[6] The $7.7 billion fourth quarter loss provision is derived by adding $4.8 billion for the cost of failures, $11.5 billion for the contingent loss reserve, and another $3.1 billion adjustment for failures occurring prior to the fourth quarter, then subtracting the $11.7 billion third quarter contingent loss reserve.

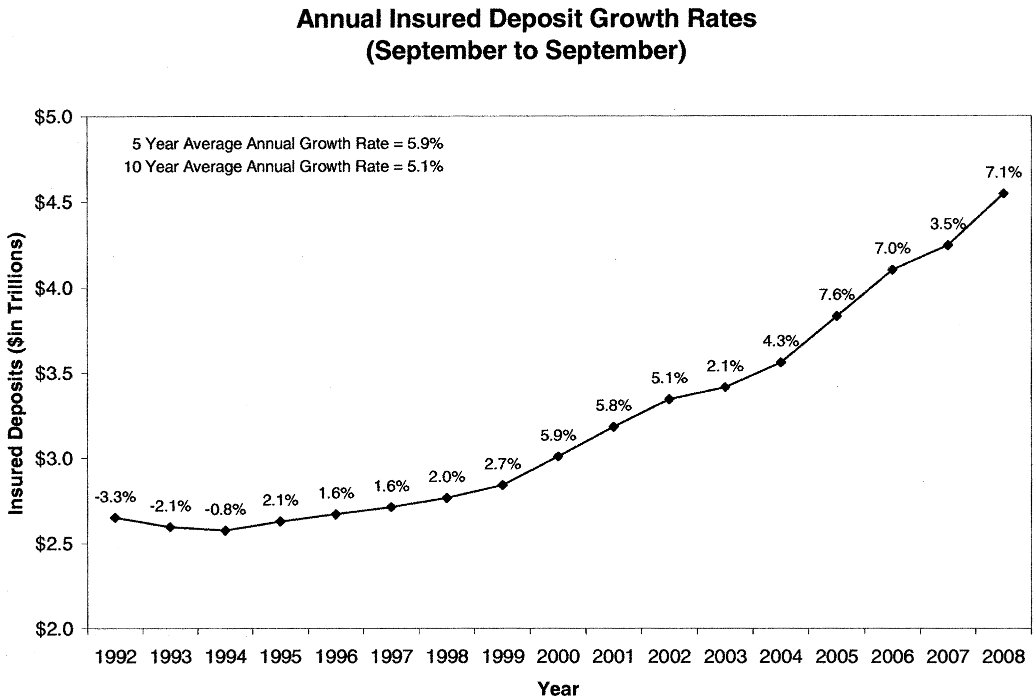
[7] Projections of interest rates are based on consideration of December Blue Chip Financial Forecasts.

[8] Section 7(b)(3)(E)(iv) of the Federal Deposit Insurance Act (12 U.S.C. 1817(b)(3)(E)(iv)).

[9] For 2008, 2009 and 2010, credits may not offset more than 90 percent of an institution's assessment. Section 7(e)(3)(D)(ii) of the Federal Deposit Insurance Act (12 U.S.C. 1817(e)(3)(D)(ii)).

increased by 7.1 percent.[10] However, the most recent 5- and 10-year averages are about 6 percent and 5 percent, respectively. Chart 1 depicts insured deposit growth rates since 1992.

Chart 1



Projections of insured deposits are subject to considerable uncertainty. Insured deposit growth over the near term could continue to rise at the more rapid pace observed in the third quarter (1.8 percent, or 7.2 percent annualized) due to a ‘‘flight to quality’’ attributable to financial and economic uncertainties. On the other hand, as the experience of the late 1980s and early 1990s demonstrated, lower overall growth in the banking industry and the economy could depress rates of growth of total domestic and insured deposits. As Table 2 shows, differences in annualized growth rates of insured deposits over the next couple of quarters will have little effect on the projected reserve ratio as of March 31, 2009.

Projected Fund Balances, Insured Deposits, and Reserve Ratios

Assuming annualized insured deposit growth of 5 percent through March of next year, projections of fund income, expenses, and losses, the fund balance, estimated insured deposits, and the reserve ratio are shown below in Table 3.

