The FDIC

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The FDIC

CHAPTER 1 FDIC- How it Functions

The FDIC (Federal Deposit Insurance Corporation) is an independent agency of the United States government that protects citizens against the loss of their deposits if an FDIC-insured bank or savings association fails. FDIC insurance is backed by the full faith and credit of the United States government. Since the FDIC's creation in 1933, no depositor has ever lost even one penny of FDIC-insured funds. The FDIC insures deposits in most, but not all, banks and savings associations. Deposits in separate branches of an insured bank are not separately insured. Deposits in one insured bank are insured separately from deposits in another insured bank. All insured institutions must display an official FDIC sign at each teller window or teller station.

What It Covers

FDIC insurance covers all deposit accounts at insured banks and savings associations, including checking, NOW, and savings accounts, money market deposit accounts and certificates of deposit (CDs) up to the insurance limit. The FDIC does not insure the money invested in stocks, bonds, mutual funds, life insurance policies, annuities or municipal securities, even if the product was purchased from an insured bank or savings association. Deposits are insured up to $250,000. A depositor can have more than $250,000 at one insured bank or savings association and still be fully insured provided the accounts meet certain requirements. In addition, federal law provides for insurance coverage of up to $250,000 for certain retirement accounts. The basic FDIC coverage limits are as follows-
Single Accounts (owned by one person): $250,000 per owner
Joint Accounts (two or more persons): $250,000 per co-owner
IRAs and certain other retirement accounts: $250,000 per owner
Revocable trust accounts: Each owner is insured up to $250,000 for the interests of each beneficiary, subject to specific limitations and requirements

These deposit insurance coverage limits refer to the total of all deposits that account holders have at each FDIC-insured bank. The listing above shows only the most common ownership categories that apply to individual and family deposits, and assumes that all FDIC requirements are met.

A depositor may qualify for more than $250,000 in coverage at one insured bank or savings association if he or she owns deposit accounts in different ownership categories. The most common account ownership categories for individual and family deposits are single accounts, joint accounts, revocable trust accounts and certain retirement accounts.

Single Account

A 'single account' is a deposit account owned by one person and titled in that person's name only, with no beneficiaries. All an individual's single accounts at the same insured bank are added together and the total is insured up to $250,000. For example, if someone has a checking account and a CD at the same insured bank, and both accounts are in that individual's name only, the two accounts are added together and the total is insured up to $250,000. Note that retirement accounts and eligible trust accounts are not included in this ownership category.

Example of Insurance Coverage for Single Accounts		
Depositor	Type of Deposit	Amount Deposited
Jane Smith	Savings account	$25,000
Jane Smith	Certificate of Deposit	$250,000
Jane Smith	NOW account	$50,000
Jane Smith's sole proprietorship	Checking account	$50,000
Total Deposited		$375,000
Insurance Available		$250,000

Uninsured Amount	$125,000

Joint Account

This is a deposit account owned by two or more people and titled jointly in the co-owners' names only, with no beneficiaries. If all co-owners have equal rights to withdraw money from a joint account, a co-owner's shares of all joint accounts at the same insured bank are added together and the total is insured up to $250,000. Note that jointly owned revocable trust accounts are not included in this ownership category. If a couple has a joint checking account and a joint savings account at the same insured bank, each co-owner's shares of the two accounts are added together and insured up to $250,000 per owner, providing up to $500,000 in coverage for the couple's joint accounts.

Requirements for Joint Accounts

Joint accounts are insured separately from other ownership categories if all of the following conditions are met:
All co-owners must be natural persons. This means that legal entities such as corporations or partnerships are not eligible for joint account deposit insurance coverage.
Each of the co-owners must have personally signed a deposit account signature card. The execution of an account signature card is not required for certificates of deposit, deposit obligations evidenced by a negotiable instrument or accounts maintained by an agent, nominee, guardian, custodian, or conservator, but the deposit must in fact be jointly owned.
Each of the co-owners must have a right of withdrawal on the same basis as the other co-owners.

For example, if one co-owner can withdraw funds on his or her signature alone, but the other co-owner can withdraw funds only on the signature of both co-owners, then this requirement has not been satisfied; the co-owners do not have equal withdrawal rights. Likewise, if a co-owner's right to withdraw funds is limited to a specified dollar amount, the funds in the account will be allocated between the co-owners according to their withdrawal rights and insured as single account funds. For example, if $250,000 is deposited in the names of A and B, but A has the right to withdraw only up to $50,000 from the account, $50,000 is allocated to A and the remainder ($200,000) is allocated to B. The funds, as allocated, are then added to any other single account funds of A or B, respectively.

Example: John and Mary have three joint accounts totaling $600,000 at an insured bank. Under FDIC rules, each co-owner's share of each joint account is considered equal unless otherwise stated in the bank's records. John and Mary each own $300,000 in the joint account category, putting a total of $100,000 ($50,000 for each) over the insurance limit.

Joint Account Example		
Account Title	Type of Deposit	Account Balance
Mary and John Smith	Checking	$50,000
John or Mary Smith	Savings	$150,000
Mary Smith or John Smith	CD	$400,000
Total Deposits		$600,000

Insurance coverage for each owner is calculated as follows:			
Account Holders	Ownership Share	Amount Insured	Amount Uninsured
John	$300,000	$250,000	$50,000
Mary	$300,000	$250,000	$50,000
Total	$600,000	$500,000	$100,000

Mary's ownership share in all joint accounts equals $300,000 [1/2 of the checking account ($25,000), 1/2 of the savings account ($75,000), and 1/2 of the CD ($200,000), for a total of $300,000]. Since her coverage in the joint ownership category is limited to $250,000, $50,000 is uninsured.
John's ownership share in all joint accounts is the same as Mary's, so $50,000 is uninsured.

How joint accounts are insured

An individual's (co-owner's) interests in all qualifying joint accounts are added together and the total is insured up to the $250,000 maximum. Each co-owner's interest (or share) in a joint account is deemed equal. The balance of a joint account can exceed $250,000, as long as no owner's share of joint accounts at the same bank exceeds $250,000. The use of different Social Security numbers does not determine insurance coverage, nor does rearranging the owners' names, changing the style of the names, or using "or" rather than "and" to join the owners' names in a joint account title.

Example of Insurance Coverage for Joint Accounts		
Account Title	Owners	Balance
#1	A and B	$250,000
#2	B and A	$120,000
#3	A and B and C	$180,000
#4	A and D	$80,000
Total		$630,000

Each owner's ownership interests in these four joint accounts follow:

A's Ownership Interest	
1/2 of the balance in account #1	$125,000
1/2 of the balance in account #2	$60,000
1/3 of the balance in account #3	$60,000
1/2 of the balance in account #4	$40,000
Total of A's Ownership Interest	$285,000

A's ownership interest in the joint account category is $285,000. This amount is more than the $250,000 maximum, so $250,000 is insured and $35,000 is uninsured.

B's Ownership Interest	
1/2 of the balance in account #1	$125,000
1/2 of the balance in account #2	$60,000
1/3 of the balance in account #3	$60,000
Total of B's Ownership Interest	$245,000

B's ownership interest in the joint account category is $245,000. That amount is less than the $250,000 maximum, so B is fully insured.

C's Ownership Interest	
1/3 of the balance in account #3	$60,000
Total of C's Ownership Interest	$60,000

C's ownership interest in the joint account category is $60,000. That amount is less than the $250,000 maximum, so C is fully insured.

D's Ownership Interest	
1/2 of the balance in account #4	$40,000
Total of D's Ownership Interest	$40,000

D's ownership interest in the joint account category is $40,000. That amount is less than the $250,000 maximum, so D is fully insured.

Summary of Insurance Coverage for Joint Accounts			
Owner	Account Balance	Insured	Uninsured
A	$285,000	$250,000	$35,000
B	$245,000	$245,000	$0
C	$60,000	$60,000	$0
D	$40,000	$40,000	$0
Total	$630,000	$595,000	$35,000

Retirement Accounts

These are deposit accounts owned by one person and titled in the name of that person's retirement plan. Only the following types of retirement plans are insured in this ownership category:
Individual Retirement Accounts (IRAs) including traditional IRAs, Roth IRAs, Simplified Employee Pension (SEP) IRAs, and Savings Incentive Match Plans for Employees (SIMPLE) IRAs
Section 457 deferred compensation plan accounts (whether self-directed or not)
Self-directed defined contribution plan accounts
Self-directed Keogh plan (or H.R. 10 plan) accounts
All deposits that an individual has in any of the types of retirement plans listed above at the same insured bank are added together and the total is insured up to $250,000. For example, if an individual has an IRA and a self-directed Keogh account at the same bank, the deposits in both accounts would be added together and insured up to $250,000.
Note: Naming beneficiaries on a retirement account does not increase deposit insurance coverage.

Revocable Trust Account

This is a deposit account held as a payable on death (POD) or in trust for (ITF) account or that is established in the name of a formal revocable trust (also known as a living or family trust account).
POD and ITF accounts These are also known as testamentary or Totten Trust accounts - are the most common form of revocable trust deposits. These informal revocable trusts are created when the account owner signs an agreement - usually part of the bank's signature card - stating that the deposits will be payable to one or more beneficiaries upon the owner's death.
Living trusts - or family trusts - are formal revocable trusts created for estate planning purposes. The owner of a living trust controls the deposits in the trust during his or her lifetime. The trust document sets forth who shall receive trust assets after the death of the owner.
Deposit insurance coverage for revocable trust accounts is provided to the owner of the trust. However, the amount of coverage is based on the number of beneficiaries named in the trust and, in some cases, the interests allocated to those beneficiaries, up to the insurance limit. A trust beneficiary can be an individual (regardless of the relationship to the owner), a charity or another non-profit organization (as defined by the IRS).
Revocable trust coverage is based on all revocable trust deposits held by the same owner at the same bank, whether formal or informal. If a revocable trust account has more than one owner, each owner's coverage is calculated separately, using the following rules:
Revocable Trust Deposits with Five or Fewer Beneficiaries - Each owner's share of revocable trust deposits is insured up to $250,000 for each beneficiary (i.e., $250,000 times the number of different beneficiaries), regardless of actual interest provided to beneficiaries.
Revocable Trust Deposits with Six or More Beneficiaries - Each owner's share of revocable trust deposits is insured for the greater of either (1) coverage based on each beneficiary's actual interest in the revocable trust deposits, with no beneficiary's interest to be insured for more than $250,000, or (2) $1,250,000.
Note: Determining coverage for living trust accounts that have six or more beneficiaries and provide different interests for the trust beneficiaries can be complicated.

How revocable trust accounts are insured

Deposit insurance coverage for revocable trust accounts is provided to the owner of the trust. However, the amount of coverage is based on the number of beneficiaries named in the trust and, in some cases, the interests allocated to those beneficiaries, up to the insurance limit. A trust beneficiary can be an individual (regardless of the relationship to the owner), a charity or another non-profit organization (as defined by the IRS). Revocable trust

coverage is based on all revocable trust deposits held by the same owner at the same insured bank, whether formal or informal. If a revocable trust account has more than one owner, each owner's coverage is calculated separately, using the following rules:

Revocable Trust Deposits with Five or Fewer Beneficiaries - Each owner's share of revocable trust deposits is insured up to $250,000 for each beneficiary (i.e., $250,000 times the number of different beneficiaries), regardless of the actual interests of the beneficiaries.
Revocable Trust Deposits with Six or More Beneficiaries - Each owner's share of revocable trust deposits is insured for the greater of either (1) the coverage based on each beneficiary's actual interest in the revocable trust deposits, with no beneficiary's interest to be insured for more than $250,000, or (2) $1,250,000.

Example - POD Accounts with One Owner			
Account Title	Account Balance	Amount Insured	Amount Uninsured
John Smith POD to son	$250,000	$250,000	$0

Explanation: This revocable trust account is insured up to $250,000 since there is one beneficiary who will receive the deposit when the owner dies.

Revocable trust account needing more than $250,000 in insurance coverage
If a revocable trust account has more than one owner (e.g., husband and wife) or is held for more than one beneficiary, the insured balance of the account can exceed $250,000 and still be fully insured. If there is more than one owner, the FDIC will assume that the owners' shares are equal unless the deposit account records state otherwise.

Example - POD Accounts with Multiple Owners and Beneficiaries			
Account Title	Account Balance	Amount Insured	Amount Uninsured
Husband and Wife POD 3 children	$1,500,000	$1,500,000	$0
Husband POD wife	$250,000	$250,000	$0
Wife POD husband	$250,000	$250,000	$0
Husband POD niece and nephew	$500,000	$500,000	$0
Husband and wife POD grandchild	$600,000	$500,000	$100,000
Total	$3,100,000	$3,000,000	$100,000

Explanation: All but one account is fully insured. The account naming the one grandchild is insured to $500,000 because each owner is entitled to $250,000 insurance coverage for the sole beneficiary.

Living Trust Example: A husband and wife have a living trust leaving all trust assets equally to their three children upon the death of the last owner. All deposits held in the name of this trust at one FDIC-insured bank would be covered up to $1,500,000. Each owner is entitled to $750,000 of insurance coverage because they each have three beneficiaries who will receive the trust deposits when both owners have died.

What is the deposit insurance coverage of a revocable trust deposit when the beneficiaries do not have equal interests?
If a revocable trust has five or fewer beneficiaries, then each owner's share of all trust deposits at one insured bank is covered up to $250,000 times the number of beneficiaries, regardless of the actual proportional interests set forth in the trust document. For example:
An individual has $750,000 in revocable trust deposits at one FDIC-insured bank. The trust document specifies that 60% goes to one child, 30% goes to a second child, and 10% to a third child. The full balance of the trust is insured,

because the owner receives coverage of $250,000 per beneficiary, regardless of the actual interests set forth in the trust document.

If a revocable trust has six or more beneficiaries, then each owner's share of revocable trust deposits is insured for the greater of either (1) the coverage based on each beneficiary's actual interest in the revocable trust deposits, with no beneficiary's interest to be insured for more than $250,000, or (2) $1,250,000. For example:
An individual has $1,400,000 in revocable trust deposits at one FDIC-insured bank. The trust document specifies that 50% of the funds will belong to the owner's son and 10% will belong to each of his five grandchildren. Coverage for this depositor's revocable trust funds is determined using the rule for a revocable trust account with six or more beneficiaries. Maximum coverage for this depositor's funds is the greater of (1) the coverage based on each beneficiary's actual interest in the revocable trust deposits, with no beneficiary's interest exceeding $250,000, or (2) $1,250,000. Applying this rule, the maximum coverage based on actual interests is $500,000 ($250,000 divided by 50% (the son's share) = $500,000). Since this is less than $1,250,000, the trust owner's deposits would be insured up to $1,250,000, and $150,000 would be uninsured.
An individual has $2.5 million in revocable trust deposits at one FDIC-insured bank. The trust document specifies that 10% of the funds will belong to each of her five children and 5% will belong to each of her 10 grandchildren. Maximum coverage for this depositor's funds is the greater of (1) the coverage based on each beneficiary's actual interest in the revocable trust deposits, with no beneficiary's interest to be insured for more than $250,000, or (2) $1,250,000. Applying this rule, the maximum coverage based on actual interests is $2.5 million ($250,000 divided by 10% (each child's share) = $2,500,000). Since this amount is greater than $1,250,000, the trust owner would be fully insured.

How a beneficiary's life estate interest is insured for a formal living (or family) trust
Living trusts often give a beneficiary the right to receive income from the trust or to use trust assets during the beneficiary's lifetime (known as a life estate interest). When the beneficiary with the life estate interests dies, the remaining assets pass to other beneficiaries. A life estate interest is insured up to $250,000, separate from the interests of the other remaining beneficiaries. For example:
A husband creates a living trust giving his wife a life estate interest in the trust assets, with the remaining assets to belong equally to the couple's two children upon both parent's death. Deposits held in the name of this trust would be insured up to $750,000 ($250,000 for each beneficiary - the wife and two children).

Living trust accounts and POD accounts- separately insured

The $250,000 per beneficiary insurance limit applies to all revocable trust accounts - POD and living trust accounts - that an owner has at the same insured bank. For example:
A father has a POD account with a balance of $400,000 naming his son and daughter as beneficiaries. He also has a living trust account with a balance of $200,000 naming the same beneficiaries. The funds in both accounts would be added together and $300,000 would be attributable as the beneficial interest of each child. Therefore, the two accounts together would be insured for $500,000 ($250,000 per beneficiary) and uninsured for $100,000.

Irrevocable Trust Accounts

Irrevocable trust accounts are deposit accounts held by a trust established by statute or a written trust agreement, in which the creator of the trust (grantor/settlor/trustor) contributes funds or property and gives up all power to cancel or change the trust.

There are two types of irrevocable trusts -
Those created following of the death of an owner of a revocable trust. The insurance coverage of these irrevocable trusts is the same as for revocable trusts, which is described above.
Those that are created as an irrevocable (usually by a court order or established under a will) and are *not* derived from a revocable trust. The insurance coverage of these irrevocable trusts is described below.
How funds deposited pursuant to an irrevocable trust document are insured
The interests of a beneficiary in all deposit accounts established by the same settlor and held at the same insured bank under an irrevocable trust are added together and insured up to $250,000, provided all of the following requirements are met:
The insured bank's deposit account records must disclose the existence of the trust relationship
The beneficiaries and their interests in the trust must be identifiable from the deposit account records of the bank or from the records of the trustee
The amount of each beneficiary's interest must not be "contingent" as that term is defined by FDIC regulations
The trust must be valid under state law

Since the amount of insurance for an irrevocable trust depends upon specific terms and conditions of the trust, owners or trustees of an irrevocable trust may wish to consult with their legal or financial advisor for assistance in determining the amount of insurance coverage available to trust deposits.

What is the insurance coverage if the grantor retains an interest in the trust?

If the grantor retains an interest in the trust, the amount of the retained interest would be added to any single accounts owned by the grantor at the same bank and the total insured up to $250,000.

What if the beneficiaries or their interests in an irrevocable trust cannot be ascertained?

When the ownership interests of the beneficiaries cannot be determined, insurance coverage for the entire trust is generally limited to a maximum of $250,000.

POD Account Example: *This example applies to POD accounts only. (Coverage may be different for some living trusts.)* Bill has a $250,000 POD account with his wife Sue as beneficiary. Sue has a $250,000 POD account with Bill as beneficiary. In addition, Bill and Sue jointly have a $1,500,000 POD account with their three children as equal beneficiaries.

Account Title	Account Balance	Amount Insured	Amount Uninsured
Bill POD to Sue	$250,000	$250,000	$0
Sue POD to Bill	$250,000	$250,000	$0
Bill and Sue POD to 3 children	$1,500,000	$1,500,000	$0
Total	$2,000,000	$2,000,000	$0

These three accounts totaling $2,000,000 are fully insured because each owner is entitled to $250,000 of coverage for each beneficiary. Bill has $1,000,000 of insurance coverage because he names four beneficiaries - his wife in the first account and his three children in the third account). Sue also has $1,000,000 of insurance coverage $250,000 for each of her beneficiaries - her husband in the second account and her three children in the third account.

When calculating coverage for revocable trust accounts, *keep in mind that:*

Coverage is based on the number of beneficiaries (and, if the account has six or more beneficiaries, the interests of the beneficiaries) named by each owner. Additional coverage is not provided for the trust owner(s). For example, if a father owns a $750,000 POD account naming his two sons as beneficiaries, the account is insured for $500,000 - $250,000 for the interest of each beneficiary. The remaining $250,000 is uninsured.

FDIC insurance limits apply to all revocable trust deposits - including all POD/ITF and living trust accounts - that a trust owner has at one insured bank. In applying the $250,000 per beneficiary insurance limit, the FDIC combines an owner's POD accounts with the living trust accounts that name the same beneficiaries at the same bank.