TABLE 3—PROJECTED FUND BALANCE, ESTIMATED INSURED DEPOSITS, AND RESERVE RATIO UNDER THE RATES ADOPTED IN THE FINAL RULE ASSUMING 5 PERCENT ANNUAL INSURED DEPOSIT GROWTH

[$ in billions]

	4th Qtr 2008	1st Qtr 2009
Beginning Fund Balance	34.6	28.0
Plus: Net Assessment Revenue	1.0	2.3
Plus: Investment Income	0.3	0.3
Less: Loss Provisions	7.7	1.1
Less: Operating Expenses	0.3	0.3
Ending Fund Balance	28.0	29.1
Estimated Insured Deposits	4,599.5	4,656.0
Ending Reserve Ratio	0.61%	0.63%

Note: Components of fund balance changes may not sum to totals due to rounding.

[10] Estimated insured deposits do not include those resulting from the temporary coverage limit increase to $250,000 under the Emergency Economic Stabilization Act of 2008, or those non-interest bearing transaction deposits covered by the Temporary Liquidity Guarantee Program.

Effect on Capital and Earnings

Appendix 1 contains an analysis of the effect of proposed rates on the capital and earnings of insured institutions. Given the assumptions in the analysis, for the industry as a whole, projected total assessments in the first quarter of 2009 would result in capital that would be 0.12 percent lower than if the FDIC did not charge assessments and 0.04 percent lower than if current assessment rates remained in effect. The proposed assessments would cause 3 institutions whose equity-to-assets ratio would have exceeded 4 percent in the absence of assessments to fall below that percentage and 2 institutions to fall below 2 percent. The proposed *increase* in assessments would cause 1 institution whose equity-to-assets ratio would have exceeded 4 percent under current assessments to fall below that threshold and no institutions to fall below 2 percent equity-to-assets.

For profitable institutions, assessments in the first quarter of 2009 would result in pre-tax income that would be 5.9 percent lower than if the FDIC did not charge assessments and 3.4 percent lower than if current assessment rates remained in effect. For unprofitable institutions, assessments would result in pre-tax losses that would be 4.4 percent higher than if the FDIC did not charge assessments and 2 percent higher than if current assessment rates remained in effect.

IV. Comments Received on the Proposal

The FDIC received comments from three nationwide industry trade groups and a few banks that specifically addressed the 7 basis point increase in assessment rates for the first quarter of 2009. The FDIC also received many comments from banks and others concerning rates for all of 2009 and beyond. Several of them also discussed proposed changes to risk-based pricing methods beginning in the second quarter of 2009.

One of the nationwide industry trade groups criticized the magnitude of the first quarter increase and expressed concern about the pace at which the FDIC would restore the insurance fund. It argued that the proposed assessment rates are too high—especially in the early stages of the Restoration Plan—and questioned why the FDIC does not take advantage of the flexibility that Congress provided to extend the restoration period beyond five years under ''extraordinary circumstances.'' The trade group argued that the FDIC's invocation of its systemic risk authority to provide additional guarantees on non-interest bearing transaction deposits and senior unsecured debt is evidence of ''extraordinary circumstances.'' The group believes that high premiums would restrain credit and run counter to other government efforts designed to stimulate lending. It urged the FDIC to implement a longer recapitalization period, such as six or seven years, and to rely on lower insured deposit growth assumptions to achieve a more moderate increase in rates. The comment letter recommended that the FDIC consider phasing in higher assessment rates and argued that it was counter-intuitive for the proposed minimum rate in the first quarter (12 basis points) to be higher than the proposed minimum rate in the second quarter (10 basis points initially and as low as 8 basis points after adjustments).

Another nationwide industry trade group commenting on the first quarter 2009 rate increase urged the FDIC to adopt a more modest increase in assessment rates and to use its ''extraordinary circumstances'' authority to extend the restoration period to at least seven years. The comment expressed the view that a smaller rate increase would keep additional funds in local communities for lending to small businesses and consumers during the current period of economic stress.

A third nationwide industry trade group estimated that the proposed 7 basis point assessment rate increase would reduce the banking industry's pre-tax income by 7 percent or more at a time when the industry needs to build its capital. It requested that the FDIC and other bank regulators take steps to reduce losses to the DIF from insured institution failures. To the extent that such efforts to reduce losses succeeded, the FDIC should develop a revised plan incorporating lower assessment rates.

One bank specifically discussing the first quarter 2009 proposed assessment rates described the measure as ''ill-timed,'' given current pressures on banks' capital and profitability, and urged the FDIC to implement a more modest increase. Another expressed concern that the increase would make it more difficult for safe and well-managed institutions to meet local credit needs.

As noted before, many comments received from banks and others pertained to the proposed increase in rates for all of 2009 and beyond (as well as proposed changes to risk-based pricing methods). Two comment letters supported the proposed changes to the assessment system, including the increase in premiums. Many commenters made similar points to those of the three industry trade groups. Several comments from banks and from state trade groups opposed any significant increase in assessment rates in the short term because many institutions are struggling to maintain adequate levels of capital and profitability. Several commenters urged the FDIC to withdraw the proposed rule and delay increasing assessment rates and overhauling the assessment system until the end of 2009. They argued that the delay would allow time for a thorough evaluation of the effectiveness of measures recently taken by the Federal government to restore stability to the banking system. One comment asserted that the proposed Restoration Plan penalizes safe and well-run community banks and urged the FDIC to require the largest banks to recapitalize the DIF. Finally, several comments urged the FDIC to invoke its ''extraordinary circumstances'' authority to extend the time period to rebuild the DIF from five to at least ten years. By lengthening the restoration period, the FDIC could keep assessments at a more moderate level, thereby reducing the burden on institutions during stressful periods.

The FDIC agrees with comments that significant increases in deposit insurance premium rates in times of economic and financial stress are not desirable. Indeed, the FDIC sought for several years legislative reforms that would allow it to charge every insured institution a risk-based premium regardless of the level of the reserve ratio, and to have the ability to let the fund rise under good economic conditions in order to have room to decline under adverse conditions without needing to sharply increase premium rates. The reforms sought by the FDIC became law in February 2006, and most of the implementing regulations became effective at the start of 2007. However, the one-time assessment credits granted to over 80 percent of the industry did not enable the fund to earn significant new revenue last year, resulting in only a 1 basis point increase in the reserve ratio during all of 2007. Thus, the insurance fund was unable to increase sufficiently to prevent the increase in failures this year from causing the reserve ratio to fall below the 1.15 percent lower bound established by Congress. While Congress gave the FDIC new flexibility to manage the fund, it prescribed limits on how much the reserve ratio could decline, requiring the FDIC to implement a Restoration Plan to increase the fund to at least 1.15 percent generally within five years. In the FDIC's view, higher premiums are necessary to meet this statutory requirement.

As the trade groups and many other commenters noted, the law does allow

FDIC to take longer than five years for the reserve ratio to reach 1.15 percent FDIC due to ''extraordinary circumstances.'' The FDIC recognizes the current severe strains on banks and the financial system. The FDIC's Temporary Liquidity Guarantee Program (TLGP) is part of a coordinated effort by the government—including the Treasury Department's Troubled Assets Relief Program (TARP) and the Federal Reserve's Commercial Paper Funding Facility—to stabilize the financial system and provide much needed liquidity. However, in the FDIC's view, it would be premature to conclude at this time that extraordinary circumstances should warrant extending the Restoration Plan horizon beyond five years. There is considerable uncertainty about future insurance fund losses and insured deposit growth. Under the Restoration Plan published in October, the FDIC will update its projections at least semiannually while the plan is in effect and adjust rates as necessary. As the FDIC updates its projections to account for changing conditions, it could also determine whether it is appropriate to adjust the time frame for reaching the 1.15 percent target due to extraordinary circumstances.

While higher deposit insurance premiums next year will result in lower industry earnings than would otherwise be the case, the FDIC believes that the coordinated efforts by the Treasury, Federal Reserve, and FDIC to expand banking system liquidity will help enable banks to increase lending to communities and businesses.