The Uniform Transfer to Minor Act

The Uniform Transfer to Minor Act is a state law that allows an adult to make a gift to a minor. Funds given to a minor by this method are held in the name of a custodian for the minor's benefit. Funds deposited for the minor's benefit under the Act are added to any other single accounts of the minor, and the total is insured up to a maximum of $250,000.

Sole Proprietorship accounts

These are deposits owned by an unincorporated business, in contrast to a business that is incorporated or a partnership. Deposit accounts owned by a sole proprietor are insured as the single funds of the person who owns the business. So, if an individual has an account in his name alone and another account in the name of his sole proprietorship, the balances in those accounts would be combined and insured to a up to a maximum of $250,000 in the single account category.

Decedent Estate accounts

These are funds deposited by an executor or administrator for the estate of a deceased person. These accounts are insured up to $250,000 as the single account funds of the deceased person. This coverage limit would include any other funds maintained in the name of the deceased individual. It is important to note that coverage is not

provided on a per beneficiary basis. So, even though there might be multiple beneficiaries of the decedent's estate, the account established for the estate would not be insured for more than $250,000. The funds are, however, insured separately from the personal funds of the executor or administrator.

Certain Retirement Accounts

These are deposit accounts owned by one person and titled in the name of that person's:
Individual Retirement Account including traditional IRA, Roth IRA, Simplified Employee Pension (SEP) IRA or Savings Incentive Match Plans for Employees (SIMPLE) IRA
Section 457 deferred compensation plan account (such as eligible deferred compensation plans provided by state and local governments regardless of whether the plan is self-directed)
Self-directed defined contribution plan account, such as a self-directed 401(k) plan, a self-directed SIMPLE plan held in the form of a 401(k) plan, a self-directed defined contribution money purchase plan, or a self-directed defined contribution profit-sharing plan
Self-directed Keogh plan account (or H.R. 10 plan account) designed for self-employed individuals

Definition of 'Self-Directed'- The FDIC defines the term "self-directed" to mean that plan participants have the right to direct how the money is invested, including the ability to direct that the deposits be placed at an FDIC-insured bank.

If a participant of a retirement plan has the right to choose a particular depository institution's deposit accounts as an investment, the FDIC would consider the account to be self-directed. Also, if a plan has as its default investment option deposit accounts at a particular FDIC-insured institution, the FDIC would deem the plan to be self-directed for deposit insurance purposes because, by inaction, the participant has directed the placement of such deposits.

However, if a plan's only investment vehicle is the deposit accounts of a particular bank, so that participants have no choice of investments, the plan would not be deemed self-directed for deposit insurance purposes. Finally, if a plan consists only of a single employer/employee, and the employer establishes the plan with a single-investment option of plan assets, the plan would be considered self-directed for deposit insurance purposes.

Roth IRAs

A Roth IRA is treated the same as a traditional IRA for deposit insurance purposes. So, if a depositor has both a Roth IRA and a traditional IRA at the same insured bank, the funds in both accounts are added together and insured up to $250,000.

Example of Insurance Coverage for Self-Directed Retirement Accounts	
Account Title	Account Balance
Bob Johnson's Roth IRA	$110,000
Bob Johnson's IRA	$75,000
Total	$185,000
Amount Insured	$185,000

Explanation: Since Bob's total in all self-directed retirement accounts at the same bank is less than the $250,000 limit, both IRAs are fully insured.

Coverdell IRAs or Health Savings Accounts

Coverdell Education Savings Accounts (formerly known as an Education IRAs), Health Savings Accounts and Medical Savings Accounts are **not** included in the certain retirement ownership category. Depending on the structure, these accounts may be included in the single account or trust account ownership category. Also, accounts established under section 403(b) of the Internal Revenue Code (annuity contracts for certain employees of public schools, tax-exempt organizations and ministers) are **not** included in the certain retirement ownership category.

Revocable Trust Accounts

A revocable trust account is a deposit account that indicates an intention that the funds will belong to one or more beneficiaries upon the death of the owner (grantor/settlor/trustor). There are both informal and formal revocable trusts:
Informal revocable trusts - often called payable on death (POD), Totten trust, or in trust for (ITF) accounts - are created when the account owner signs an agreement, usually part of the bank's signature card, stating that the funds are payable to one or more beneficiaries upon the owner's death.
Formal revocable trusts - known as living or family trusts - are written trusts created for estate planning purposes. The owner (also known as a grantor, settlor or trustor) controls the funds in the trust during his or her lifetime and reserves the right to revoke the trust.

Employee Benefit Plan Accounts
The general rule is that deposits belonging to pension plans and profit-sharing plans receive pass-through insurance, meaning that each participant's non-contingent and ascertainable interest in a deposit-as opposed to the deposit as a whole-is insured up to $250,000. In order for a pension or profit-sharing plan to receive pass-through insurance, the institution's deposit account records must specifically disclose the fact that the funds are owned by an employee benefit plan. In addition, the details of the participants' beneficial interests in the account must be ascertainable from the institution's deposit account records or from the records that the plan administrator (or some other person or entity that has agreed to maintain records for the plan) maintains in good faith and in the regular course of business.

Employee benefit plan coverage and the number of plan participants
Employee benefits are various non-wage compensations provided to employees in addition to their cash wages. Normally, employer provided benefits are tax-deductible to the employer and non-taxable to the employee. Coverage for an employee benefit plan's deposits is based on each participant's share of the plan. Because plan participants normally have different interests in the plan, insurance coverage cannot be determined by simply multiplying the number of participants by $250,000. To determine the maximum amount a plan can have on deposit in a single bank and remain fully insured, first determine which participant has the largest share of the plan assets, then divide $250,000 by that percentage. For example, if a plan has 20 participants, but one participant has an 80% share of the plan assets, the most the plan can have on deposit in a single bank and still remain fully insured is $312,500. ($250,000/.80 = $312,500)

Example - Employee Benefit Plan that Qualifies for Pass-Through Coverage				
Account Title				Balance
Happy Pet Clinic Benefit Plan				$700,000
Plan Participants	Plan Share	Share of Deposit	Amount Insured	Amount Uninsured
Dr. Todd	35%	$245,000	$245,000	$0
Dr. Jones	30%	$210,000	$210,000	$0
Tech Evans	20%	$140,000	$140,000	$0
Tech Barnes	15%	$105,000	$105,000	$0
Plan Total	100%	$700,000	$700,000	$0

Explanation: This employee benefit plan can deposit $700,000 in an FDIC-insured bank and have all of its participants fully insured. The $700,000 deposit results in Dr. Todd's interest (the largest participant) being insured for $245,000 (35% of $700,000). When Dr. Todd's interest is fully insured, the interests of the other participants are also fully insured, since they have smaller shares of the plan.

Corporation, Partnership, and Unincorporated Association Accounts
These are accounts established by businesses and organizations - including for-profit and not-for-profit organizations - engaged in an independent activity, meaning that the entity is operated primarily for some purpose other than to increase insurance coverage.
Unincorporated associations typically include religious, community and civic organizations and social clubs that are not incorporated.

Deposit insurance coverage for funds deposited by a corporation, partnership, or unincorporated association
Funds deposited by a corporation, partnership, or unincorporated association are insured up to a maximum of $250,000. Funds deposited by a corporation, partnership, or unincorporated association are insured separately from the personal accounts of the stockholders, partners or members. To qualify for this coverage, the entity must be engaged in an independent activity, meaning that the entity is operated primarily for some purpose other than to increase deposit insurance.

Additional insurance coverage
There is no way that a corporation, partnership or unincorporated association can qualify for more than $250,000 in insurance coverage for its deposits at one bank. Separate accounts owned by the same entity, but designated for different purposes, are not separately insured. Instead, such accounts are added together and insured up to $250,000. If a corporation has divisions or units that are not separately incorporated, the deposit accounts of those divisions or units will be added to any other deposit accounts of the corporation for purposes of determining deposit insurance coverage.

Total of partners, members or account signatories
The number of partners, members or account signatories that a corporation, partnership, or unincorporated association has does not affect coverage. For example, deposits owned by a homeowners association are insured up to $250,000 in total, not $250,000 for each member of the association.

Sole-proprietorships not insured
Deposits owned by a business that is a sole proprietorship are not insured under this category. Rather, they are insured as the single account deposits of the person who is the sole proprietor. So, funds deposited in the sole proprietorship's name are added to any other single accounts of the sole proprietor and the total is insured to a maximum of $250,000.

Government Accounts
Government accounts are also known as public unit accounts. This category includes deposit accounts of the United States, any state, county, municipality (or a political subdivision of any state, county, or municipality), the District of Columbia, Puerto Rico and other government possessions and territories, or an Indian tribe

How public unit accounts are insured
Insurance coverage of a public unit account differs from a corporation, partnership, or unincorporated association account in that the coverage extends to the official custodian of the funds belonging to the public unit rather than the public unit itself. The insurance coverage of public unit accounts depends upon (1) the type of deposit, and (2) the location of the insured depository institution. All time and savings deposits owned by a public unit and held by the same official custodian in an insured depository institution within the State in which the public unit is located are added together and insured up to $250,000. Separately, all demand deposits owned by a public unit and held by the same official custodian in an insured depository institution within the State in which the public unit is located are added together and insured up to $250,000. For the purpose of these rules, the term "savings deposits" includes NOW accounts, money market deposit accounts and other interest-bearing checking accounts.

Maintaining funds in an out of state bank
The insurance coverage of public unit accounts is different if the depository institution is located outside the State in which the public unit is located. In that case, all deposits owned by the public unit and held by the same official custodian are added together and insured up to $250,000. Time and savings deposits are not insured separately from demand deposits.

The definition of a political subdivision- The term "political subdivision" is defined to include drainage, irrigation, navigation, improvement, levee, sanitary, school or power districts, and bridge or port authorities and other special districts created by state statute or compacts between the states. The term "political subdivision" also includes any subdivision or principal department of a public unit (state, county, or municipality) if the subdivision or department meets the following tests:
The creation of the subdivision or department has been expressly authorized by the law of such public unit;
Some functions of government have been delegated to the subdivision or department by such law; and
The subdivision or department is empowered to exercise exclusive control over funds for its exclusive use.

Definition of an official custodian- An "official custodian" is an officer, employee or agent of a public unit having official custody of public funds and lawfully depositing the funds in an insured institution. In order to qualify as an official custodian, a person must have plenary authority - including control - over the funds. Control of public funds

includes possession as well as the authority to establish accounts in insured depository institutions and to make deposits, withdrawals and disbursements.

What Is Not Insured

Increasingly, institutions are also offering consumers a broad array of investment products that are not deposits, such as mutual funds, annuities, life insurance policies, stocks and bonds. Unlike the traditional checking or savings account, however, these non-deposit investment products are not insured by the FDIC.

Mutual Funds

Investors sometimes favor mutual funds over other investments, perhaps because they hold promise of a higher rate of return than say, CDs. And with a mutual fund, such as a stock fund, the risk of a company going bankrupt, resulting in the loss of investors' funds - is more spread out because the investor owns a piece of a lot of companies instead of a portion of a single enterprise. A mutual fund manager may invest the fund's money in either a variety of industries or several companies in the same industry. Or the funds may be invested in a money market mutual fund, which may invest in short-term CDs or securities such as Treasury bills and government or corporate bonds. Do not confuse a money market mutual fund with an FDIC-insured money market deposit account (described earlier), which earns interest in an amount determined by, and paid by, the financial institution where the funds are deposited. Potential investors can - and should - obtain definitive information about any mutual fund before investing in it by reading a prospectus, which is available at the bank or brokerage where he or she plans to do business. The key point to remember when contemplating purchasing mutual funds, stocks, bonds or other investment products, whether at a bank or elsewhere, is: Funds so invested are NOT deposits, and therefore are NOT insured by the FDIC - or any other agency of the federal government.

Securities owned by an investor, including mutual funds, that are held for his or her account by a broker, or a bank's brokerage subsidiary are not insured against loss in value. The value of investments can go up or down depending on the demand for them in the market. The Securities Investors Protection Corporation (SIPC), a non government entity, replaces missing stocks and other securities in customer accounts held by its members up to $500,000, including up to $100,000 in cash, if a member brokerage or bank brokerage subsidiary fails. For more information contact:

Treasury Securities

Treasury securities include Treasury bills (T-bills), notes and bonds. T-bills are commonly purchased through a financial institution. Customers who purchase T-bills at banks that later fail become concerned because they think their actual Treasury securities were kept at the failed bank. In fact, in most cases banks purchase T-bills via book entry, meaning that there is an accounting entry maintained electronically on the records of the Treasury Department; no engraved certificates are issued. Treasury securities belong to the customer; the bank is merely acting as custodian. Customers who hold Treasury securities purchased through a bank that later fails can request a document from the acquiring bank (or from the FDIC if there is no acquirer) showing proof of ownership and redeem the security at the nearest Federal Reserve Bank. Or, customers can wait for the security to reach its maturity date and receive a check from the acquiring institution, which may automatically become the new custodian of the failed bank's T-bill customer list (or from the FDIC acting as receiver for the failed bank when there is no acquirer). Even though Treasury securities are not covered by federal deposit insurance, payments of interest and principal (including redemption proceeds) on those securities that are deposited to an investor's deposit account at an insured depository institution ARE covered by FDIC insurance up to the $250,000 limit. And even though there is no federal insurance on Treasury securities, they are backed by the full faith and credit of the United States Government - the strongest guarantee anyone can get.

Safe Deposit Boxes

The contents of a safe deposit box are not insured by the FDIC. (Depositors should make sure to read the contract with the bank when renting the safe deposit box in the event that some type of insurance is provided; some banks may make a very limited payment if the box or contents are damaged or destroyed, depending on the circumstances.) If a person is concerned about the safety, or replacement, of items placed in a safe deposit box, he or she may wish to consider purchasing fire and theft insurance. Separate insurance for these perils may be available through the boxholder's insurance agent. Usually such insurance is part of a homeowner's or tenant's insurance policy for a residence and its contents.

In the event of a bank failure, in most cases an acquiring institution would take over the failed bank's offices, including locations with safe deposit boxes. If no acquirer can be found the FDIC would send boxholders instructions for removing the contents of their boxes.

Robberies and Other Thefts

Stolen funds may be covered by what's called a banker's blanket bond, which is a multi-purpose insurance policy a bank purchases to protect itself from fire, flood, earthquake, robbery, defalcation, embezzlement and other causes of disappearing funds. In any event, an occurrence such as a fire or bank robbery may result in a loss to the bank but should not result in a loss to the bank's customers.

If a third party somehow gains access to an account and transacts business that the account holder would not approve of, he or she must contact the bank and local law enforcement authorities, who have jurisdiction over this type of wrongdoing.

Coverage Summary	
FDIC-Insured Checking Accounts (including money market deposit accounts) Savings Accounts (including passbook accounts) Certificates of Deposit	Not FDIC-Insured Investments in mutual funds (stock, bond or money market mutual funds), whether purchased from a bank, brokerage or dealer Annuities (underwritten by insurance companies, but sold at some banks) Stocks, bonds, Treasury securities or other investment products, whether purchased through a bank or a broker/dealer

CHAPTER 2 The FDIC, How it Came to Be

The **Federal Deposit Insurance Corporation** (**FDIC**) was created by the Glass-Stegall Act of 1933. It is a government sponsored entity that provides deposit insurance guaranteeing the safety of checking and savings deposits in member banks. The coverage limit has changed over the years. In the fall of 2008, the limit was raised to $250,000 per depositor per bank. The FDIC insures deposits according to the ownership category in which the funds are insured and how the accounts are titled. The standard deposit insurance coverage limit is $250,000 per depositor, per FDIC-insured bank, per ownership category. The vast number of bank failures in the Great Depression lead to the creation of an institution to guarantee deposits held by commercial banks.

The FDIC insures accounts at different banks separately. For example, a person with accounts at two separate banks (not merely branches of the same bank) can keep $250,000 in each account and be insured for the total of $500,000. Also, accounts in different ownerships (such as beneficial ownership, trusts, and joint accounts) are considered separately for the $250,000 insurance limit. Under the Federal Deposit Reform Act of 2005, Individual Retirement Accounts are insured to $250,000.

History of Deposit Insurance, Introduction

"After all, there is an element in the readjustment of our financial system more important than currency, more important than gold, and that is the confidence of the people."

These words were spoken by President Franklin D. Roosevelt in his first "fireside chat" to the people of the United States on March 12, 1933. In announcing an end to the bank holiday he had proclaimed six days earlier, President Roosevelt was exhorting the people to remain calm and avoid the panicked withdrawals that had crippled the nation's banking system in the first months of 1933. However, despite the federal government's newly adopted plans to reorganize many closed but viable banks, some 4,000 banks that had closed earlier in 1933 or during the bank holiday never reopened.

The confidence of the people still was shaken, and public opinion remained squarely behind the adoption of a federal plan to protect bank depositors. Opposition to such a plan had been voiced earlier by President Roosevelt, the Secretary of the Treasury and the Chairman of the Senate Banking Committee. They believed a system of deposit insurance would be unduly expensive and would unfairly subsidize poorly managed banks. Nonetheless, public opinion held sway with the Congress, and the Federal Deposit Insurance Corporation was created three months later when the President signed into law the Banking Act of 1933. The final frenetic months of 1933 were spent organizing and staffing the FDIC and examining the nearly 8,000 state-chartered banks that were not members of the Federal Reserve System. Federal deposit insurance became effective on January 1, 1934, providing depositors with $2,500 in coverage, and by any measure it was an immediate success in restoring public confidence and stability to the banking system. Only nine banks failed in 1934, compared to more than 9,000 in the preceding four years.

Millennium

At the new Millennium, federal deposit insurance remains an integral part of the nation's financial system, although some have argued at different points in time that there have been too few bank failures because of deposit insurance, that it undermines market discipline, that the current coverage limit of $100,000 is too high, and that it amounts to a federal subsidy for banking companies. Each of these concerns may be valid to some extent, yet the public appears to remain convinced that a deposit insurance program is worth the cost, which ultimately is borne by them. The severity of the 1930s banking crisis has not been repeated, but bank deposit insurance was harshly tested in the late 1980s and early 1990s. The system emerged battered but sound and, with some legislative tweaking, better suited to the more volatile, higher-risk financial environment that has evolved in the last quarter of the 20th century.

This chapter focuses on the insurance function of the FDIC. The agency also serves as the primary federal supervisor for state-chartered nonmember banks and has backup supervisory authority over all other insured depository institutions; and the FDIC manages the receiverships of failed insured banks and thrifts. These supervisory and receivership-management functions are not fully addressed here. The document also does not directly address the savings-and-loan crisis of the 1980s. The FDIC only began insuring the deposits of savings associations in 1989, as a result of the legislation that resolved the S&L crisis.

Antecedents of Federal Deposit Insurance

During the years immediately following the organization of the federal government in 1789, banks were chartered by special acts of state legislatures or the Congress, usually for a limited number of years. Initially, bank failures were nonexistent. It was not until 1809, with the failure of the Farmers Bank of Gloucester, Rhode Island, that people realized that such an event was even possible (Carter H. Golembe, "Origins of Deposit Insurance in the Middle West, 1834-1866," *The Indiana Magazine of History*, Vol. LI, June, 1955, No. 2, p. 113). Any notion that this failure represented an isolated incident was dispelled after the first wave of bank failures occurred five years later.

Insurance of Bank Obligations, 1829 - 1866

The ensuing economic disruptions caused by these and subsequent bank failures fueled demands for banking reform. In 1829, New York became the first state to adopt a bank-obligation insurance program. The term "bank obligation" refers to both circulating notes and deposits.

New York's program was devised by Joshua Forman, a Syracuse businessman. The insurance concept embodied in his plan was suggested by the regulations of the Hong merchants in Canton (*Assembly Journal*, New York State, 1829, p. 179).

The regulations required merchants who held special charters to trade with foreigners to be liable for one another's debts. Writing in 1829, when bank-supplied circulating medium was largely in the form of bank notes rather than deposits, Forman noted:
The case of our banks is very similar; they enjoy in common the exclusive right of making a paper currency for the people of the state, and by the same rule should in common be answerable for that paper.

The plan conceived by Forman had three principal components:

- the establishment of an insurance fund, to which all banks had to pay an assessment;
- a board of commissioners, which was granted bank examination powers;
- a specified list of investments for bank capital.

The first two provisions were adopted virtually intact; the proposal pertaining to the investment of bank capital initially was rejected. Upon reconsideration during the 1830s, the bank capital proposal was modified and subsequently enacted. From 1831 to 1858, five additional states adopted insurance programs: Vermont, Indiana, Michigan, Ohio, and Iowa. The purposes of the various plans were similar:
to protect communities from severe fluctuations of the circulating medium caused by bank failures
to protect individual depositors and noteholders against losses

Available evidence indicates that the first of these, concern with the restoration of the circulating medium *per se*, predominated (Carter H. Golembe, "The Deposit Insurance Legislation of 1933: An Examination of Its Antecedents and Its Purposes," *Political Science Quarterly*, Vol. LXXV, No. 2, June, 1960, p.189).

Nature of plans

In striving to meet these insurance goals, the states employed one of three approaches. Following New York's lead, Vermont and Michigan established insurance funds. Indiana did not; instead, all participating banks were required mutually to guarantee the liabilities of a failed bank. The insurance programs adopted by Ohio and Iowa incorporated both approaches. Although participating banks were bound together by a mutual guaranty provision, an insurance fund was available to reimburse the banks in the event special assessments were necessary immediately to pay creditors of failed banks. The insurance fund was replenished from liquidation proceeds. Table 1 summarizes the principal provisions of the six programs which operated between 1829-1866.

Coverage

In the first four programs adopted, insurance coverage primarily extended to circulating notes and deposits. New York later restricted coverage to circulating notes. In the case of Ohio and Iowa, insurance coverage from the outset only extended to circulating notes. None of the six programs placed a dollar limit on the amount of insurance provided an individual bank creditor. The extension of insurance coverage to bank notes in all of the six programs reflected their importance as a circulating medium. Because it was common practice for banks to extend credit by using bank notes, nearly one-half of the circulating medium before 1860 was in this form. In those states that limited insurance coverage to bank notes, the belief was that banks affected the circulating medium only through their issuance. Additionally, it was believed that depositors could select their banks, whereas noteholders had

considerably less discretion and thus were in greater need of protection (Federal Deposit Insurance Corporation, *Annual Report*, 1952 (1953), p. 61).

Methods used to protect creditors of banks in financial difficulty

Ad hoc measures frequently were taken in some of the six states to protect creditors of banks in financial difficulty. Faced with the possible insolvency of several banks in 1837, New York State's Comptroller began redeeming their notes from the insurance fund. This action prevented the banks from failing and they eventually were able to reimburse the insurance fund. In 1842, New York faced a more serious crisis after the failure of eleven participating banks within a three-year period threatened the solvency of the insurance fund.

Table 1 Principal Provisions of Bank-Obligation Insurance Programs in Operation 1829 - 1866

State	Period of Operation	Obligations Insured	Banks Participating	Assessments; Size of Fund	Payment of Bank Creditors
New York	1829 - 1866	1829-42, all debts[2] 1842-66, circulating notes [3]	All banks established or rechartered subsequent to passage of act[4]	Annually ½ of 1% of capital stock to maximum of 3%. If fund reduced, annual assessment not to exceed above rate until fund restored to maximum.	After completion of liquidation of failed bank.
Vermont	1831 - 1866	All debts[2]	All banks established or rechartered subsequent to passage of act[5]	Annually ¾ of 1% of capital stock to maximum of 4 ½%. If fund reduced, annual assessments not to exceed above rate until fund restored to maximum.	After completion of liquidation of failed bank.
Indiana	1834 - 1866	All debts[2]	Branch banks[6]	No specific amount; special assessments as necessary.	Within one year after failure, if liquidation proceeds and stockholder contributions are insufficient
Michigan	1836 - 1842	All debts[2]	All banks established or rechartered subsequent to passage of act	Annually ½ of 1% of capital stock to maximum of 3%. If fund reduced, annual assessment not to exceed above rate until fund restored to maximum.	After completion of liquidation of failed bank.
Ohio	1845 - 1866	Circulating notes	Branch banks	Single assessment prior to opening of bank: 10% of amount of circulating notes. Thereafter, assessments at above rate	Immediately, through special assessments on solvent branch banks. Assessments to be repaid from insurance fund, and fund repaid

				applicable only to circulating notes, if any, issued by bank.	from proceeds of liquidation of assets of failed bank.
Iowa	1858 - 1865	Circulating notes	Branch banks	Single assessment before opening of bank: 10% of amount of circulating notes. Thereafter, assessments at above rate applicable only to circulating notes, if any, issued by bank.	Immediately, through special assessments on solvent branch banks. Assessments to be repaid from insurance fund, and fund repaid from proceeds of liquidation of assets of failed bank.

Notes:
1 In a number of cases, the law was repealed subsequent to the terminal date shown above. In some of the states, closing dates may have preceded the date shown
by one year.
2 Included circulating notes, deposits and miscellaneous liabilities; excluded capital accounts.
3 Act of April 12, 1842.
4 Free banks, which were authorized in 1838, did not participate in insurance.
5 Free banks, which were authorized in 1851, did not participate in insurance. In 1842, participating banks were authorized under specified conditions to
withdraw from insurance.
6 Branch banks were essentially independent banks that had their own officers, distributed earnings to their own stockholders and collectively constituted the
"State Bank" in these states.
Source: Federal Deposit Insurance Corporation*, Annual Report*, 1952 (1953), pp. 62-63.

The legislature authorized the State Comptroller to sell bonds sufficient to meet all claims against the insurance fund. The bonds later were redeemed from subsequent payments into the fund by participating banks. Other states similarly grappled with the question of whether to assist or close a distressed bank. On several occasions, authorities in Ohio kept a number of distressed banks from closing by levying special assessments upon healthy participating banks. Indiana and Iowa also granted financial assistance to distressed banks.

Method of paying creditors of failed banks

Only the programs of Ohio and Iowa provided for immediate payment of insured obligations. Necessary funds were made available in those two states through special assessments levied on the sound participating banks. Creditors in New York, Vermont and Michigan were not paid until the liquidation of a failed bank had been completed. Indiana's program provided that creditors were to be paid within one year after a bank failed if liquidation proceeds and stockholder contributions were insufficient to cover realized losses.

Role of bank supervision

Bank supervision was an essential element of the insurance programs that operated prior to 1866. The function of supervision was essentially twofold:
1.) To reduce the potential risk exposure of the various insurance programs.
2.) To provide some measure of assurance to well-managed banks that the unsound banking practices of badly managed banks would not go completely unchecked
(Carter H. Golembe and Clark Warburton, *Insurance of Bank Obligations in Six States* (Washington, D.C.: Federal Deposit Insurance Corporation, 1958), pp. I-9).

Table 2 summarizes the principal provisions relating to bank supervision in the six insurance states. Better supervision of banks was achieved by the programs with mutual guaranty than by the simple insurance fund programs (Federal Deposit Insurance Corporation, *Annual Report*, 1953 (1954), p. 59).

Under the mutual guaranty programs in Indiana, Ohio and Iowa, supervisory officials were largely selected by, and accountable to, the participating banks. The officials were given wide latitude to check unsound banking practices because the participating banks were keenly aware that the cost of lax supervision ultimately would be borne by them. During the Indiana program's 30 years of operation, not one state-chartered bank failed. Indiana's success principally was attributable to the quality of bank supervision. A strong supervisory board was the cornerstone of the program. The board, which included four members appointed by the Indiana General Assembly and one representative from each of the participating banks, could close any member bank.

Table 2 Principal Provisions Relating to Supervision of Banks Participating in Bank-Obligation Insurance Programs, Six States, 1829 - 1866

State	Supervisory Agency	Bank Examination	Condition Reports	Supervisory Enforcement Powers
New York	1829-37: Three Bank Commissioners; one appointed by Governor, two by banks. 1837-43: Three Bank Commissioners appointed by Governor. 1843-51: State Comptroller. 1851-55: Banking Department; Superintendent appointed by Governor.	1829-43: Each bank three times per year; additional examinations if requested by three participating banks. 1843-66: Examination only when bank was believed to be insolvent or to have submitted false condition report.	1829-43: Annually to Bank Commissioners. 1843-66: Quarterly to Comptroller or Superintendent of Banking Department. Content expanded.	If bank insolvent or had violated law, could apply to court of chancery for injunction against continued operation.
Vermont	1831-37: Three Bank Commissioners; one appointed by legislature, two by banks. 1837-58: One Bank Commissioner appointed by legislature.	Each bank once per year; additional examinations if requested by a stockholder or bank debtor.	Annually to Bank Commissioners.	If bank insolvent or had violated law, could apply to court of chancery for injunction against continued operation.
Indiana	1834-55: Board of Directors of the State Bank of Indiana; President and four directors appointed by legislature and one director by each Branch Bank. 1856-65: Board of Directors of the Bank of the State of Indiana; four	Each bank twice per year; additional examinations if requested by directors of a bank.	Monthly to Board	If bank insolvent, had violated law or was mismanaging its affairs, could close bank. Could regulate dividend payments.[1] Could establish ratio, between specified limits, of loans and discounts to capital for any or all banks. Loans of deposited funds exempted.

	directors appointed by legislature, one director by each Branch Bank and President by Board.			
Michigan	1836-37: One Bank Commissioner appointed by Governor. 1837-40: Three Bank Commissioners appointed by Governor. 1840-42: Attorney General.	1836-40: Each bank three times per year; additional examinations if requested by three participating banks. 1840-42: At Governor's request.	Annually to Bank Commissioners or Attorney General.	If bank insolvent or had violated law, could apply to court of chancery for injunction against continued operation.
Ohio	Board of Control of the State Bank of Ohio; one member appointed by each Branch Bank; President elected by Board from outside its membership.	Left to discretion of Board; policy was to examine each bank annually.	Quarterly to Board; policy to require monthly reports to Board.	If bank insolvent, had violated law or any order of Board, could close bank. Could order any bank to reduce its circulation or liabilities to whatever level was considered safe. Could determine proportion of reserve to be in vault cash.[1]
Iowa	Board of Directors of the State Bank of Iowa; three directors appointed by legislature; one director by each Branch Bank; President by Board.	Left to discretion of Board; policy was to examine each bank twice per year.	Monthly to Board	If bank insolvent, had violated law or any order of Board, could close bank. Could regulate dividend payments. Could order any bank to reduce its circulation or liabilities to whatever level was considered safe.
Notes: 1 Not stipulated in law but assumed by agency. *Source*: Carter H. Golembe and Clark Warburton, *Insurance of Bank Obligations in Six States* (Washington, DC: The Federal deposit Insurance Corporation, 1958), pp. 1-8, 1-9.				

The causes for closing a bank were:
insolvency;
mismanagement; and
refusal to comply with any legal directive of the board.

The board's power was absolute since there was no provision for appeal to the courts or to any other state agency. Supervisory authorities in Ohio and Iowa could issue cease-and-desist orders, as well as require banks to be closed. Ohio had four banks fail: one in 1852 because of defalcation and three in 1854 because of asset deterioration. While none failed in Iowa, it should be noted that Iowa's program operated during a period of more favorable economic conditions.

Assessments and the insurance funds

Insurance fund assessments were levied on capital stock or insured obligations. To provide a basis for comparison with later assessment rates under federal deposit insurance, previous researchers have computed the equivalent average annual rate on total obligations (*i.e*., deposits plus circulating notes) levied by the five states that had insurance funds (Table 3). On this basis, Michigan's annual rate of one-tenth of 1 percent most closely approximated the statutory rate of one-twelfth of 1 percent (before credits) in effect under federal deposit insurance from 1935 through 1989. Other rates were substantially higher, ranging from one-fifth of 1 percent in Vermont to almost 2 percent in Iowa. Three insurance programs had positive fund balances at the time of their closing (Table 3). The Vermont and Michigan insurance funds were deficient by $22,000 and $1.2 million, respectively. In both states the first failures occurred before the insurance funds were adequately capitalized. Michigan's program collapsed under the strain. Although Vermont's fund subsequently recovered, it had a negative balance at the time the program closed because of the payment of unauthorized refunds to banks previously withdrawing from the program.

Demise of the insurance programs

Two primary factors contributed to the eventual collapse of the state insurance systems. The first factor was the emergence of the "free banking" movement in the 1830s. This movement developed in response to the void created by the closing of the Second Bank of the United States in 1836. To fill this void, many states enacted laws designed to ease bank entry restrictions. The movement produced an alternative for insurance of bank notes, which permitted a bank to post bonds and mortgages with state officials in an amount equal to its outstanding bank notes. Banks taking advantage of this alternative were excluded from insurance. This exclusion did not apply in Michigan. As the number of "free banks" increased, participation in state insurance programs declined. Consequently, the original intent to include all banks in the individual state insurance programs was thwarted.

Creation of National Banking System

The second factor in the collapse of the state insurance systems was the establishment of the national bank system in 1863. In 1865, Congress levied prohibitive tax on state bank notes causing many state-chartered banks to convert to national charters in order to escape the tax. As conversions increased, membership in the state insurance systems declined, eventually to the point where these programs ceased to exist.

Mechanics- Circulating Bank Notes Guaranteed by the Federal Government

National bank notes were collateralized by United States bonds. More importantly, the primary guaranty for the notes was the credit of the federal government rather than the value of the posted collateral. Holders of notes of a failed national bank were to be paid immediately and in full by the U.S. Department of the Treasury regardless of the value of the bonds backing the notes. The Comptroller of the Currency stated in his first report to Congress.
If the banks fail, and the bonds of the government are depressed in the market, the notes of the national banks must still be redeemed in full at the treasury of the United States. The holder has not only the public securities, but the faith of the nation pledged for their redemption. (U.S., Comptroller of the Currency, *Annual Report*, November 28, 1863)

So long as national bank notes retained their relative importance in the circulating medium, bank-obligation insurance was considered unnecessary. However, bank deposits soon overtook and then eclipsed national bank notes in importance. By 1870, deposits were about twice, and by the end of the century seven times, circulating notes. It was against this backdrop that efforts were renewed to provide for deposit insurance. Various proposals to that effect were introduced at the federal and state levels. Although the first attempts were made in Congress as early as 1886, the states took the lead.

Table 3 Insurance Funds and Assessments for States with Bank-Obligation Insurance Programs, 1829 - 1866 ($ Thousands)

	New York 1829 - 1866	Vermont 1831 - 1866	Michigan 1836 - 1842	Ohio 1845 - 1866	Iowa 1858 - 1865
Average fund size	$192	$19	$0.3	$759	$196
Fund as a percent of -					
Total obligations	0.6%	2.0%	0.09%	7.7%	8.4%
Average insured obligations	1.0%	2.0%	0.09%	11.5%	21.4%
Balance or (deficiency) at close of program	$13	($22)	($1,198)	$815[2]	$338[2]
Assessments and income available for insurance operations:	$3,221	$63	$3	$1,567	$338
Assessments paid[3]	3,120	63	3	1,567	338
Interest received[4]	101	--	--	--	--
Used for insurance operations	3,208	44	--	722[5]	--
Refunded to banks or state[6]	13	19	--	845	338
Assessments necessary to cover insurance costs	$3,208	$68	$1,198	$722[5]	--
Equivalent average annual rate of assessment on total obligations	0.24%	0.2%	0.1%	0.8%	1.8%

Notes:
1 In Indiana the insurance system was one of mutual guaranty with no refund.
2 Amount in fund in last year of full operation of insurance system.
3 Assessments paid and used for insurance operations other than administrative expenses except in Michigan, where
amount paid was completely absorbed by such expenses.
4 In excess of amounts used to pay administrative expenses and amounts paid to banks. In Vermont, Ohio and Iowa,
such expenses absorbed the whole of investment income.
5 Total of special assessments used to redeem notes of failed banks or aid operating banks, plus estimated amounts
secured from assets in insurance funds of failed banks. Recoveries from other assets of such banks by insurance system are not known.
6 In New York, paid into Treasury; in Vermont, refunded to six banks withdrawing prior to close of system; in Ohio, refunded to one bank withdrawing prior to close of system and to all banks at close of system; and in Iowa, refunded to all banks at close of system.
Source: Federal Deposit Insurance Corporation, *Annual Report*, 1953 (1954), p. 58.

State Insurance of Bank Deposits, 1908 - 1930

From 1908 to 1917, eight states adopted deposit insurance programs. Seven of the eight states were located west of the Mississippi in predominantly agricultural areas. Table 4 summarizes the principal provisions of the eight programs.

Coverage. Insurance coverage in the eight states extended only to deposits. Although the insurance programs were commonly known as "deposit guaranty" programs, the guaranty was that of a fund derived from assessments on the participating banks. In no instance did the state explicitly guarantee the deposits.

Table 4 Principal Provisions of Deposit Insurance Programs Adopted by Eight States, 1907 - 1917

State	Deposits Insured	Banks Participating[1]	Assessment on Insured Deposits[2]	Payment of Depositors
Oklahoma Act of 19083 as amended or modified 1909, 1911, 1913	All deposits not otherwise secured and on which rate of interest was within limits specified by law.	Compulsory for all state banks and trust companies.	Annually 1/5 of 1% until fund equaled 2% of base. If fund reduced, special assessments at same rate annually.4	In cash by Bank Commission immediately upon taking possession of bank. If fund insufficient, in 6% certificates of indebtedness to be paid in order of issue. After 1913, certificates sold at not less than par for purpose of securing cash for depositors.
Kansas Act of 1909 as amended or modified 1911, 1921, 1923	All deposits not otherwise secured and on which rate of interest was within limits specified by law.	Voluntary for all incorporated state banks. Trust companies and private banks excluded. Banks organized after passage of Act eligible to apply after operating one year.	Annually 1/20 of 1% of base, less capital and surplus until fund equaled $1 million. If fund reduced below $500,000, special assessment for amount necessary.	In interest-bearing certificates of indebtedness, reduced as proceeds of liquidation become available. Deficiency, if any, paid from fund.
Nebraska Act of 1909 as amended or modified 1911	All deposits except money deposited on a collateral agreement or condition other than an agreement for length of time to maturity and rate of interest.	Compulsory for all incorporated state banks.	Semiannually 1/20 of 1% until fund equaled 1½% of base. If fund reduced below 1%, assessment renewed and special assessments if necessary not to exceed 1% of base in any one year.	In cash from fund immediately after determination by the court of amount due depositors, less cash immediately available to the receiver for such payments.
Texas Act of 1909 as amended or modified 1921, 1923	Noninterest-bearing deposits not otherwise secured. Excluded public deposits, secured deposits, certificates of deposit, deposits made for the purpose of converting a loan into a deposit covered by the fund, and certificates of deposit converted to noninterest bearing deposits within 90 days of failure.	All state-chartered banks required to choose between guaranty fund system or bond security system.	Annually ¼ of 1% of base until fund equaled $5 million. If fund reduced below $2 million, or below level of preceding January 1, special assessments not to exceed 2%.	In cash immediately, out of cash in failed bank and fund.