Finally, if Congress did not enact the reforms in 2006 that FDIC had sought, the FDIC would have to increase the reserve ratio to 1.25 percent within one year or charge an average rate on assessable deposits of at least 23 basis points. Banks and thrifts, in fact, did pay a minimum of 23 basis points in the early 1990s to rebuild the insurance funds.[11] The first quarter 2009 rates adopted in the final rule are significantly lower—most banks will be charged an annual rate between 12 and 14 basis points.

V. Effective Date

The final rule will take effect January 1, 2009, for the assessment for the first quarter of 2009.

VI. Regulatory Analysis and Procedure

A. Administrative Procedure Act

The final rule setting assessment rates for the first assessment period of 2009 will become effective on January 1, 2009. In this regard, the FDIC invokes the good cause exception to the requirements in the Administrative Procedure Act that, once finalized, a rulemaking must have a delayed effective date of thirty days from the publication date.[12] The FDIC has determined that good cause exists for waiving the customary 30-day delayed effective date.

Recent failures of FDIC-insured institutions caused the reserve ratio of the DIF to decline from 1.19 percent as of March 31, 2008, to 0.76 percent as of September 30, 2008. Furthermore, the FDIC expects a higher rate of institution failures in the next few years compared to recent years, leading to a further decline in the reserve ratio. Under these circumstances, the FDIC is required by statute to establish and implement a restoration plan to restore the reserve ratio to no less than 1.15 percent within five years. In light of the current reserve ratio, the continuing unusual and exigent circumstances in the banking system, and the statutory requirements, restoring the reserve ratio to at least 1.15 percent within five years requires an increase in assessment rates, including an increase in the assessment rates for the first quarter of 2009. For these reasons, the FDIC finds that good cause exists to justify a January 1, 2009 effective date.

B. Solicitation of Comments on Use of Plain Language

Section 722 of the Gramm-Leach-Bliley Act, Public Law 106–102, 113 Stat. 1338, 1471 (Nov. 12, 1999), requires the federal banking agencies to use plain language in all proposed and final rules published after January 1, 2000. The FDIC invited comments on how to make this proposal easier to understand and received one response. The comment (which did not distinguish between the provisions effective January 1, 2009, and those effective April 1, 2009) stated that the proposal was too complicated and should have included an executive summary in bullet point format.

C. Regulatory Flexibility Act

The Regulatory Flexibility Act (RFA) requires that each federal agency either certify that a proposed rule would not, if adopted in final form, have a significant economic impact on a substantial number of small entities or prepare an initial regulatory flexibility analysis of the proposal and publish the analysis for comment.[13] Certain types of rules, such as rules of particular applicability relating to rates or corporate or financial structures, or practices relating to such rates or structures, are expressly excluded from the definition of ''rule'' for purposes of the RFA.[14] The final rule relates directly to the rates imposed on insured depository institutions for deposit insurance. Nevertheless, the FDIC voluntarily undertook a regulatory flexibility analysis to aid the public in commenting upon the small business impact of the proposed rule. The initial regulatory flexibility analysis was published in the **Federal Register** (73 FR 61560) on October 16, 2008. Public comment was invited. The FDIC received no comments on the initial regulatory flexibility analysis regarding the 7 basis point increase in assessment rates proposed for the first quarter of 2009 only.

As of September 30, 2008, of the 8,384 insured commercial banks and savings institutions, there were 4,753 small insured depository institutions as that term is defined for purposes of the RFA (*i.e.*, those with $165 million or less in assets).[15]

The FDIC's total assessment needs are driven by the statutory requirement that the FDIC adopt a Restoration Plan that provides that the fund reserve ratio reach at least 1.15 percent within five years (absent extraordinary circumstances) and by the FDIC's aggregate insurance losses, expenses, investment income, and insured deposit growth, among other factors. Under the final rule, each institution's existing rate for the first quarter of 2009 is increased uniformly by 7 basis points to help meet FDIC assessment revenue needs. Apart from the uniform increase in rates on all institutions to help meet the FDIC's total revenue needs, the final rule makes no other changes in rates for any insured institution, including small insured depository institutions. The final rule increasing assessment rates uniformly by 7 basis points across the board for all institutions, including small institutions for RFA purposes, does not alter the present distribution of assessment rates.