Mississippi Act of 1914	All deposits not otherwise secured nor bearing interest exceeding 4% per annum.	Voluntary until May15, 1915. Thereafter, compulsory for all banks operating under state law, including trust companies and savings banks.	Annually 1/20 of 1% of average guaranteed deposits, less capital and surplus, until fund approximated $500,000 over and above initial contribution. If fund depleted, special assessments at same rate not to exceed five in any one year.	In interest-bearing certificates of indebtedness, reduced as proceeds of liquidation become available. Deficiency, if any, paid from fund.
South Dakota Act of 1915 as amended or modified 1921	All deposits not otherwise secured. Deposits could not pay interest in excess of 5% unless authorized by the depositors guaranty fund commission, and in no case greater than 5 ½% per annum.	Compulsory for all state and private banks.	Annually ¼ of 1% until fund equaled 1½% of base. Resumed whenever fund reduced to 1% of base.	In cash immediately from fund. If fund deficient, Commissioner to issue certificates of indebtedness at 5% and not to exceed 7% if sold to secure cash for depositors.
North Dakota Act of 1917 as amended or modified 1923	All deposits not otherwise secured and on which interest was within limits specified by law.	Compulsory for every corporation in business of receiving deposits or buying and selling exchange, except national banks.	Annually 1/20 of 1% until fund equaled 2% of base. If fund reduced to 1½% of base, assessments resumed. Special assessments at same rate at option of Bank Commissioners, not to exceed four per year.	In cash from fund after certification of net amounts due depositors. If fund deficient, in certificates of indebtedness.
Washington Act of 1917 as amended or modified 1921	Deposits subject to check or other forms of withdrawal and not otherwise secured. Payment of interest at rates higher than authorized by guaranty fund board subjected bank to loss of insurance.	Voluntary for all state banks including trust companies but excluding mutual savings banks.	Annually 1/10 of 1% until fund equaled 3% of base. If fund reduced, special assessments not to exceed ½ of 1% in any one year.	In warrants on fund issued on proof of claim. If fund deficient, warrants to bear 5% interest until paid.

Notes:
1 National banks were prohibited from participating in state insurance plans by ruling in July 1908 by Attorney General of the United States.
2 In terms of percentage of average daily insured deposits for preceding calendar year, unless otherwise noted. Excludes initial payments or contributions
where applicable.
3 The banking laws of Oklahoma were codified, revised and reenacted May 25, 1908, with little change in guaranty

law.
4 Special assessments in addition to regular annual assessments authorized 1914-1916.
Source: Federal Deposit Insurance Corporation, *Annual Report*, 1953 (1954), pp. 68-69

Methods of paying depositors of failed banks

In Kansas and Mississippi the depositors of a failed bank received interest-bearing certificates. Dividends on these certificates were paid from liquidation proceeds. Upon final liquidation of all assets, the balance due on the certificates was paid from the insurance fund. Mississippi law stipulated that if the insurance fund was insufficient to pay the depositors, they were to be paid *pro rata*, and the remainder paid from subsequent assessments. In the remaining six states the deposit insurance law provided for immediate cash reimbursement by the fund, either in full or to whatever extent was practical. In most instances provision also was made for the issuance of certificates of indebtedness in the event there was insufficient money in the fund.

Role of bank supervision

A majority of the eight states granted authority to regulate banks. Semiannual bank examinations were the norm. Banking officials could enforce capital requirements and issue cease-and-desist orders to bring about correction of various infractions. In four of the states, supervisory authorities could order the removal of bank officials for just cause. Despite the powers granted to banking authorities, supervision often proved to be lax. Because of understaffing and insufficient funding, examiner workloads frequently were untenable. In other instances, banking authorities were thwarted when they tried to enforce existing laws. In a few cases, the authorities were the root of the problem. Oklahoma provided the worst example in that the bank commissioner's office itself became corrupt after 1919. An in-depth discussion of the role of bank supervision appears in Clark Warburton's study, *Deposit Insurance in Eight States During the Period 1908-1930* (Washington, D.C. Federal Deposit Insurance Corporation, 1959).

Assessments on participating banks

All of the insurance programs derived the bulk of their income from assessments. Both regular and special assessments were based on total deposits. The assessments levied ranged from an amount equivalent to an average annual rate of about one-eighth of 1 percent in Kansas to about two-thirds of 1 percent in Texas. Some states permitted participating banks to retain their insurance assessments in the form of deposits, subject to withdrawal by order of the insurer. Other states provided for the physical collection of assessments by the insurer or the state treasurer.

Adequacy and termination of insurance funds

The state insurance funds were unable to cope with the economic events of the 1920s. The depression of 1921, and the severe agricultural problems that persisted throughout much of the decade, resulted in numerous bank failures. The resultant claims on the various insurance funds generally exceeded their size. Although the Texas fund was able to meet all claims, the insured deposits in the other states that were never paid from any source ranged as high as 70 percent. The first fund to cease operations was Washington's in 1921. By early 1930, all of the funds had ceased operation, including the Texas fund, which became insolvent after most of the participating banks withdrew.

Congressional Proposals for Deposit Insurance, 1886 - 1933

A total of 150 proposals for deposit insurance or guaranty were made in Congress between 1886 and the establishment of the Federal Deposit Insurance Corporation in 1933. Financial crises prompted the introduction of many of these proposals. In the 60th Congress, following the panic of 1907, more than 30 proposals for deposit guaranty legislation were introduced. Similarly, in response to the developing banking crisis, more than 20 bills were introduced in the 72nd Congress, which opened in 1931. Another group of bills, similar in principle to deposit insurance, proposed to authorize national banks to issue circulating notes on the basis of various types of assets or as general obligations of the banks, backed by a guaranty or insurance fund to which all national banks would contribute. These proposals were numerous during the 30 years preceding establishment of the Federal Reserve System in 1913.

Three general methods of providing depositor protection were proposed in the bills. Of the 150 bills, 118 provided for the establishment of an insurance fund out of which depositors' losses would be paid, 22 provided for United States government guaranty of deposits, and 10 required banks to purchase surety bonds guaranteeing deposits in

full. Most of the deposit insurance bills introduced prior to establishment of the Federal Reserve System authorized participation of national banks only. After 1913, approximately one-half of the deposit insurance bills provided for participation of all members of the Federal Reserve System (national and state member banks). Only a few provided for coverage of deposits in nonmember banks, and then participation usually was optional.

Nearly two-thirds of the bills introduced prior to establishment of the Federal Reserve System provided for administration of the insurance system by the Comptroller of the Currency. After 1913, some of the proposals provided for administration by the Federal Reserve Board or by the Federal Reserve Banks under supervision of the Board. Other proposals called for the establishment of a special administrative board to oversee the insurance system. Eighty percent of the bills provided for insurance or guaranty of all, or nearly all, deposits. The bills that provided for only partial coverage of deposits contained a variety of limitations. Generally, all liabilities not otherwise secured were to be protected by the insurance or guaranty system. In nearly one-half of the bills, the entire cost of deposit insurance, and in about one-fourth of the bills the major part of the cost, was to be met by assessments based upon total deposits or average total deposits. The rates of assessment ranged from one fiftieth of 1 percent to one-half of 1 percent per year, while in a number of cases assessments were to be adjusted to meet the total cost. The most common rate was one tenth of 1 percent. Many of the bills provided for special initial assessments, or for assessments as needed, in addition to those collected periodically.

In a number of bills, assessments upon the banks were to be supplemented by appropriations from the United States government or, particularly in the bills introduced in the later years, by levies on the earnings or surplus of the Federal Reserve Banks. In several cases the cost was to be met solely by the United States government. In cases where the insurance was in the form of surety bonds, the cost of the bonds was to be borne by the banks. Many of the bills called for a limit on the accumulation of funds by the insurance or guaranty system. In a few bills, assessment rates were to be adjusted by the administrative authority and were required to be sufficient to meet all losses to depositors or to maintain the fund at a given size. In some proposals, the fund was authorized to borrow if necessary, and in others to issue certificates to unpaid depositors if the fund were depleted.

Section Summary

The disruption caused by bank failures was a recurrent problem during the 19th century and the first third of the 20th century. Numerous plans were proposed or adopted to address this problem. Many embodied the insurance principle. Insurance of bank obligations by the states occurred during two distinct periods. The first began in 1829 with the adoption of an insurance plan by New York. During the next three decades five other states followed New York's lead. Except for Michigan's insurance plan, which failed after a short period of operation, these plans accomplished their purposes. Nevertheless, the last of these insurance programs went out of existence in 1866 when the great majority of state-chartered banks became national banks. Insurance of bank obligations was not attempted again by the states until the early 1900s. Eight states established deposit guaranty funds from 1908 to 1917. In contrast to the earlier state insurance systems, those adopted from 1908 to 1917 were generally unsuccessful. Most of the eight insurance plans were particularly hard hit by the agricultural depression that followed World War I. The numerous bank failures spawned by that depression placed severe financial stress on the insurance funds. By the mid-1920s, all of the state insurance programs were in difficulty, and by early 1930 none remained in operation. The federal government, in turn, sought to secure the safety of the circulating medium through direct guaranty by the Treasury of national bank notes, beginning in the 1860s. However, the subsequent rapid growth of bank deposits relative to bank notes once again aroused concern regarding the safety of the circulating medium in the event of a bank failure. Consequently, 150 proposals for deposit insurance or guaranty were introduced into Congress between 1886 and 1933. The basic principles of the federal deposit insurance system were developed in these bills and in the experience of the various states that adopted insurance programs. These principles included financing the federal deposit insurance fund through assessments; the use of rigorous bank examination and supervision to limit the exposure of the fund; and other elements, such as standards for failed-bank payoffs and liquidations, intended to minimize the economic disruptions caused by bank failures.

CHAPTER 3 Establishment of the FDIC

The adoption of nationwide deposit insurance in 1933 was made possible by the times, by the perseverance of the Chairman of the House Committee on Banking and Currency, and by the fact that the legislation attracted support from two groups which formerly had divergent aims and interests-those who were determined to end destruction of circulating medium due to bank failures and those who sought to preserve the existing banking structure (Golembe, "The Deposit Insurance Legislation of 1933," p. 182).

Banking Developments, 1930 - 1932

An average of more than 600 banks per year failed between 1921 and 1929, which was 10 times the rate of failure during the preceding decade. The closings evoked relatively little concern, however, because they primarily involved small, rural banks, many of which were thought to be badly managed and weak. Although these failures caused the demise of the state insurance programs by early 1930, the prevailing view apparently was that the disappearance of these banks served to strengthen the banking system. This ambivalence disappeared after a wave of bank failures during the last few months of 1930 triggered widespread attempts to convert deposits to cash. Many banks, seeking to accommodate cash demands or increase liquidity, contracted credit and, in some cases, liquidated assets. This reduced the quantity of cash available to the community which, in turn, placed additional cash demands on banks. Banks were forced to restrict credit and liquidate assets, further depressing asset prices and exacerbating liquidity problems. As more banks were unable to meet withdrawals and were closed, depositors became more sensitive to rumors. Confidence in the banking system began to erode and bank "runs" became more common.

Liquidity Problems

During this period, the Federal Reserve did little to ease the liquidity problems of banks. The failure of the Federal Reserve to adopt an aggressive stance with respect to either open market purchases of securities or its discount window operations has been ascribed to several factors. A discussion of the Federal Reserve System's attitude appears in Milton Friedman and Anna J. Schwartz, *A Monetary History of the United States, 1867-1960* (Princeton, New Jersey: National Bureau of Economic Research, 1963), pp. 357-359. Much of the discussion relating to the events preceding the nationwide bank holiday is based on this source. Most notably, it was generally believed that bank failures were an outgrowth of bad management and, therefore, were not subject to corrective action by the Federal Reserve. Concern within the Federal Reserve also was muted because most failed banks in 1930 were nonmembers for which Federal Reserve officials felt no responsibility.

In all, 1,350 banks suspended operations during 1930 (Table 5).15 Bank failures during the previous decade had been confined primarily to agricultural areas; this no longer was the case in 1930. In fact, the Bank of United States, one of the nation's largest banks based in New York City, failed that year. The large jump in bank failures in 1930 was accompanied by an even greater increase in depositor losses.

The terms "bank suspensions" and "bank failures" often are used interchangeably. For the most part, this practice is followed throughout the chapter. Technically, however, "suspensions" include all banks that are closed because of financial difficulties, whereas "failures" are limited to those suspended banks that were placed in the hands of receivers and liquidated. Some of the suspended banks were reorganized or restored to solvency and resumed operations. In either instance, the assumption is that the suspended bank actually failed, though rehabilitation later occurred.

Table 5 Commercial Bank Suspensions, 1921 - 1933 ($ Thousands)

Year	Number of Suspensions (1)	Deposits (2)	Losses Borne by Depositors (3)	Losses as a Percent of Deposits in All Commercial Banks (4)
1921	506	$172,806	$59,967	0.21%
1922	366	91,182	38,223	0.13
1923	646	149,601	62,142	0.19
1924	775	210,150	79,381	0.23
1925	617	166,937	60,799	0.16
1926	975	260,153	83,066	0.21
1927	669	199,332	60,681	0.15
1928	498	142,386	43,813	0.10
1929	659	230,643	76,659	0.18
1930	1,350	837,096	237,359	0.57
1931	2,293	1,690,232	390,476	1.01
1932	1,453	706,187	168,302	0.57
1933	4,000	3,596,708	540,396	2.15
Sources: Columns (1), (2) and (3), FDIC; column (4), Friedman and Schwartz.				

As liquidity pressures subsequently eased during the early months of 1931, the number of bank failures declined sharply, but the decrease proved to be short-lived. Bank failures again rose between March and June as the public resumed converting deposits into currency and banks sought to meet withdrawal demands. During the second-half of the year, another, more serious, liquidity scramble occurred. Once again, the Federal Reserve failed to inject sufficient liquidity into the banking system. In 1931, policymakers were primarily preoccupied with international monetary matters. The abandonment by Great Britain of the gold standard in September 1931 aroused general fears that other countries might follow. These fears caused many foreigners with U.S. bank accounts to convert deposits to gold in the New York money market. To stem the ensuing gold outflow, the Federal Reserve Bank of New York sharply increased its rediscount rate. Although this action achieved the desired effect, no steps were taken to augment already depleted bank reserves through extensive open market purchases of securities. By ignoring domestic financial considerations, the Federal Reserve added to the banking industry's woes. The effects of these liquidity crises were reflected in the bank failure statistics. About 2,300 banks suspended operations in 1931. The number of failures thus exceeded the average number for the 1921-1929 period by almost threefold. Losses borne by depositors in 1931 exceeded losses for the entire 1921-1929 period.

In an attempt to ease bank liquidity problems, the National Credit Corporation was organized by private-sector bankers in October 1931 to extend loans to weakened banks. However, the corporation failed within a matter of weeks. Business leaders appealed to the federal government for assistance. The Hoover Administration responded by recommending two measures. The first resulted in the creation, in January 1932, of a new major federal lending agency, the Reconstruction Finance Corporation (RFC). One of its primary functions was to make advances to banks. By the end of 1932, the RFC had authorized almost $900 million in loans to assist over 4,000 banks striving to remain open. The RFC might have assisted more banks had Congress not ordered it to disclose publicly the names of borrowers, beginning in August 1932. Appearance of a bank's name on the list was interpreted as a sign of weakness and frequently led to runs on the bank. Consequently, many banks refrained from borrowing from the RFC.

The second measure supported by the Hoover Administration - the Glass-Steagall Act of February 27, 1932 - broadened the circumstances under which member banks could borrow from the Federal Reserve System. It enabled a member bank to borrow from a Federal Reserve Bank upon paper other than that ordinarily eligible for rediscount or as collateral for loans. Although the amounts subsequently borrowed were not large in the aggregate, the measure did aid individual banks. The generally improved banking situation during the ensuing months was marked by a significant drop in both the number of bank failures and depositor losses. However, other signs suggested that the industry's troubles were far from over. Waves of bank failures still occurred during the year. Another disquieting sign was the emergence of bank moratoria. Initially, they were declared by individual local communities. Later that year, Nevada proclaimed the first statewide moratorium when runs on individual banks threatened to involve banks throughout the state. Similar moratoria were to play a role in the events that culminated in the nationwide bank holiday of 1933.

The Banking Crisis of 1933

During the winter of 1932-1933, banking conditions deteriorated rapidly. In retrospect, it is not possible to point to any single factor that precipitated the calamitous events of this period. The general uncertainty with respect to monetary and banking conditions undoubtedly played the major role, although there were specific events that tended to increase liquidity pressures within the system. Banks, especially in states that had declared bank moratoria, accelerated withdrawals from correspondents in an attempt to strengthen their position. Currency holdings increased significantly, partially in anticipation of additional bank moratoria.

Additional liquidity pressures were brought about by concern relating to the future of the dollar. With the election of Franklin D. Roosevelt in November 1932, rumors circulated that the new administration would devalue the dollar, which led to an increase in speculative holdings of foreign currencies, gold and gold certificates. Unlike the period of international monetary instability in 1931, a significant amount of the conversions from Federal Reserve notes and deposits to gold came from domestic sources. These demands placed considerable strain on New York City banks and, ultimately, on the Federal Reserve Bank of New York. It was the suddenness of the withdrawal demands in selected parts of the country that started a panic of massive proportions. State after state declared bank holidays. The banking panic reached a peak during the first three days of March 1933. Visitors arriving in Washington to attend the presidential inauguration found notices in their hotel rooms that checks drawn on out-of-town banks would not be honored. By March 4, Inauguration Day, every state in the Union had declared a bank holiday. As one of his first official acts, President Roosevelt proclaimed a nationwide bank holiday to commence on March 6 and last four days. Administration officials quickly began to draft legislation designed to legalize the holiday and resolve the banking crisis. Early in their deliberations they realized that the success of any proposed plan of action primarily would hinge on favorable public reaction. As noted by Raymond Moley, a key presidential adviser who attended many of the planning sessions:

We knew how much of banking depended upon make-believe or, stated more conservatively, the vital part that public confidence had in assuring solvency. (Raymond Moley, *The First New Deal* (New York: Harcourt, Brace & World, Inc. 1966), p. 171)

Formulating an Insurance Plan

To secure public support, officials formulated a plan that relied on orthodox banking procedures. Few members of Congress knew what was contained in the Administration's bill when they convened in extraordinary session at noon on March 9. In fact, Henry B. Steagall, Chairman of the Committee on Banking and Currency, purportedly had the only copy of the bill in the House. Waving the copy over his head, Steagall had entered the House chamber, shouting, "Here's the bill. Let's pass it." After only 40 minutes of debate, during which time no amendments were permitted, the House passed the bill, known as the Emergency Banking Act. Several hours later, the Senate also approved the emergency legislation intact. The Emergency Banking Act legalized the national bank holiday and set standards for the reopening of banks after the holiday. The Act expanded the RFC's powers as a means of dealing with the crisis then threatening the banking system. It authorized the RFC to invest in the preferred stock and capital notes of banks and to make secured loans to individual banks.

To ensure an adequate supply of currency, the Act provided for the issuance of Federal Reserve Notes, which were to be backed by U.S. government securities. The Federal Reserve Banks were empowered to advance the new currency to member banks without requiring much collateral. After the Act was signed into law, the Bureau of Engraving and Printing promptly went into 24-hour production to manufacture the currency. The President subsequently issued a proclamation extending the holiday in order to allow time for officials to reopen the banks. In his first "fireside chat," delivered on March 12, President Roosevelt reviewed the events of the past several days and outlined the reopening schedule. Following proper certification, member banks in the 12 Federal Reserve Bank cities were to reopen on March 13. Member banks in some 250 other cities with recognized clearinghouses were to reopen on March 14. Thereafter, licensed member banks in all other localities were to reopen. The President indicated that the Secretary of the Treasury already had contacted the various state banking departments and requested them to follow the same schedule in reopening state nonmember banks. Before concluding his radio address, the President cautioned that he could not promise that every bank in the nation would be reopened. About 4,000 banks never reopened either because of the events of the previous two months or the bank holiday itself.

The task of implementing the Emergency Banking Act primarily was the responsibility of the Secretary of the Treasury. Under the Act, licenses for all member banks, both national and state, were to be issued by the Secretary. (State nonmember banks were to be licensed by the state banking departments.) The Treasury, however, demanded that each of the Federal Reserve Banks approve of the reopening of banks in their respective districts. The Federal Reserve Board balked at this demand, preferring instead that the Treasury Department shoulder the entire burden of reopening member banks. The controversy was resolved in the Treasury Department's favor. It was agreed that licenses would be issued by the Secretary of the Treasury upon the recommendation of the district Federal Reserve Bank, the chief national bank examiner and the Comptroller of the Currency. Several hundred banks soon reopened for business on the certification of the Treasury. As the reopening proceeded, public confidence increased significantly and widespread hoarding ceased.

Federal Deposit Insurance Legislation

After some semblance of order had returned to the financial system, efforts were renewed in Congress to enact deposit insurance legislation. Although a deposit insurance bill had been passed by the House in 1932, the Senate had adjourned without acting on the proposal. Insurance proponents hoped that legislative efforts would prove successful this time, since the banking crisis was still fresh in the public's mind. In their view, recent events had shown that a system of federal deposit insurance was necessary to achieve and maintain financial stability.
One of the chief proponents of federal deposit insurance in Congress was Representative Steagall. He has been credited with proposing the legislation that created the Federal Deposit Insurance Corporation, leading the fight for its adoption in the House and helping to effect a compromise when chances for passage of the bill appeared doomed. Steagall's achievement was all the more remarkable in view of the formidable opposition confronting the proponents of deposit insurance. Opposition emanated from the Roosevelt Administration, segments of the banking industry and from some members of Congress.

Arguments offered against deposit insurance reflected both practical and philosophical considerations. Opponents asserted that deposit insurance would never work. They pointed to the defunct state-level deposit insurance programs to substantiate their argument. Another widely held view was that deposit insurance would remove penalties for bad management. Critics also charged that deposit insurance would be too expensive and that it would represent an unwarranted intrusion by the federal government into the private sector. Within the Roosevelt Administration, the Secretary of the Treasury Woodin was strongly opposed to the idea of federal deposit

insurance. While historians have asserted that the Secretary's views were partially responsible for President Roosevelt's opposition to deposit insurance, accounts differ regarding the nature and extent of Roosevelt's opposition. However, the Administration was not of one mind on the issue. Support was voiced by Vice President John Nance Garner and Jesse H. Jones of the RFC, among others. Prior to Roosevelt's inauguration, Garner, then-Speaker of the House, had appealed to the President-elect to support deposit insurance. When Roosevelt declined, stating that it would never work, Garner predicted that deposit insurance legislation eventually would be passed. Banking interests, particularly those representing the larger banks, generally viewed federal deposit insurance with distaste. The President of the American Bankers Association declared that deposit insurance was "unsound, unscientific and dangerous." ("Wires Banks to Urge Veto of Glass Bill," *The New York Times*, June 16, 1933, p. 14.)

The banking industry's views had only limited effect since banking at that time was held in low esteem. The industry's already tarnished image was not helped by disclosures of unsavory security market dealings on the part of certain New York banks which came to light when deposit insurance was being considered in Congress. More formidable opposition to deposit insurance came from several influential Congressmen. One of the most vociferous opponents was Carter Glass of Virginia, Chairman of the Senate Banking and Currency Committee. He had been Roosevelt's initial choice to serve as Secretary of the Treasury, but declined the Cabinet offer. Although Senator Glass was intent on passing banking reform legislation, federal deposit insurance was not one of the reforms he supported or sought. In opposing federal deposit insurance, Glass pointed to the record of the defunct state insurance programs. Nevertheless, he subsequently allowed bank deposit insurance to be written into a banking bill that he had sponsored. One business journal during the period reported that Glass simply had yielded to public opinion in saying "It became perfectly apparent that the voters wanted the guarantee [deposit insurance], and that no bill which did not contain such a provision would be satisfactory either to Congress or to the public. Washington does not remember any issue on which the sentiment of the country has been so undivided or so emphatically expressed as upon this." ("Deposit Insurance," *Business Week*, April 12, 1933, p. 3.)

Genesis of Glass-Steagall

In mid-May both Senator Glass and Representative Steagall formally introduced banking reform bills, which included provisions for deposit insurance. The two bills primarily differed with respect to the conditions for membership in the deposit insurance corporation that was to be created. Whereas membership in the Federal Reserve was a precondition for obtaining deposit insurance under the Senate bill, it was not a prerequisite in the House version. Both bills incorporated the demands made by the Roosevelt Administration that deposit coverage be based on a sliding scale, and there be a one-year delay in the start of the insurance corporation.

Later that month, however, the Glass bill was amended to incorporate Senator Arthur Vandenberg's proposal calling for the creation of a temporary deposit insurance fund. Vandenberg opposed a delay in the start of deposit insurance because, as he put it, "…the need is greater in the next year than for the next hundred years." ("Bank Bill Debate to Open in Senate," *The New York Times*, May 19, 1933, p. 4)

On the day Vandenberg introduced his proposal, Vice President Garner was presiding over the Senate, which was sitting as a court of impeachment in the trial of a district judge. Garner had heard that Vandenberg had formulated a deposit insurance plan that would accomplish the same goals as those contained in an insurance bill which Garner had pushed through the House in 1932. Desiring that deposit insurance be implemented as soon as possible, Garner therefore approached Vandenberg during the impeachment proceedings and inquired whether he had the deposit insurance amendment in his possession. After Vandenberg responded affirmatively, Garner instructed him to introduce the amendment when signaled. Several minutes later, Garner suspended the court proceedings and ordered the Senate into regular session to consider more banking legislation. With Garner sitting by his side, Vandenberg then offered his deposit insurance amendment, which was overwhelmingly adopted.

Vandenberg Amendment

The amendment stipulated that, effective January 1, 1934; the temporary fund would provide insurance coverage up to $2,500 for each depositor and would function until a permanent corporation began operations on July 1, 1934. If demands on the temporary fund exceeded available monies, the Treasury would be obligated to make up the difference. The amendment also provided that solvent state banks could join the fund. The inclusion of the Vandenberg amendment in the Senate bill almost resulted in the defeat of deposit insurance in Congress. When the banking reform bills that had been passed by both houses were sent to a joint conference committee for resolution of differences, an impasse promptly developed. The House conferees opposed the Vandenberg amendment contained in the Senate version of the bill, particularly the provision calling for the immediate establishment of a temporary insurance corporation. Another issue that split the conferees was whether Federal Reserve membership should be a precondition for obtaining deposit insurance. A compromise finally was reached

on June 12, after the Senate conferees threatened to remove all deposit insurance provisions from the bill. They feared that the impasse over deposit insurance could endanger all of the banking reform measures contained in the bill. In order to save the bill, the House conferees reluctantly accepted the Senate's version as well as an additional provision desired by the Senate conferees to liberalize the branching restrictions governing national banks. This provision reflected widespread public disillusionment with the failure-prone independent banking system. Proponents of branch banking maintained that geographic diversification of lending risks and the deposit base would result in a lower bank failure rate.

The bill agreed to by the conferees passed both houses of Congress on the following day. Some opponents of deposit insurance had not yet thrown in the towel, though. The American Bankers Association wired its member banks, urging them to telegraph President Roosevelt immediately to request his veto of the legislation. Nevertheless, Roosevelt signed the measure, known as the Banking Act of 1933, into law on June 16, 1933. Section 8 of the Act created the Federal Deposit Insurance Corporation through an amendment to the Federal Reserve Act. The Banking Act of 1933 also created the Federal Reserve Open Market Committee and imposed restrictions on the permissible activities of member banks of the Federal Reserve System.

Deposit Insurance Provisions of the Banking Act of 1933

Section 12B of the Federal Reserve Act as amended created the Federal Deposit Insurance Corporation and defined its organization, duties and functions. It provided for two separate plans of deposit insurance: a temporary plan which was to be initiated on January 1, 1934, and a permanent plan which was to become effective on July 1, 1934. Capital necessary to establish the FDIC was to be provided by the United States Treasury and the 12 Federal Reserve Banks. The Treasury was to contribute $150 million. Each of the Federal Reserve Banks was required to subscribe to Class B capital stock in an amount equal to one-half of its surplus as of January 1, 1933.

Management of the FDIC was vested in a Board of Directors consisting of three members. The Comptroller of the Currency was designated a member *ex officio*; the other two members were to be appointed by the President for six-year terms with the advice and consent of the Senate. One of the two appointive directors was to serve as Chairman of the Board, and not more than two members of the Board could be members of the same political party. The temporary plan of deposit insurance was to initially limit protection to $2,500 for each depositor. Banks admitted to insurance under the temporary plan were to be assessed an amount equal to one-half of 1 percent of insurable deposits. One-half of the assessment was payable at once; the rest was payable upon call by the FDIC. All Federal Reserve member banks licensed by the Secretary of the Treasury under terms of an Executive Order of the President, issued March 10, 1933, were required by law to become members of the temporary fund on January 1, 1934. Other banks were authorized to join the fund upon certification of their solvency by the respective state supervisory agencies and after examination by, and with the approval of, the Federal Deposit Insurance Corporation.

The original permanent plan, while it never took effect and was superseded by a new permanent plan in the Banking Act of 1935, contained certain features of historical interest. Banks participating in insurance under the original plan were to subscribe to capital stock of the FDIC and be subject to whatever assessments might be needed to meet the losses from deposit insurance operations. The plan provided for full protection of the first $10,000 of each depositor, 75 percent coverage of the next $40,000 of deposits, and 50 percent coverage of all deposits in excess of $50,000. In order to retain their insurance, all participating banks were required to become members of the Federal Reserve System within two years. Thus, with regard to financing, degree of protection and supervisory provisions, the original plan differed significantly from both the temporary plan and the permanent plan that became effective with the Banking Act of 1935.

Formation of the Federal Deposit Insurance Corporation

One of the first tasks facing the FDIC was the formation of an operating organization. As provided in the Banking Act of 1933, the Comptroller of the Currency, J. F. T. O'Connor, was designated as a director. He served as the FDIC's chief executive until the appointment of the other two directors. In September, the President appointed as the other directors Walter J. Cummings, then-special-assistant to Secretary of the Treasury Woodin, and E. G. Bennett, a Republican banker and businessman from Utah. The directors organized on September 11, 1933, and elected Cummings to serve as Chairman of the Board. As was his intent, Cummings' chairmanship lasted only through the initial organization of the FDIC. In January 1934, he left the FDIC to assume the chairmanship of Continental Illinois National Bank & Trust Company in Chicago. Bank examination consumed nearly all of the FDIC's efforts in the months before the establishment of the temporary fund on January 1, 1934. The hastily assembled examination force had to examine almost 8,000 state-chartered nonmember banks in three months in order for the FDIC to meet its responsibilities under the Banking Act of 1933. The task of completing these admission examinations was largely accomplished as intended by the end of 1933. Of the 7,834 applicant

nonmember banks, 83 percent were approved for insurance, 12 percent were rejected, 4 percent were still pending decisions, and less than 1 percent remained to be examined.

The Temporary Federal Deposit Insurance Fund

Actual insurance of bank deposits became effective on January 1, 1934. The Temporary Federal Deposit Insurance Fund opened with 13,20l banks insured (or approved for insurance). Of these, 12,987 were commercial banks and 214 were mutual savings banks. These represented 90 percent of all commercial banks and 36 percent of all mutual savings banks. The lower participation rate among savings banks was attributable to several factors.

Admission standards

Many savings banks questioned whether they needed deposit insurance. Unlike commercial banks, savings banks had not been seriously affected by bank runs since they legally could restrict deposit withdrawals. In several states mutual savings banks legally could not subscribe to stock in the FDIC. In other instances, savings banks objected to FDIC membership on philosophical grounds. As summed up by one savings banker, "I for one want none of this FDIC. If it's New Deal, that damns it as far as I'm concerned." (Oscar Schisgall, *Out of One Small Chest* (New York: AMACOM, 1975), p. 146)

Pursuant to the intent of Congress, the FDIC accepted for insurance all banks that it found to be solvent. However, it was recognized that a great many banks lacked sufficient capital, which posed a huge risk for the insurance fund. Some banks were admitted upon a commitment to increase their capital, either from the RFC or local interests. A program of reexamination and rehabilitation was carried on throughout the year by the FDIC.

Organizational changes and Legislative developments

Following the departure of Walter J. Cummings, E. G. Bennett served briefly as acting chairman of the FDIC. In February 1934, Leo T. Crowley, a 46-year-old bachelor, became chairman. As former owner of several Wisconsin banks during the Depression, he had organized and headed the Wisconsin Banking Review Board. In December 1933, he journeyed to Washington, D.C., seeking aid for several hundred Wisconsin banks so they could qualify for deposit insurance. His role in restoring the health of Depression-struck banks in his native state brought him to the attention of the Roosevelt Administration. The appointment of Crowley proved to be especially felicitous. An imposing man, he possessed both a witty personality and exceptional administrative skills. He left an indelible imprint on the FDIC during his 12-year term as chairman.

The Banking Act of 1933 provided for termination of the Temporary Federal Deposit Insurance Fund and the inauguration of the permanent insurance plan on July 1, 1934. However, in the early part of 1934, FDIC officials recommended that the Temporary Federal Deposit Insurance Fund be extended for another year and that the law be amended in certain minor respects to facilitate administration. It was considered advisable to give the states additional time to adopt legislation to enable state banks to enjoy the full benefits of federal deposit insurance. FDIC officials also desired to gain more experience with the administration and operation of an insurance plan prior to the inauguration of the permanent plan. Moreover, the capital rehabilitation program for banks could not have been completed by July 1934, as required, to permit all banks insured with the Temporary Federal Deposit Insurance Fund to qualify for insurance under the permanent plan. On June 16, 1934, Congress extended the life of the Temporary Federal Deposit Insurance Fund, and the effective date of the permanent plan was postponed one year, to July 1, 1935. The life of the temporary plan subsequently was extended for an additional two months. The second extension was approved June 28, 1935, while the Banking Act of 1935 was under consideration, and was designed merely to continue the temporary plan until that Act could be approved.

Insured nonmember banks were allowed to terminate their membership in the Temporary Federal Deposit Insurance Fund on July 1, 1934, provided they gave adequate notice to the FDIC. Provision was made for refunding the assessments collected from the banks that withdrew. Only 21 commercial banks elected to withdraw from the fund. There had been some doubt as to the legality of some mutual savings banks qualifying as members of the permanent plan of deposit insurance. Furthermore, many mutual savings banks considered themselves preferred risks and wished to avoid assessment at the same rate as commercial banks. For these and other reasons, 169 mutual savings banks withdrew from the Temporary Federal Deposit Insurance Fund at the end of June 1934. Of these, 133 were located in New York State. Only two New York mutual savings banks, Emigrant Savings Bank and Franklin Savings Bank, kept their insurance with the FDIC.

Effective July 1, 1934, insurance protection was increased from $2,500 to $5,000 for each depositor at an insured institution, except in the case of certain mutual savings banks. Insurance protection remained at $2,500 for each depositor at a mutual savings bank except that any mutual savings bank could, with the consent of the FDIC, elect

to be insured up to $5,000. At the discretion of its Board of Directors, the FDIC was authorized to set up a separate fund for mutual savings banks to be known as the Fund For Mutuals. The Temporary Federal Deposit Insurance Fund was not to be subject to the liabilities of the Fund For Mutuals, and *vice versa*. A separate Fund For Mutuals was established by the Board of Directors on July 14, 1934, effective July 1, 1934. Upon inception of the permanent plan in 1935, this fund and the fund for commercial banks were consolidated. Under the previously existing law, insured nonmember banks were required to apply to become members of the Federal Reserve System on or before July 1, 1936, in order to continue their insurance. With the one-year delay in the establishment of the permanent fund, this requirement was changed by pushing the date back to July 1, 1937. Banks in the territories of Hawaii, Puerto Rico, Alaska and the Virgin Islands were made eligible for insurance. In addition, the language authorizing the FDIC to act as receiver in the case of failed insured banks was clarified. By a new provision of the law, each insured bank was required to display signs to the effect that its deposits were insured by the Federal Deposit Insurance Corporation. The intent of this practice, which continues today, was to make the absence of such a sign conspicuous.

Deposit Insurance and Banking Developments in 1934

Total deposits in insured and uninsured licensed commercial banks increased during 1934 by about $7.2 billion dollars, or 22 percent. This growth in deposits had rarely been equaled in the past and restored to the banking system approximately half of the decline in deposits that had occurred during the preceding three years. The growth in bank deposits was accompanied by changes in the character and quality of the assets held by insured banks. Cash, amounts due from other banks and holdings of direct obligations of the United States government increased considerably. The average quality of the assets of insured commercial banks improved as large amounts of worthless and doubtful assets were written off. Increased earnings and new capital, obtained from the RFC and local interests, is what maintained banks' capital positions. At the close of 1934, insured banks held 98 percent of the assets of all licensed commercial banks. The liquidity buildup undertaken by banks during 1934 caused FDIC officials some concern. They feared that excessive holdings by banks of cash and government securities could stifle economic recovery. Speeches given by the FDIC's directors during that period frequently contained exhortations urging bankers to expand their loan portfolios. Only nine insured banks and 52 uninsured licensed banks suspended operations during 1934. All but one of the insured banks and most of the uninsured licensed banks that failed during 1934 were small institutions. More than 900 banks that were not licensed after the holiday were placed in receivership or liquidation. More than half of these banks had a part of their assets and liabilities taken over by successor banks.

In its 1934 *Annual Report*, the FDIC rather modestly attributed the small number of failures of licensed banks to factors other than deposit insurance. It noted that many banks were able to survive because they had received necessary financial assistance from the RFC and other governmental agencies. Secondly, events during 1933 had weeded out many weak banks. Third, improved economic conditions also had played a role in keeping down the failure rate. The FDIC warned that the low rate of failures could not be expected to continue. During 1934, the fierce opposition of the banking industry faded in the face of the success of deposit insurance. The industry's changed attitude was reflected in the public endorsement of the temporary insurance plan by the Executive Council of the American Bankers Association in April of that year. Public sentiment continued to support deposit insurance.

CHAPTER 4 The Early Years of FDIC: 1934 - 1941

The history of the FDIC cannot be considered apart from changes in economic and banking conditions. The early years of the FDIC's existence were not a period of risk-taking by banks. Caution marked the attitudes of both the supervisory agencies and the industry itself. For their part, the supervisory agencies viewed the events that culminated in the nationwide bank holiday as a banking rather than a monetary phenomenon.

Background

The prevailing philosophy was that unfettered competition in the past had resulted in excesses and abuses in banking. Consequently, the supervisory agencies followed what the FDIC later termed as a policy of keeping banks and banking practices within the bounds of rightful competition. The attitude of bankers was similarly circumspect. Those who survived the Depression were chastened by that experience. The effect of the Depression experience on the industry was reflected in the subsequent massive liquidity buildup undertaken by banks. By 1937, for example, cash and holdings of U.S. government securities comprised about 52 percent of the industry's total assets, or more than twice the proportion held in 1929. To the dismay of would-be borrowers, banks continued to stress liquidity for many more years.