The final rule does not directly impose any ''reporting'' or ''recordkeeping'' requirements within the meaning of the Paperwork

[11] The insurance funds were the Bank Insurance Fund and Savings Association Insurance Fund. The funds were merged in 2006.

[12] 5 U.S.C. 553(d)(3).

[13] See 5 U.S.C. 603, 604 and 605.

[14] 5 U.S.C. 601

[15] Throughout this regulatory flexibility analysis (unlike the rest of the notice of proposed rulemaking), a ''small institution'' refers to an institution with assets of $165 million or less.

Reduction Act. The compliance requirements for the proposed rule would not exceed existing compliance requirements for the present system of FDIC deposit insurance assessments, which, in any event, are governed by separate regulations.

The FDIC is unaware of any duplicative, overlapping or conflicting federal rules.

D. Paperwork Reduction Act

No collections of information pursuant to the Paperwork Reduction Act (44 U.S.C. 3501 *et seq.*) are contained in the proposed rule.

E. The Treasury and General Government Appropriations Act, 1999—Assessment of Federal Regulations and Policies on Families

The FDIC has determined that the final rule will not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, enacted as part of the Omnibus Consolidated and Emergency Supplemental Appropriations Act of 1999 (Pub.L. 105–277, 112 Stat. 2681).

F. Small Business Regulatory Enforcement Fairness Act

The Office of Management and Budget has determined that the final rule is not a ''major rule'' within the meaning of the relevant sections of the Small Business Regulatory Enforcement Act of 1996 (SBREFA) Public Law No. 110–28 (1996). As required by law, the FDIC will file the appropriate reports with Congress and the General Accounting Office so that the final rule may be reviewed.

List of Subjects in 12 CFR Part 327

Bank deposit insurance, Banks, banking, Savings associations.

■ For the reasons set forth in the preamble, the FDIC proposes to amend chapter III of title 12 of the Code of Federal Regulations as follows:

PART 327—ASSESSMENTS

■ 1. The authority citation for part 327 continues to read as follows:

Authority: 12 U.S.C. 1441, 1813, 1815, 1817–1819, 1821; Sec. 2101–2109, Pub. L. 109–171, 120 Stat. 9–21, and Sec. 3, Pub. L. 109–173, 119 Stat. 3605.

■ 2. In § 327.10 add a new paragraph (d) to read as follows:

§ 327.10 Assessment rate schedules.

* * * * *

(d) *Assessment Rate Schedule for First Assessment Period of 2009.* The annual assessment rate for an insured depository institution for the assessment period beginning January 1, 2009 and ending March 31, 2009, shall be the rate prescribed in the following schedule:

	Risk category				
	I *		II	III	IV
	Minimum	Maximum			
Annual Rates (in basis points)	12	14	17	35	50

* Rates for institutions that do not pay the minimum or maximum rate will vary between these rates.

(1) *Risk Category I Rate Schedule.* The annual assessment rates for all institutions in Risk Category I shall range from 12 to 14 basis points.

(2) *Risk Category II, III, and IV Rate Schedule.* The annual assessment rates for Risk Categories II, III, and IV shall be 17, 35, and 50 basis points respectively.

(3) All institutions in any one risk category, other than Risk Category I, will be charged the same assessment rate.

Note: This Appendix will not appear in the Code of Federal Regulations.

Appendix 1—Analysis of the Projected Effects of the Payment of Assessments on the Capital and Earnings of Insured Depository Institutions

I. Introduction

This analysis estimates the effect of the deposit insurance assessments adopted in the final rule for the first quarter of 2009 on the equity capital and profitability of all insured institutions. The analysis assumes that each institution's pre-tax, pre-assessment income in the first quarter is equivalent to one fourth of the amount reported over the four quarters ending in September 2008. Each institution's rate under the rate schedule is based on data as of September 30, 2008.[16] In addition, the projected use of one-time credits authorized under the Reform Act is taken into consideration in determining the effective assessment for an institution.

II. Analysis of the Projected Effects on Capital and Earnings

While deposit insurance assessment rates generally will result in reduced institution profitability and capitalization compared to the absence of assessments, the reduction will not necessarily equal the full amount of the assessment. Two factors can mitigate the effect of assessments on institutions' profits and capital. First, a portion of the assessment may be transferred to customers in the form of higher borrowing rates, increased service fees and lower deposit interest rates. Since information is not readily available on the extent to which institutions are able to share assessment costs with their customers, however, this analysis assumes that institutions bear the full after-tax cost of the assessment. Second, deposit insurance assessments are a tax-deductible operating expense; therefore, the assessment expense can lower taxable income. This analysis considers the effective after-tax cost of assessments in calculating the effect on capital.[17]

An institution's earnings retention and dividend policies also influence the extent to which assessments affect equity levels. If an institution maintains the same *dollar* amount of dividends when it pays a deposit insurance assessment as when it does not, equity (retained earnings) will be less by the full amount of the after-tax cost of the assessment. This analysis instead assumes that an institution will maintain its dividend *rate* (that is, dividends as a fraction of net income) unchanged from the weighted average rate reported over the four quarters ending September 30, 2008. In the event that the ratio of equity to assets falls below 4 percent, however, this assumption is modified such that an institution retains the amount necessary to achieve a 4 percent minimum and distributes any remaining funds according to the dividend payout rate.

The equity capital of insured institutions as of September 30, 2008 was $1.304 trillion. Based on the assumptions for earnings described above, March 31, 2009 equity capital is projected to equal $1.302 trillion under the rates adopted in the final rule. In the absence of an assessment, total equity would be an estimated $1.6 billion higher. Alternatively, total equity would be an estimated $0.6 billion higher if current rates remained in effect.

[16] For purposes of this analysis, the assessment base (like income) is not assumed to increase, but is assumed to remain at September 2008 levels. Income is defined as income before taxes, extraordinary items, and deposit insurance assessments. Assessments are adjusted for the use of one-time credits, and all income statement items used in this analysis were adjusted for the effect of mergers. Institutions for which four quarters of earnings data were unavailable, including insured branches of foreign banks, were excluded from this analysis.

[17] The analysis does not incorporate any tax effects from an operating loss carry forward or carry back.

On an industry weighted average basis, projected total assessments through the end of the first quarter of 2009 would result in capital that is 0.1 percent less than in the absence of assessments and 0.04 percent less than if the current rates remained in effect. The analysis indicates that assessments would cause 3 institutions whose equity-to-assets ratio would have exceeded 4 percent in the absence of assessments to fall below that percentage and 2 institutions to have below 2 percent equity-to-assets that otherwise would not have. Alternatively, compared to current assessments, the increase in assessments would cause one institution whose equity-to-assets ratio would otherwise have exceeded 4 percent to fall below that threshold and no institutions to fall below 2 percent equity-to-assets.

The effect of assessments on institution income is measured by deposit insurance assessments as a percent of income before assessments, taxes, and extraordinary items (hereafter referred to as ''income''). This income measure is used in order to eliminate the potentially transitory effects of extraordinary items and taxes on profitability. For profitable institutions, the median projected reduction in income relative to the absence of assessments is 8.3 percent, while the weighted average reduction for the same institutions is 5.9 percent. For unprofitable institutions, assessments would increase losses by 4.4 percent. When compared to current rates (rather than the absence of assessments), the weighted average reduction in income for profitable institutions is 3.4 percent, while the increase in losses for unprofitable institutions is 2 percent.

By order of the Board of Directors.

Dated at Washington, DC, this 16th day of October 2008.

Federal Deposit Insurance Corporation.

Robert E. Feldman,

Executive Secretary.

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FEDERAL DEPOSIT INSURANCE CORPORATION

12 CFR Part 371

RIN 3064–AD30

Recordkeeping Requirements for Qualified Financial Contracts

AGENCY: Federal Deposit Insurance Corporation (FDIC).

ACTION: Final rule.