Legislation enacted in the 1930s to insulate banks from competing with one another too aggressively also restrained bank behavior. The Banking Act of 1933 outlawed the payment of interest by member banks on demand deposits. The Act also authorized the Federal Reserve Board to set a ceiling on time deposit rates offered by member banks in order to forestall ruinous competition among banks. In addition, the 1933 law ordered the separation of investment from commercial banking to be completed by mid-June 1934. The Banking Act of 1935 similarly incorporated provisions designed to limit bank behavior. The Act expanded the FDIC's supervisory powers and set more rigorous standards for admission to insurance. The 1935 law required the FDIC to prohibit the payment of interest on demand deposits in insured nonmember banks and to limit the rates of interest paid.

While the effects of a still-depressed economy also engendered caution on the part of bankers and regulators, conditions improved from the low point reached in 1933. Unemployment declined significantly, real GNP increased at an average annual compound growth rate of 9.5 percent between 1933 and 1937, and price increases were moderate. The recession of 1937-1938 interrupted this pattern of economic expansion. Owing to the continuous improvement in the banking system that had occurred since the bank holiday of 1933, however, banks were able to meet without difficulty the strains resulting from the decline in business activity that ensued. Following the recession, economic conditions improved once again as real GNP rose and unemployment abated.

Capital Rehabilitation

After the initial admission examinations had been completed, in early 1934 the FDIC shifted the emphasis of its examination function from determining minimal acceptability to the strengthening of weaker banks, particularly in the area of capital adequacy. It was determined that minimal safety required banks to have net sound capital equal to at least 10 percent of deposits. Net sound capital was defined as equity, capital notes, debentures and reserves, fewer assets classified as worthless or of doubtful value, including bond depreciation. Based upon admission examination findings, all banks not meeting this standard were reexamined during the first six months of 1934. The same cooperation accorded to banks initially rejected for deposit insurance was given to those banks requiring capital rehabilitation. Of the state nonmember banks admitted to the fund, 35 percent were found to be undercapitalized. Subsequent examinations and rehabilitative efforts reduced this ratio to just 13 percent by the end of 1934. Many other banks recorded significant improvements though they still fell short of the 10 percent standard. For example, 20 percent of the initial applicants had net sound capital of less than 5 percent, but by year-end 1934, only 3 percent were under this level. This improvement in capital was achieved despite the fact that insured nonmember banks wrote off adversely classified assets equal to 20 percent of their total capital. The RFC supplied most of the funds used to offset these write-offs, while the remainder was supplied by local interests and retained earnings. By the end of 1934, the concept of federal deposit insurance was generally accepted, even by most of its detractors. As one measure that public confidence had been restored, bank runs were no longer a significant problem, although they did not disappear altogether. Local concerns about the solvency of an individual bank still gave rise to occasional bank runs. In some instances, fears were aroused when it was felt that bank examiners had overstayed their "normal" visit to a bank, although these fears were usually groundless. (Interview with Neil Greensides, former Chief, FDIC Division of Examinations, Washington, DC, August 16, 1983)

Safety-and-Soundness Examination Policy

After completing its first two examination tasks - admissions and capital rehabilitation - the FDIC again shifted its examination focus and concentrated on developing permanent examination policies and procedures. The purposes of these examinations were fivefold:
Appraise assets in order to determine net worth;
Determine asset quality;
Identify practices that could lead to financial difficulties;
Appraise bank management; and
Identify irregularities and violations of law.

In addition to completing and reviewing its own examinations, in 1936 the FDIC began reviewing examination reports of national and state member banks because the FDIC had an insurance exposure for these banks supervised by the Comptroller of the Currency and the Federal Reserve. Some analysts came to the conclusion that supervisory policies in the 1930s were unduly harsh, and that recessionary periods were not the time to pressure banks to sell depreciated assets and reduce risk. Such practices, it was felt, would lead to a restriction of credit as well as otherwise unnecessary bank liquidations and forced mergers. These concerns had been expressed to the Comptroller of the Currency in 1931, but policy directives at that time were generally ineffective. A sharp recession had begun in 1937, rekindling these criticisms of bank examination policy, and in 1938 Secretary of the Treasury Morgenthau called for a conference of bank examiners. This time around, policy changes were strictly translated into examination procedures, resulting in more lenient asset valuation techniques. It was agreed that most bonds would be appraised at book value rather than market value, a policy believed to be more reflective of long-term investment quality. Moreover, a larger portion of classified assets were to be included in the capital ratio calculation. These policy shifts caused only a slight increase in aggregate capital-to-assets ratios - 12.8 percent under the new method *versus* 12.6 percent under the old - but the difference at individual banks, particularly marginal performers, could be critical. The 1938 conference also led to a revision of the nomenclature of asset classification, establishing the four groups that have remained essentially unchanged:
I not mentioned,
II substantial and unreasonable risk,
III loss is probable and
IV uncollectible (immediate charge-off)

Since 1949, categories II, III and IV have been referred to respectively as substandard, doubtful and loss.

The Banking Act of 1935

During the 20 months that the Temporary Federal Deposit Insurance Fund was in operation, the banking situation improved significantly. Attention was shifted to the specific insurance provisions of the 1933 Act. Most of those who had originally opposed deposit insurance legislation apparently had been convinced that the existence of the FDIC was a major contributing factor to the drastic reduction in bank failures. However, various provisions of the original permanent plan were viewed as not being appropriate in the new environment. The banking industry did not like the potential for virtually unlimited assessments and generally felt that the assessment rate should be set at a relatively low level. Large banks took exception to shifting the assessment base from insured to total deposits, contending that they would be unduly penalized because of the relatively large proportion of uninsured deposits held in larger institutions. State-chartered nonmember banks objected to mandatory membership in the Federal Reserve System as a precondition for retaining deposit insurance coverage.

FDIC recommendations

For its part, the FDIC was faced with a dilemma. Although the bank failure rate had dropped precipitously and the capital rehabilitation program of the RFC and the FDIC had been moderately successful, the banking system was not strong and the prospects for bank earnings were not bright. Additionally, the fears and uncertainties regarding the bank failure rate had not been dispelled by 1934 and indeed would not recede for more than two decades. The FDIC thus was faced with the problems of protecting the earnings of insured banks until capital and reserve positions could be rebuilt while, at the same time, conserving what was by historical standards a modest deposit insurance fund. During 1934, FDIC staff began drafting what was to become Title I of the Banking Act of 1935. In hearings beginning in February 1935 before the House Committee on Banking and Currency, FDIC Chairman Leo Crowley articulated his plan for the future of federal deposit insurance. The FDIC had calculated that during the period 1865-1934, an annual average assessment rate of about one-third of 1 percent of total deposits would have been required to cover the actual losses on deposit balances in failed banks. However, if certain "crisis" years in which losses were unusually high were eliminated, the necessary rate would have been lowered to about one-twelfth of 1 percent. Adoption of the lower rate was justified on the grounds that many banking reforms and

improvements had occurred to strengthen the banking system and prevent bank failures. In addition to an assessment rate lower than historical experience would suggest, Crowley's plan consisted of a combination of stricter entrance standards for new banks and expanded authority over the actions of existing banks, expanded powers regarding the handling of failing banks, a reduction in insurance exposure (*i.e.*, retaining the $5,000 insurance coverage rather than the higher limits envisioned in the original permanent plan) and other provisions that would tend to conserve the deposit insurance fund. From a practical point of view, the program advocated by Crowley consisted of attempting to strengthen the banking system, while using every legal means available to conserve FDIC financial resources. This philosophy dominated FDIC behavior until the mid-1960s.

Enactment and Admissions

By early August, the two houses of Congress resolved their differences on changes in the assessment rate, accepting the rate recommended by the FDIC. A compromise also was reached on the Federal Reserve membership issue. In the final conference report, which was accepted by both houses on August 19, only insured banks with more than $1 million in deposits would be required to join the Federal Reserve System, beginning in 1941. The membership requirement was rescinded altogether in 1939. The Banking Act of 1935 became effective August 23, 1935. The deposit insurance provisions of the Act, with few exceptions, were identical to the draft legislation prepared by the FDIC. From a financial point of view, one of the most significant revisions to the original permanent plan related to the calculation of assessments levied on insured banks. The 1935 Act provided that assessments were to be based on a flat annual rate of one-twelfth of 1 percent of *total* (adjusted) deposits. The effect of this change was to shift the relative burden of the deposit insurance system to the larger banks while protecting the level of assessment income to the FDIC.

The Banking Act of 1935 provided for the automatic admission to insurance under the permanent plan of all banks insured at the close of the temporary funds, except banks which signified, within 30 days, their intention to withdraw from insurance and those banks that had failed to file the required certified statement of deposits and to pay the required assessments. Thirty-four banks insured under the temporary plan withdrew within 30 days after the close of the temporary funds. One other bank had its insurance status terminated by reason of failure to file the certified statement. Automatically admitted to insurance under the permanent plan were 14,219 banks. Of these, 14,163 were commercial banks insured in the Temporary Federal Deposit Insurance Fund and 56 were mutual savings banks insured in the Fund For Mutuals. The 1935 Act set more rigorous standards for admission to insurance. In acting on insurance applications from new banks, the FDIC was required to consider the adequacy of the bank's capital, its future earnings prospects, the quality of its management and its usefulness in serving the convenience and needs of the community. The revised law, moreover, provided that any balances to which an insured bank was entitled, upon termination of the temporary federal deposit insurance funds, were to be credited toward the assessment to be levied under the permanent insurance plan. These balances consisted of the unused portion of assessments collected under the temporary plan. Since investment income of the temporary funds was sufficient to pay all of the operating expenses of the FDIC and cover deposit insurance losses and expenses, insured banks received a credit for the full amount of the assessments they had paid.

Supervisory powers

Insured nonmember banks were required to obtain the FDIC's approval before opening new branches or reducing their capital. The Act required all insured banks to obtain approval before merging or consolidating with noninsured institutions. The FDIC was empowered to require any insured bank to provide protection and indemnity against burglary, defalcation and other similar insurable losses. If an insured bank was found by the FDIC to have continued unsafe or unsound practices, the practices were to be reported to the appropriate supervisory authorities. A bank's insurance status could be terminated if the practices were not corrected. In order to strengthen the banking system, the FDIC was given the right to make a loan to, or purchase assets from, an open or closed insured bank to facilitate its merger or consolidation with another insured bank, if the merger would reduce the risk or avert a threatened loss to the FDIC. This power, which was first granted on a temporary basis, later was made permanent. The Banking Act of 1935 required the FDIC to prohibit the payment of interest on demand deposits in insured nonmember banks and to limit the rates of interest paid on savings and time deposits. The FDIC also was required to prohibit insured nonmember banks from paying any time deposit before its maturity, except as prescribed by the FDIC. In granting these and other regulatory powers to the FDIC, Congress sought to prevent unsound competition among banks. The prevailing philosophy was that unfettered competition in the past had resulted in excesses and abuses in banking as well as other industries. The restrictive powers contained in the Banking Act of 1935 were thus consistent with the tenor of other New Deal legislative programs.

Borrowing authority- The FDIC was authorized to issue notes or other obligations in an amount not to exceed $975 million, and the RFC and the Secretary of the Treasury were directed to purchase up to $500 million of these

notes if the funds were needed for the payment of depositors. The FDIC never borrowed under this provision of the Act. The Act also deleted the requirement for initial and subsequent capital subscriptions by insured banks, and the payment of dividends on capital stock held by the U.S. Treasury was eliminated.

Insured-Bank Failures

The Banking Act of 1933 authorized the FDIC to pay up to $2,500 to depositors in insured banks that failed. The only procedure to be used to pay depositors was a Deposit Insurance National Bank (DINB), a new national bank chartered without any capitalization and with limited life and powers. During the period of the temporary deposit insurance plan, January 1, 1934 to August 23, 1935, 24 insured banks were placed into receivership and their depositors paid off through a DINB. The first FDIC insured bank to fail was the Fondulac State Bank in East Peoria, Illinois, which was closed by the state in May 1934. Mrs. Lydia Lobsiger received the first federal deposit insurance payout, a check for $1,250 dated July 3, 1934. This was the only bank to fail while the $2,500 coverage limit was in effect. The 1935 Act gave the FDIC the authority to pay off depositors directly or through an existing bank, and once that authority was granted, the FDIC ceased using the DINB for the next 29 years. The DINB provides a vehicle for a slow and orderly payout, and its use in recent years has been confined to situations where only limited banking services were available in the community or where a regular payoff would have been substantially delayed. In addition to broadening the ways in which a payoff could be affected, the 1935 Act gave the FDIC the authority to make loans, purchase assets and provide guarantees to facilitate a merger or acquisition. This authority had been sought by the FDIC because of its concern that many of the banks that had been granted deposit insurance might not survive, and paying off insured depositors in these banks would be too expensive. In addition, most banking observers felt that there were too many banks in operation and that it would be desirable if the FDIC could facilitate an orderly reduction in their number through increased mergers.

The FDIC handled 370 bank failures from 1934 through 1941, an average of more than 50 per year. Most of these were small banks. Without the presence of federal deposit insurance, the number of bank failures undoubtedly would have been greater and the bank population would have been reduced. The presence of deposit insurance also may have limited the necessity for some banks to merge, and may have indirectly encouraged retention of restrictive state branching laws. Insurance losses totaled nearly $23 million during this period. The FDIC had positive net income in all but its first year of operation, though, and the insurance fund continued to grow. The year-end 1941 fund balance was $553.5 million. This resulted in a ratio of the fund to insured deposits of 1.96 percent, which remains the highest reserve ratio in the history of the FDIC. The end of 1941 marked the completion of eight years of successful operation of the system of federal insurance of bank deposits. It also marked the close of a period of economic recovery under peacetime conditions, which provided especially favorable circumstances for the establishment of deposit insurance and for improvement in the financial condition of banks.

CHAPTER 5 War and Recovery: 1942 - 1970

During World II, government financial policies and private-sector restrictions produced an expanding banking system. Total bank assets at the end of 1945 were nearly double the $91 billion total at the end of 1941. Large-scale war financing of the federal government was the primary factor contributing to the rise in bank assets. Banks played a major role in financing the war effort by lending to other bond buyers, by handling the bulk of the war loan campaign sales volume, and by purchasing government obligations themselves. At the end of 1945, holdings of those obligations accounted for 57 percent of total bank assets.

Loan losses were practically nonexistent during the war years and bank failures declined significantly. Only 28 insured banks failed in the period 1942-1945. The decline in the number of troubled banks can be ascribed primarily to the highly liquid state of bank assets, the absence of deposit outflows, and vigorous business activity. As the war drew to a close and ended, the transfer to peacetime conditions raised questions whether the economy would enter another recession or experience disruptive inflation. Many individuals feared that unemployment, declining income and business failures would ensue. However, inflation rather than deflation ensued. The public had a large volume of liquid assets, there was a tremendous demand for goods, and the immediate problem was one of inadequate production rather than of unemployment.

Effects of the War on the FDIC

The participation by the United States in World War II affected both the FDIC and the state banks it supervised, and some of those effects carried on well past the 1940s. The short-term effects included such things as moving some headquarters personnel to Chicago to vacate Washington office space for the war effort. The FDIC also suffered

the same personnel shortage felt by many government agencies resulting from military enlistments and transfers to defense-oriented programs. A shortage of examiners meant that the FDIC was unable to fulfill its policy of annual bank examinations. Even after the war, government hiring restrictions and rapid growth of the economy led to a shortfall of qualified examiners, and it was not until 1951 that the FDIC again was able to examine all of its banks annually. Another temporary effect of the war effort was the transfer to the FDIC of responsibility for the supervision and examination of about 4,000 federal credit unions, though the FDIC did not insure their deposits. Federal credit unions previously had been supervised by the Farm Credit Administration. In 1948, after six years of FDIC supervision, this responsibility was transferred to the Federal Security Agency. FDIC Chairman Leo Crowley had come to be regarded by President Roosevelt as one of the best administrators, in or out of government, and he accepted numerous wartime responsibilities. While retaining his FDIC post, Crowley held nine separate government positions, including those of Alien Property Custodian and head of the Foreign Economic Administration, the latter a cabinet-level post that included the lendlease program. Thus, all foreign economic dealings, and assets and authorizations totaling more than $40 billion, were administered from Crowley's FDIC office in the Press Building on Fourteenth Street.

A more lasting effect of the war was a rapid decline in bank capital ratios, due primarily to the growth of banks' assets. However, the same process that led to rapid bank expansion - government financing - reduced the riskiness of bank portfolios. By the end of 1944, cash and U.S. government obligations had grown to 79 percent of bank assets. Between 1934 and year-end 1944, the aggregate capital-to-assets ratio of banks had declined from 13.2 percent to 5.9 percent. Despite the decline in capital ratios, bank examiners were not particularly critical of bank behavior because of the quality and liquidity of bank assets.

Post-World War II Developments

The banking industry had emerged from World War II in very liquid condition and was in a favorable position to finance the spending spree that was poised to occur. Yet, many individuals expressed doubts whether banks were up to the task of resuming their traditional lending function. These concerns proved groundless. In 1947 alone, bank lending increased from 16 percent to 25 percent of the industry's assets. Lending subsequently did reach 40 percent of assets in the mid-1950s, and 50 percent in the early 1960s. This resurgence of lending did not produce a concomitant increase in loan losses. Throughout this period, loan losses remained relatively small. Net charge-offs averaged considerably less than one-tenth of 1 percent of outstanding loans during the 1950s. Several factors accounted for the relatively low level of loan losses during the postwar years. First, banking behavior by present standards continued to be very conservative. In addition, the economy remained strong. Recessions were reasonably mild and short. This was a period of general prosperity, with a secularly increasing real GNP and relatively low unemployment.

Bank lending had increased, but banks were still operating within traditional markets, and risks to the soundness of the banking system and to the deposit insurance fund were minimal, even during recessionary periods. Bank failures that did occur often received a great deal of attention, including Congressional hearings in some instances. This concern was reflected in the strict supervisory posture that prevailed during this period, but most bankers were content to accept tight regulation in exchange for the restraints it placed upon competition among banks and with nonbank competitors. During the late 1940s and 1950s there were no more than five bank failures in any single year. However, the low incidence of failures was regarded by some as a sign that the bank regulators were overly strict, operating with policies and practices rooted in the banking crises and economic chaos of the 1930s. In a speech marking the dedication of the headquarters building of the FDIC in 1963, Wright Patman, then-Chairman of the House Banking and Currency Committee, declared:

. . . I think we should have more bank failures. The record of the last several years of almost no bank failures and, finally last year, no bank failure at all, is to me a danger signal that we have gone too far in the direction of bank safety.

Until about 1960, banks continued to operate in this safe, insulated environment. Then banks gradually began to change the way they operated. The Depression experience ceased to be a dominant influence on bank management. The new generation of bankers who came to power in the 1960s abandoned the traditional conservatism that had characterized the industry for many years. Instead, they began to strive for more rapid growth in assets, deposits and income. Intensified competition and higher costs of funds put pressure on interest margins, and greater risks were assumed in order to increase portfolio yields. The trend was particularly pronounced among large banks. These banks also began pressing at the boundaries of allowable activities. They expanded into fields considered by some to involve more than the traditional degree of risk for commercial banks. Banks in general had become more susceptible to the effects of business downturns (as reflected in loan-loss rates) and interest-rate fluctuations. Before the 1970s, banks were not noticeably harmed by the movement toward increased risk-taking. Generally favorable economic conditions enabled many otherwise marginal borrowers to

meet their obligations. With the exception of relatively mild recessions, the economy produced high levels of production, employment and income during most of the period.