SUMMARY: The FDIC is adopting a final rule establishing recordkeeping requirements for qualified financial contracts (QFCs) held by insured depository institutions in a troubled condition as defined in this rule. The appendix to the rule requires an institution in a troubled condition, upon written notification by the FDIC, to produce immediately at the close of processing of the institution's business day, for a period provided in the notification, the electronic files for certain position level and counterparty level data; electronic or written lists of QFC counterparty and portfolio location identifiers, certain affiliates of the institution and the institution's counterparties to QFC transactions, contact information and organizational charts for key personnel involved in QFC activities, and contact information for vendors for such activities; and copies of key agreements and related documents for each QFC.

DATES: This final rule is effective January 21, 2009.

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SUPPLEMENTARY INFORMATION:

I. Background

QFCs are certain financial contracts that have been defined in the Federal Deposit Insurance Act (FDI Act) and receive special treatment by the FDIC in the event of the failure of an insured depository institution (institution). The special treatment of QFCs after the FDIC's appointment as receiver or conservator for a failed institution initially was codified in the FDI Act as part of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) [1] and places certain restrictions on the FDIC as receiver [2] for a failed institution that held QFCs.

The FDI Act identifies QFCs using the statutory definition of five specific financial contracts. This statutory list of QFCs consists of securities contracts, commodity contracts, forward contracts, repurchase agreements, and swap agreements.[3] The FDIC also may define other similar agreements as QFCs by rule or order.[4] In addition, a master agreement that governs any contracts in these five categories is treated as a QFC,[5] as are security agreements that ensure the performance of a contract from the five enumerated categories.[6]

Under the FDI Act and other U.S. insolvency statutes, a party to QFCs with the insolvent entity can exercise its contractual right to terminate QFCs and offset or net out any amounts due between the parties and apply any pledged collateral for payment.[7] Under the Bankruptcy Code, this right is immediate upon initiation of bankruptcy proceedings, while under the FDI Act, counterparties cannot exercise this contractual right until after 5 p.m. (Eastern Time) on the business day following the appointment of the FDIC as receiver.[8] By contrast, parties to most other contracts with insured institutions cannot terminate the contracts based upon the appointment of the FDIC as receiver.[9] The special rights granted by the FDI Act to QFC counterparties are designed to protect the stability of the financial system and to reduce the potential for cascading interrelated defaults.

If QFC counterparties were unable to terminate and liquidate their positions in a timely manner after the failure of the institution, they would be exposed to market risks and uncertainty regarding the ultimate resolution of QFCs. Absent the ability to terminate a QFC in a timely manner when the counterparty becomes insolvent (which may include exercising rights to offset positions, net payments, and use collateral to cover amounts due), the potential for fluctuation in the value of the QFCs from changes in interest rates and other market factors may create market uncertainty that could lead to broader market disruptions. Consequently, while the Bankruptcy

[1] Public Law No. 101–73, 103 Stat. 514 (August 9, 1989).

[2] Most of the restrictions applicable to the treatment of QFCs by an FDIC receiver also apply to the FDIC in its conservatorship capacity. *See* U.S.C. 1821(e)(8), (9), (10), and (11). While the treatment of QFCs by an FDIC conservator is not identical to the treatment of QFCs in a receivership, *see* 12 U.S.C. 1821(e)(8)(E) and (10)(B)(i) and (ii), for purposes of this preamble we intend reference to the FDIC in its receivership capacity to include its role as conservator under this statutory authority.

[3] 12 U.S.C. 1821(e)(8)(D)(ii)–(vi).

[4] 12 U.S.C. 1821(e)(8)(D)(i). The FDIC has provided clarifying definitions for repurchase agreements and swap agreements in 12 CFR 360.5.

[5] 12 U.S.C. 1821(e)(8)(D)(ii)(XI), (iii)(IX), (iv)(IV), (v)(V), and (vi)(V).

[6] 12 U.S.C. 1821(e)(8)(D)(ii)(XII), (iii)(X), (iv)(V), (v)(VI), and (vi)(VI).

[7] 12 U.S.C. 1821(e)(8); 11 U.S.C. 555 (securities contracts), 556 (commodities and forward contracts), 559 (repurchase agreements), 560 (swap agreements), and 561 (master netting agreements).

[8] *See* 12 U.S.C. 1821(e)(10)(B).

[9] 12 U.S.C. 1821(e)(13).