There were other changes during the 1960s that had an effect on banking. States began to liberalize branching laws. The use of the bank holding company corporate structure was expanded as an alternative form of multioffice banking and as a means to enter new product markets. With the introduction of the large, negotiable certificate of deposit, banks' reliance on purchased money increased. In addition to the bank regulatory agencies having to monitor these developments, federal legislation gave them additional enforcement responsibilities in the areas of securities disclosure, antitrust and consumer protection. As banking entered the 1970s, it was on a new course that had brought it out of the period of post-war stability and into a period of increasing volatility and change.

Insured-Bank Failures

After 20 insured banks failed in 1942, fewer than 10 banks failed in each of the next 32 years. In 1962, one insured bank failed, but it required no disbursement by the FDIC, the only year in the FDIC's history with no failure-related disbursements. Because most of the banks that failed during the period 1942 to 1970 were small institutions, insurance losses remained low. In just four of these years did losses exceed $1 million, and losses averaged only $366,000 per year.

Financial Operations

The deposit insurance fund continued to grow during the 1940s, surpassing $1 billion at year-end 1946. Because of the highly liquid condition of the banking industry, the legislation passed in the 1930s to reduce risks in many sectors of the economy and the low bank failure rate, many observers felt that a $1-billion fund was sufficient to cover almost any economic contingency. Apparently, Congress also felt that the fund was adequate at that time and legislatively mandated repayment of the original capital subscriptions. The $150 million contributed by the Treasury and the $139 million in capital stock purchased by the Federal Reserve Banks was fully repaid by the end of 1948. Bankers also had voiced concern that the assessment rate was too high. By 1950 the fund had reached a balance of $1.2 billion, despite the repayment of capital completed two years earlier. Assessment income had been growing at a high rate, reflecting the rapid growth in bank deposits during the war and post-war years. Moreover, because of low interest rates during this same period, bank earnings lagged increases in prices and deposit insurance expenses.

The FDIC was reluctant to support a permanent reduction in the basic assessment rate. There still was concern that accumulated earnings would be insufficient to handle the increased rate of bank failures that many thought would occur during the 1950s. This fear was reinforced by the decrease in capitalization of the banking industry because of low earnings and rapid asset expansion since 1940. As a compromise, deposit insurance charges were effectively reduced by the Federal Deposit Insurance Act of 1950. Rather than lowering the basic assessment rate, however, the reduction was accomplished through a rebate system. After deducting operating expenses and insurance losses from gross assessment income, 40 percent was to be retained by the FDIC, with the remainder to be rebated in the form of assessment credits to insured banks. This procedure meant that losses were to be shared by insured banks and the FDIC on a 60/40 basis. This procedure tended to stabilize FDIC earnings despite periods of fluctuating loss experience.

From 1934 to 1949, insured banks had paid an assessment rate of one-twelfth of 1 percent, or 8.3 cents per $100 of assessable deposits. As a result of the 1950 Act, the effective assessment rate fell to 3.7 cents per $100. In 1960, the rebate scheme was modified slightly to adjust for a change in the calculation of an institution's assessable deposits, and the rebate proportion was increased from 60 percent to 66-2/3 percent. From 1950 to 1980, the effective assessment rate stayed in the range of 3.1 cents to 3.9 cents per $100 of assessable deposits, except for a slight blip in 1974 (4.4 cents). Higher insurance losses after 1980 soon eliminated the assessment credits, restoring the effective rate to 8.3 cents

The 1950 Act also required the FDIC to reimburse the Treasury for interest foregone on the initial capital contributions by the Treasury and the Federal Reserve Banks. This requirement was the result of an exchange between FDIC Chairman Maple T. Harl and Senator Paul Douglas of Illinois during hearings on the 1950 Act. The exchange went as follows:
Senator Douglas: ...Mr. Harl, on page 2 [of your prepared statement] you speak of making final payment to the Treasury on August 30, 1948, when you paid the Treasury out in full for the loans [capital] which were advanced. Do I understand that to be your statement?
Mr. Harl: We paid them for the money advanced.
Senator Douglas: Would that include the interest upon the Government loan which was made?
Mr. Harl: It did not. The law provided that there should be no dividend upon the capital stock.

Senator Douglas: In practice, the Government has made an advance to the FDIC which has not been repaid; namely, the interest on the bonds which the Government issued, but for which it was not reimbursed.
. . .
Mr. Harl: ...This Corporation stands ready to reimburse the Government, or anyone else, provided it is legally authorized to do so.
Senator Douglas: You are ready to pay the interest, is that right?
Mr. Harl: If we have an obligation we are ready to pay it.
. . .
Senator Douglas: That is a possible source of revenue that I had not thought of. This brief conversation, which I at first thought was going to be unprofitable, might yield the Government as much as $40,000,000. I first thought it was love's labor lost. It may turn out there was gold in "them there hills."
(U.S., Congress, Senate, Committee on Banking and Currency, Hearings before a subcommittee of the Senate Committee on Banking and Currency on Bills to Amend the Federal Deposit Insurance Act, 81st Cong., 2d sess., January 11, 23 and 30, 1950, pp.27-29)

The amount estimated by Senator Douglas was somewhat low. During 1950 and 1951, the FDIC paid approximately $81 million to the Treasury for the interest foregone on the initial contribution of both the Treasury and the Federal Reserve Banks. An interesting benchmark was passed in 1961 when investment income ($73.9 million) surpassed assessment revenue ($73.4 million) for the first time. This remained so until the late 1980s, when insurance losses had eliminated assessment credits, thus increasing assessment revenue, and depleted the fund's investment portfolio and earnings. With the low insurance-loss experience of the 1950s and 1960s, and despite the implementation of the assessment credit program in 1950, the insurance fund continued to grow, reaching $4.4 billion at the end of 1970. The fund's growth rate trailed that of insured deposits, though, and the reserve ratio declined to 1.25 percent by the end of 1970. There were three increases in the insurance coverage limit during the years 1942 to 1970. Coverage was raised from $5,000 to $10,000 in 1950, to $15,000 in 1966 and to $20,000 in 1969.

CHAPTER 6 A Costly Evolution: 1971 - 1991

The economic environment affecting banks began to change during the 1970s and the pace of change accelerated during the 1980s. Also, the market for financial services became far more competitive as nonbanking companies began to encroach on traditional banking markets and banks sought to enter new product markets. As a result, banking became a riskier and more demanding business than ever before. The ramifications of unforeseen market developments or bad decisions were greatly magnified.

Economic Variables Affecting Deposit Insurance

This chapter documents some major changes in the banking environment that occurred from 1971 to 1991, a period that included record insured-bank failures and insurance losses and ended with the Bank Insurance Fund technically insolvent by $7 billion. The period of remarkable post-World War II stability came to an end in the 1970s.

Foreign exchange-rate volatility

An important change resulted from the movement to a floating exchange-rate system from a fixed-rate system that occurred in 1973. As international trade expanded in the post-World War II era, the maintenance of fixed exchange rates required adjustments to trading relationships and domestic economic policies of trading nations that were not optimal. With the Smithsonian Agreement (Washington, DC, 1971), exchange rates among all of the major currencies of the world were realigned and permitted to float without upper and lower bounds. This development predictably gave rise to considerably greater exchange-rate volatility at a time when world trade was expanding rapidly. Since 1970, there have been periods of relative calm in the exchange rates - for example, 1976 and 1977 - interspersed with periods of substantial volatility, some considerably extended, and periods with volatility varying among currencies. Markets for forwards and futures exchange-rate contracts were developed to permit firms to manage foreign exchange-rate risk more effectively. For example, the Chicago Mercantile Exchange formed the International Money Market in 1972 and began offering the first foreign exchange futures contracts on major currencies. Without well-developed markets for forwards and futures contracts for foreign exchange, this volatility would be less manageable and would significantly lessen foreign trade.

Interest-rate volatility

Interest-rate volatility also increased considerably in the 1970s. Oil embargo shocks in 1973 and 1978 resulted in accelerating inflation and contributed considerably to interest-rate volatility. The Federal Reserve dramatically changed monetary policy in October 1979 by switching from an interest-rate target to a monetary aggregates target, such as nonborrowed reserves, with the objective of reducing inflation. The result of this policy was a highly volatile interest-rate period from October 1979 until late 1982. Interest-rate volatility can give rise to volatility in bank earnings to the extent that banks face gaps between interest-sensitive assets and interest-sensitive liabilities. The causes of this volatility in interest rates have been linked to expectations of changes in future short-term interest rates, fed by the volatility in the rate of inflation and inflation expectations. The yield curve - *i.e.*, the relation between interest rates and maturity - has been volatile and at times has become inverted, such as 1972 through late 1974 and early 1978 through 1982, when the one-year Treasury bond yield was higher than the 10-year yield. This required considerable caution in funding long positions in long-term assets or fixed-rate assets with short-term, variable-rate liabilities. This was a particularly difficult period for FDIC-insured savings banks, which held proportionately more fixed-rate, long-term assets (residential mortgages) than did the typical commercial bank

Economic conditions

Volatility in the 1970s and 1980s also arose from general economic activity. To a considerable extent, the volatility in general economic activity can be traced to real shocks, such as the oil embargoes of the 1970s, wars, dissolution of the Soviet Union, and the fiscal and monetary policies of the major industrialized nations. These shocks caused considerable volatility in commodity prices and real output. The record inflation of the late 1970s was followed by a period of slower inflation, but greater commodity-price volatility. The 1980s also witnessed a surge in the number of newly issued commercial bank charters, which began operations at a time when inexperience was a distinct liability. (George Hanc, "The Banking Crisis of the 1980s and Early 1990s," *FDIC Banking Review* 11, no. 1 (1998), p. 19)

The volatility of prices and general economic activity can have a substantial effect on banking performance, as the experience of the 1980s made clear. The sectoral inflation and subsequent deflation of agricultural prices in the late 1970s and early to mid-1980s were major contributors to the failure of hundreds of agricultural banks. Similarly, the boom and subsequent collapse of oil prices caused significant problems for banks in states whose economies had important energy sectors. The declines in real estate markets in the 1980s and early 1990s caused major problems for many banks. These problems can be traced in part to unanticipated changes in regional economic conditions, as the behavior of real-estate prices departed sharply from past patterns.

Developments in the Banking Industry

The business of banking changed considerably during this period. As noted above, risks increased as interest rates, exchange rates and commodity prices became more volatile and as economic shocks were transmitted more widely *via* the globalization of markets. Meanwhile, competition in the financial marketplace greatly intensified. The traditional intermediation function of banks assumed a smaller role in aggregate economic activity, largely because financial and technological innovations increased the funding options for firms that formerly were restricted to bank loans. Banks were forced to seek new sources of income and to implement untested business strategies, and such experimentation carried inherent risks. Dramatic evidence that banking became riskier is evident in the annual rates of bank failures. Although annual bank failures exceeded single digits only rarely between 1940 and 1980, failure rates rose rapidly thereafter, to a record high of 280 in 1988. A similar picture emerges from the data on FDIC insurance losses relative to insured deposits. Annual insurance losses were quite stable and extremely low, on average, before 1980, at less than half a basis point (0.005 percent) of insured deposits. Losses for the period from 1980 to 1991 averaged nearly 16 basis points (0.16 percent) and were highly variable.

Net loan charge-offs as a percent of average total loans trended upward beginning in the early 1970s and accelerated rapidly in the 1980s. This ratio was 0.34 percent in 1970 and 0.37 percent in 1980 before soaring to a peak of 1.59 percent in 1991. Over the same period, bank stocks substantially underperformed the Standard & Poor's 500 index. The effects of increased competition and innovation are inextricably intertwined. Both played a role in the banking industry's declining share of financial-sector credit market assets since 1971. U.S.-chartered commercial banks held a 37.6-percent share in 1971, but this share declined to 23.2 percent by the end of 1991. Many larger companies found that they could raise money more efficiently by issuing their own commercial paper. In 1971, outstanding commercial paper equaled just 4 percent of banks' commercial and industrial (C&I) loans, but by 1991 this ratio had risen fourfold, to nearly 17 percent. This development had added significance because many of these larger companies had been banks' most creditworthy, "prime" borrowers. During this period, banks also were losing business borrowers to finance companies. In 1971, finance companies' business loans were 15 percent of banks' C&I loans, but by 1991 this ratio had grown to more than 50 percent.

Asset-Backed Securities

The growth of asset-backed securities represents another dimension of the competitive pressures faced by depository institutions. By increasing the liquidity and efficiency of the credit markets, securitization produces a narrowing of the spreads available to traditional lenders such as banks and thrifts. The outstanding example of this process occurred in the mortgage market, where the proportion of consumer mortgages that had been securitized grew from about 8 percent in 1971 to more than 40 percent as of year-end 1991. On the liability side, banks faced increasing competition from many nonbank financial institutions. Foremost among these were the money-market mutual funds (MMMFs), which rose from obscurity in 1975 to prominence by 1981. Because of interest-rate regulations, banks were unable to match the high, market interest rates offered by these instruments. The ratio of MMMF balances to comparable commercial bank deposits (small time and savings deposits) was virtually zero in the mid-1970s, but reached 36 percent by 1981. Despite the elimination by 1983 of most interest-rate controls, MMMFs had established a durable presence. By 1991, the ratio of MMMFs to banks' small time and savings deposits had risen to 39.5 percent. These developments forced changes in the strategies of commercial bankers. Faced with diminished opportunities for C&I lending, banks shifted into real-estate lending.

This new portfolio composition exacerbated the adverse effects on banks of downturns in regional real-estate markets, including the Southwest in the mid-1980s and the Northeast a few years later. This typified other periodic, large-scale movements in and out of particular types of lending, and these portfolio shifts suggested that many banks embarked on a widening search for new profit opportunities in response to the competitive pressures undermining their traditional niche in the financial marketplace. The behavior of banks in the regions and sectors that suffered recessions during the 1980s exhibited some common elements. Recessions occurred in the Midwest in the early 1980s, in the Southwest in the mid-1980s, in the Northeast in the late 1980s and in California in the early 1990s. In the economic expansions that preceded these recessions, banks generally responded aggressively to rising credit demands. Banks that failed generally had assumed greater risks, on average, than those that survived, as measured by the ratios of total loans and commercial real-estate loans to total assets. Banks that

failed generally had not been in a weakened condition, as measured by equity-to-assets ratios, in the years preceding the regional recessions.

Safety-and-Soundness Examination Policy

In 1936, the problems cited most frequently by bank examiners were inadequate capital, excessive insider lending, excessive volume of poor loans, inadequate credit documentation and incompetent management. In a survey 40 years later (1976), these same problems were cited by examiners, along with inadequate liquidity and violations of consumer credit law. Some people recognized, though, that it was becoming increasingly difficult in the 1970s to effect adequate supervision within the confines of policies and procedures designed for the less diversified, less dynamic industry of previous decades. Edward Roddy, who served as the FDIC's Director of Bank Supervision from 1971 until his death in 1975, was credited by many as being particularly aware of the changes that were taking place and the growing inadequacy of existing supervisory policies. It was largely through his efforts that policies were overhauled in the early and mid-1970s, the first substantive changes in several decades. In an important shift in FDIC policy, it was decided that smaller, sound, well-managed banks did not require annual full-scope examinations and that it would be more effective to concentrate examination resources on those banks presenting greater risks to the insurance fund. This concept was furthered in the late 1970s and early 1980s with the expanded use of off-site monitoring systems to identify institutions posing unacceptable risks and to target supervisory resources.

Insured-Bank Failures

. In 1971, the FDIC utilized for the first time powers granted under the 1950 Act to provide "open-bank assistance" to a failing insured bank.

Open-bank assistance

Section 13(c) of the Federal Deposit Insurance Act authorized the FDIC to provide financial assistance to an insured operating bank in danger of closing whenever, in the opinion of the Board of Directors, the continued operation of such a bank is essential to providing adequate banking services to the community. Unity Bank, with deposits of $9.3 million, was established in 1968 as a community venture to serve the black community of the Roxbury-Dorchester area of Boston, Massachusetts. The bank received a loan from the FDIC in the amount of $1.5 million, but Unity did not remain viable and in 1982 was merged into another bank with FDIC assistance.

Failures

Many of the economic and banking developments described above encouraged banks to take greater risks, but the new environment also provided harsh punishment for their mistakes. The *number* of bank failures during the 1970s and early 1980s remained within historical parameters, but the failed-bank assets and insurance losses soon began to escalate beyond historical levels. When Bank of the Commonwealth (Detroit, Michigan) failed in 1972 and United States National Bank (San Diego, California) failed in 1973, they each had total assets greater than $1 billion and were by far the largest FDIC-insured banks to fail. Bank of the Commonwealth received open-bank assistance from the FDIC, in consultation with the Federal Reserve Board and the State of Michigan, because of its essentiality in providing banking services to minority neighborhoods in Detroit. In 1984, Bank of the Commonwealth was acquired by another bank, without FDIC assistance.

Insurance losses for 1973 totaled $67.5 million, nearly double the losses incurred by the FDIC in its previous 39-year history. However, much larger losses were soon to come. From 1982 through 1991, more than 1,400 FDIC-insured banks failed, including 131 that remained open only through FDIC financial assistance. In Texas alone, more than 500 insured banks failed. Total insurance losses exceeded $1 billion in each of these 10 years, topping $6 billion in 1988, 1989 and 1991. The insurance fund had grown to $18.3 billion by year-end 1987, but these crushing losses quickly exhausted the fund. At the end of 1991, the balance of the Bank Insurance Fund, excluding loss reserves, was *negative* $7 billion. A succession and overlapping of regional and sectoral problems combined temporarily to overwhelm the system's ability to absorb losses. There was a sharp increase in the number of new charters issued in the 1980s, and these institutions suffered a disproportionately high rate of failure. Of the 2,800 banks chartered from 1980 to 1990, 16.2 percent had failed by the end of 1994. By comparison, of the banks that already were in existence at the beginning of 1980, just 7.6 percent had failed by year-end 1994. In New England in the early 1990s, mutual savings banks that converted to the stock form of ownership suffered a similar high rate of failure. After conversion, these institutions had large amounts of new cash to invest, just at the time the region was plunging into a recession. Twenty-one percent of stock savings banks failed in the early 1990s, compared to 8 percent of mutual savings banks.

Financial Operations

Insurance coverage

In 1974, deposit insurance coverage was increased from $20,000 to $40,000, and to $100,000 for deposits held by states and political subdivisions. Coverage was increased to $100,000 for IRA and Keogh accounts in 1978. In 1980, despite the reservations of the FDIC, deposit insurance coverage for all accounts was increased to $100,000 by provisions of the Depository Institutions Deregulation and Monetary Control Act. This last increase represented a departure from previous changes in insurance coverage, which generally had been more modest and more or less reflected changes in the price level. The increase to $100,000 was not designed to keep pace with inflation but rather was in recognition that many banks and savings-and-loan associations, facing disintermediation in a high interest-rate climate, had sizable amounts of large certificates of deposit (CDs) outstanding. The new limit facilitated retention of some of these deposits and attraction of new deposits to offset some of the outflows. In 1980, only time accounts with balances in excess of $100,000 were exempt from interest rate ceilings. Disintermediation is the removal of intermediaries or "cutting out the middleman". Instead of going through traditional distribution channels, which had an intermediate (such as a bank or savings and loan), consumers began to place discretionary funds directly into stocks, bonds, mutual funds or other investment (as opposed to savings) vehicles.

Assessments

In 1980, the assessment credit percentage was reduced from 66-2/3 percent to 60 percent, the level that had been in effect from 1950 to 1960. At this time, there also was established a range in which the reserve ratio of the fund was to be maintained. The assessment credit percentage was to be adjusted if the reserve ratio either exceeded 1.40 percent or fell below 1.10 percent. Because of mounting losses, reduced assessment credits were paid in 1981 through 1983, and no assessment credits were paid thereafter. Effective assessment rates generally ranged under 4 basis points during the 1970s. Thereafter, rates grew rapidly as insurance losses mounted throughout the 1980s and early 1990s. When the full statutory rate of one-twelfth of 1 percent (8.3 basis points) proved too low, Congress mandated an increase to 12 basis points in 1990 and gave the FDIC board more flexibility to raise rates. With losses continuing at record levels, rates were increased twice in 1991, first to 19.5 basis points and then to 23 basis points.

FIRREA

Congress enacted the Financial Institution Reform, Recovery, and Enforcement Act (FIRREA) in 1989 in a largely successful effort to resolve the savings and loan crisis of the 1980s. Many provisions of FIRREA drastically affected FDIC operations. The former Federal Deposit Insurance Fund was renamed the Bank Insurance Fund (BIF), and the FDIC assumed responsibility for the new Savings Association Insurance Fund (SAIF), which replaced the defunct Federal Savings and Loan Insurance Fund. A third fund was placed under FDIC management - the FSLIC Resolution Fund - which consisted of the remaining FSLIC receivership assets. The FDIC also was charged with organizing and, initially, managing the new Resolution Trust Corporation (RTC), which was created to resolve failed and failing savings associations and to manage savings association receiverships.

Investment policy

By law, FDIC investments essentially are limited to Treasury securities. Before the mid-1970s, the FDIC assumed a passive role in managing its portfolio, allowing the Treasury to invest FDIC funds in whatever issues the Treasury felt appropriate. About this time, though, the FDIC started to shorten the average maturity of its portfolio and began to achieve a better maturity balance with respect to anticipated bank failures and liquidity needs.

CHAPTER 7 FDIC; A Remarkable Turnaround: 1992 - 1998

In 1991, the commercial banking industry was struggling. A recession in 1990 and early 1991 had trimmed loan demand, losses related primarily to commercial real estate lingered, and the Bank Insurance Fund was insolvent by $7 billion. More than 1,000 commercial banks, with aggregate assets exceeding $500 billion, were on the FDIC's "problem bank" list, many of which were expected to fail. The industry earned a return on assets of just 0.53

percent, well below the profitability benchmark of 1 percent. These hardly were measures of an industry on the verge of an unprecedented run of prosperity, but events already were underway that would reverse banks' fortunes. Short-term interest rates began to plummet in the latter part of 1990. The three-month Treasury bill had an average yield of 7.75 percent in the second quarter of 1990. The yield fell to 4.54 percent by the end of 1991, and it would continue to fall, remaining near 3 percent throughout 1993. Following the 1990-1991 recession, the U.S. economy began an expansion that continued well into 1998.

Developments in the Banking Industry

Performance

Commercial banks earned an industry record $32 billion in 1992, compared to $18 billion in 1991. Their earnings would improve in each of the following five years, reaching $59 billion in 1997. In 1991, one of every nine banks was unprofitable, but by 1997 that figure had fallen to less than one in 20. Part of this earnings improvement was attributable to the overall growth of the industry: total assets were up from $3.4 trillion at the end of 1991 to $5 trillion at year-end 1997. However, banks' average return on assets also improved markedly, surpassing 1 percent in each year from 1993 through 1997, including a record 1.23 percent in 1997. Despite this rapid growth in total assets, the growth of bank capital more than kept pace. The ratio of total equity to assets rose from 6.75 percent in 1991 to 8.33 percent at the end of 1997. Important changes also were underway in the composition of bank earnings. Banks became less reliant on spread-based revenues (*i.e.*, net interest income) and more reliant on noninterest income. Banks and their holding companies diversified into new activities that were less affected by interest-rate swings than were traditional banking products. In 1997, noninterest income was 60 percent of net interest income, up from 49 percent in 1991.

Banks also used this period to improve the quality of their assets. The proportion of noncurrent loans fell from a crippling 3.70 percent in 1991 to under 1 percent in 1997. The level of foreclosed assets also fell dramatically, from $28 billion in 1991 to $4.5 billion by the end of 1997. Banks also maintained a high level of loan-loss reserves. Coupled with the decline in noncurrent loans, banks had nearly $2 in reserves for each dollar of noncurrent loans at year-end 1997, up from 73 cents in 1991. At the end of 1997, the number of institutions on the FDIC's "problem bank" list had fallen to just 71 banks, with total assets of $5 billion.

Consolidation

The number of FDIC-insured commercial banks remained remarkably constant from 1934 to 1988, ranging from 13,000 to 14,500. In 1989, the number of banks fell below 13,000 for the first time and continued to fall, to 9,143 at the end of 1997. Part of this consolidation was attributable to bank holding companies combining their bank subsidiaries, which was facilitated by the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994. This Act, which became fully phased in by June 1997, also enabled interstate combinations between unaffiliated banks. The most dramatic effects have been mergers between some of the nation's largest banking companies. Some concerns were raised about the ability of smaller banks to compete with these enormous financial conglomerates, but there are many reasons to believe that well-managed community banks will continue to prosper independently. Additional concerns were raised about the ability of the FDIC to handle the failure of one of the "megabanks."

FDICIA

The Federal Deposit Insurance Corporation Improvement Act (FDICIA) was enacted in December 1991 as Congress addressed the insolvent Bank Insurance Fund. The Act was comprehensive in nature, covering both insurance funds and their finances as well as supervisory and resolution practices. Its most important provisions are summarized here.

Risk-based premiums

By statute, the FDIC had always charged a flat rate for deposit insurance. FDICIA required the FDIC to have in place by 1994 an assessment system wherein each bank's assessment would be reflective of the risks it posed to its insurance fund. The FDIC had backed such a change and implemented a risk-based premium system on January 1, 1993, a year ahead of schedule. Assessment rate schedules were adopted separately for the BIF and the SAIF. Each schedule was composed of a nine-cell matrix, with rates ranging from 23 cents per $100 of assessable deposits to 31 cents. Institutions were categorized according to a capital subgroup (1, 2 or 3) and a supervisory subgroup (A, B or C). Thus, the best-rated institutions were in cell 1A, and the weakest institutions were in cell 3C. FDICIA set the minimum assessment at 23 basis points until each fund was fully capitalized at 1.25 percent of insured deposits. It required the FDIC to adopt a recapitalization schedule for the BIF to achieve full

capitalization with 15 years. Such a schedule was adopted in 1992. Because nearly half of SAIF assessments were diverted by law to other purposes, that fund was expected to take even longer to become fully capitalized. A capitalization schedule for the SAIF was not required until 1998.

Prompt corrective action

The law required federal regulators to establish five capital zones ranging from well-capitalized to critically undercapitalized that serve as the basis for mandatory prompt corrective active by regulators. Increasingly harsh restrictions apply to institutions that are less than well-capitalized. Institutions whose tangible capital ratio falls below 2 percent are critically undercapitalized and face closure if the situation is not corrected within 90 days. It was expected that by closing institutions before their capital was totally depleted, losses to the deposit insurance funds would be mitigated. Until FDICIA, the FDIC did not have the authority to close a failing insured bank; that power rested with the chartering authority, which was the Comptroller of the Currency or the state.

Least-cost resolution- FDICIA required the FDIC to select the resolution alternative for failing institutions that results in the lowest cost to the insurance fund. Previously, the FDIC could select any resolution alternative if it was less costly than a payout of insured deposits and liquidation of assets. Thus, if two resolution alternatives were less costly than a payout, previously the FDIC could have chosen either method; under FDICIA, the FIDC must choose the least costly of the two. Beginning in the mid-1960s, the FDIC had routinely protected all depositors, when possible, by transferring all deposits of a failed bank to an acquiring institution, thus protecting even uninsured depositors. That policy was no longer an option.

Too big to fail

This concept asserts that certain corporations, and particularly financial institutions, are so large and so interconnected that their failure would be disastrous to the greater economic system, and that they therefore must be supported by government when they face potential failure. Proponents of this theory believe that some institutions are so important that they should become recipients of beneficial financial and economic policies from governments or central banks. Some economists hold that economies of scale in banks and in other businesses are worth preserving, so long as they are well regulated in proportion to their economic clout, and therefore that "too big to fail" status can be acceptable.

The FDIC has the responsibility to rescue an insolvent bank by the least costly method. There is widespread belief among depositors that a loss of depositors and bondholders will be prevented for large banks. This belief is bolstered by the exception in cases of systemic risk. Before FDICIA, the FDIC had the authority under the open-bank assistance provisions of the 1950 Act to determine that a failing institution was so large that its failure could result in a systemic risk to the banking system by undermining public confidence. This authority was used only two times, in 1980 with First Pennsylvania Bank (total assets $8 billion) and in 1984 with Continental Illinois National Bank (total assets $45 billion). Both instances required a finding of essentiality. FDICIA requires that, in situations threatening systemic risk, the FDIC Board, the Board of Governors of the Federal Reserve System and the Secretary of the Treasury, in consultation with the President, must agree that the closure of the insured institution would have a serious effect on economic conditions or financial stability. Any loss to an insurance fund under this exception must be recovered through a special assessment paid by members of that fund. This authority has not yet been used.

Since the full amount of the deposits and debts of "too big to fail" banks are effectively guaranteed by the government, large depositors and investors view investments with these banks as a safer investment than deposits with smaller banks. Therefore, large banks are able to pay lower interest rates to depositors and investors than small banks are obliged to pay. During November 2013, the Moody's credit rating agency reported that it would no longer assume the eight largest U.S. banks would receive government support in the event they faced bankruptcy. However, the GAO reported that politicians and regulators would still face significant pressure to bail out large banks and their creditors in the event of a financial crisis.

Borrowing authority- FDICIA also increased from $5 billion to $30 billion the amount the FDIC is authorized to borrow from the Treasury to cover insurance losses. Any borrowings were to be repaid through deposit insurance assessments. In 1990, the FDIC was authorized to borrow money for working capital from the Federal Financing Bank. Any borrowings were to be repaid by the sale of receivership assets. These provisions were necessary because when an institution fails, the FDIC has large initial expenses - the payment of insured deposits - and relatively slow recovery through the sale of receivership assets. Working capital borrowings, which amounted to about $10 billion at year-ends 1991 and 1992, were repaid in full in 1993.

Depositor Preference

The Omnibus Budget Reconciliation Act of 1993 included provisions that established a uniform order for distributing the assets of failed insured depository institutions. Previously, federal and state laws often set different priorities in terms of the hierarchical order for payment of receivership claims. Under the national depositor preference law, a failed institution's assets are to be distributed in the following order:
The administrative expenses of the receiver;
The claims of all depositors, including the FDIC in the place of insured depositors;
General creditor claims;
Subordinated creditor claims; and
The claims of shareholders

The law was expected to reduce the cost of resolutions and thus conserve the deposit insurance funds.

Insured-Bank Failures

The profitability of the overall banking industry recovered quickly in 1992, but some banks did not survive the travails of the preceding years. One hundred twenty-seven banks failed in 1992, resulting in estimated insurance losses of $3.6 billion. Insurance losses for any given year include estimated losses for institutions that failed during that year as well as adjustments to estimated losses for institutions that failed in previous years. The industry's financial health was evident in the lower numbers of failures and losses in subsequent years. From 41 failures in 1993, the numbers fell to 13, six, five and one in the years 1994 through 1997, respectively, and insurance losses declined proportionately. The low failure experience has continued in 1998. Through the first eight months of the year, just three commercial banks failed, resulting in estimated losses of $33 million.

Financial Operations

The Bank Insurance Fund recovered far more quickly than was anticipated from its insolvency at year-end 1991. With declining insurance losses and substantially higher assessment revenue mandated by FDICIA, the fund balance became positive in 1993 and reached full capitalization in May 1995. At midyear 1995, the fund's balance was $24.7 billion, which represented 1.29 percent of insured deposits. It is important to note that the recovery of the BIF was aided significantly by a reduction in the reserves previously set aside for anticipated failures. Failures projected by the FDIC and the General Accounting Office in the early 1990s did not materialize as the banking industry went on to seven years of record profits. In 1992, 1993 and 1994,
the FDIC recorded *negative* loss provisions totaling $12.8 billion, which increased net income and the fund balance. Much smaller - though still negative - loss provisions were recorded in 1995 through 1997.

BIF assessment rates- With the BIF recapitalized in 1995, the FDIC was able to reduce deposit insurance assessments for BIF members. In recognizing the legislative safeguards recently implemented, the FDIC Board concluded that the insurance losses of the 1980s and early 1990s were atypical of what could be expected in the foreseeable future. The staff determined that an assessment rate of 4 to 5 basis points would have been sufficient to balance revenues and expenses - and capitalize deposit growth - in the period from 1950 to 1980. Interestingly, this was the same exercise undertaken by FDIC staff 60 years earlier, based on the period 1865 to 1934, in recommending an assessment rate when Congress was drafting the Banking Act of 1935. The results were not widely dissimilar. However, the Board also wanted to maintain risk-based pricing, so rates were reduced from a range of 23 to 31 basis points to a range of 4 to 31 basis points, effective June 1, 1995. Because of incentives in the risk-based premium system and improvements in the health of the industry, the vast majority of banks - nearly 92 percent - was in the 1A rate cell and qualified for the lowest rate. The average assessment rate was 4.4 basis points, down from 23.2 basis points before recapitalization of the BIF. Also, by increasing the spread from 8 basis points (23 to 31) to 27 basis points (4 to 31), the Board hoped to provide additional financial incentive to weaker banks to improve their condition. Later in 1995, the Board lowered BIF rates again, to a range of 0 to 27 basis points, effective at the start of 1996. Because of the low level of projected insurance losses and receivership activity, the Board determined that investment earnings would be sufficient to cover the BIF's expenses. To maintain the incentives provided by risk-based pricing, though, it was decided to retain higher rates for banks presenting greater risks to the fund. In 1997, BIF assessment revenues totaled just $25 million, compared to $5.6 billion in 1994.

SAIF assessment rates- At the time the BIF became recapitalized in 1995, the SAIF still was substantially short of the designated reserve ratio of 1.25 percent. On June 30, 1995, the fund balance was $2.6 billion, and its reserve ratio was just 0.36 percent. Therefore, SAIF assessment rates could not be set lower than 23 basis points and there existed a sizable differential between SAIF assessment rates and the new BIF rates. It soon became apparent that this provided sufficient incentive to SAIF members to shift deposits to BIF insurance. Despite

legislative and regulatory prohibitions, some SAIF members succeeded to some extent. Concern arose that if SAIF-assessable deposits continued to shrink, it eventually would not be able to meet its insurance and other financial obligations. Moreover, it was likely to be the stronger institutions that would be successful in shifting deposits, leaving the SAIF with a higher risk profile. Under FIRREA, the FDIC Board had the option of reducing SAIF assessment rates to 18 basis points during the period from January 1, 1994 to December 31, 1997. However, the Board opted to maintain the minimum rate at 23 basis points until the SAIF was fully capitalized.

Congress responded with the Deposit Insurance Funds Act of 1996 (Funds Act). It called for a special assessment - later set by the FDIC at 65.7 basis points - on all SAIF-assessable deposits in order to bring the fund to full capitalization. The special assessment brought in $4.5 billion and raised the fund balance to $8.7 billion. The SAIF faced another significant problem, however. SAIF assessments of up to $793 million annually were diverted to cover interest payments by the Financing Corporation (FICO) on 30-year bonds issued in the 1980s in an effort to end the savings-and-loan crisis. This amounted to nearly half of all SAIF assessments and was the primary reason why the fund's growth lagged behind that of the BIF. Even when fully capitalized, SAIF assessment rates of 12 basis points or more would have been needed to cover expenses and fund FICO interest payments. The Funds Act allocated the FICO expense to all FDIC-insured institutions. Beginning in 1997, BIF members became subject to FICO assessment, though at a lower initial rate than SAIF members. SAIF members' costs were reduced significantly, and beginning in 2000, all insured institutions will pay a *pro rata* share of the FICO expense, expected to be about 2 basis points annually. With the SAIF fully capitalized, the FDIC was able to lower SAIF assessment rates to a range of 0 to 27 basis points, the same as paid by BIF members, effective October 1, 1996.

CHAPTER 8 Issues in Deposit Insurance

Federal deposit insurance was an extremely important factor in restoring public confidence in the banking system in the 1930s. Deposit insurance may play a smaller role in today's relatively stable economic environment, but in periods of adversity or change, deposit insurance gains consequence. As recounted in the 'A Costly Evolution' segment previously, financial markets in the United States and around the world, in many respects, have become and are expected to remain more volatile than in the past. The effects of this volatility on depository institutions may have been masked, to some extent, by the recent favorable environment, with low and stable interest rates and a prolonged economic expansion. As well, the huge returns earned in the stock market in recent years have reduced for many investors the attractiveness of bank deposits and, thereby, the perceived value of deposit insurance. In periods of relative stability as in periods of economic peril, consumers remain quite concerned about deposit insurance. The FDIC constantly receives inquiries from consumers about certain banks' insurance status, and the Division of Compliance and Consumer Affairs recently added an option to determine "Is my bank insured?" on the FDIC's Web site. Consumers also call frequently to determine the amount of insurance coverage on various types of accounts.

Attempts to Reduce Risk

Many banks have reduced the risks that they faced in the past. Interest-rate risk management has improved, banks in general are less dependent on spread-based income, and bank supervisors have implemented new programs that are expected to be more effective in identifying and addressing emerging risks. Only 16 FDIC-insured institutions failed in the period 1995-2005, including 15 BIF members and one SAIF member. There is no evidence, though, that the business cycle has ceased to exist, and these improvements in bank and supervisory practices have yet to be tested in an adverse environment. Perhaps more significantly, some behaviors of the past remain unchanged. As an economic expansion wanes, profit margins narrow, competition for creditworthy borrowers increases, and underwriting standards are compromised in many instances. At the end of 1997, for all FDIC-insured banks and thrifts, insured deposits comprised less than half of total liabilities for the first time. This proportion fell from more than 60 percent earlier in the 1990s to 49.6 percent at year-end 1997. This likely is attributable, in part, to the favorable environment. In a choppy or adverse economic climate, bank deposits in general, and insured deposits in particular, are likely to gain favor. It also has been the FDIC's experience that when an insured institution encounters difficulties, uninsured depositors quickly seek protection. This can be accomplished in many ways, such as by withdrawing uninsured deposits or by obtaining or increasing loans against which to offset uninsured deposit claims in the event of a failure. Overall, the federal deposit insurance program has served the nation well. However, a number of deposit insurance issues currently face the FDIC, the Congress and the banking industry. The FDIC sponsored a symposium on deposit insurance on January 29, 1998, in order to facilitate a discussion of the role and nature of deposit insurance in the current financial services environment. The symposium addressed the issues related to deposit insurance and financial modernization, in light of the recent rapid pace of banking evolution and the prospect of newly permissible activities for banking organizations; the various deposit insurance reform proposals that would curtail the role of the federal government in protecting depositors; and the right balance between the pursuit of safety and soundness and the need to allow banks to compete and evolve. Some current issues are summarized below.

The Year 2000 Date Change

Although it seems like ancient history now, in the 1990's one of the more immediate deposit insurance issues involved the Year 2000 date change. Attention was focused on the potential for computer systems to encounter problems handling the date change into the next century. Many older computer applications stored the year as a two-digit number and, unless corrected, these programs are likely to interpret January 1, 2000, as January 1, 1900. The financial-services industry was viewed as particularly vulnerable to this problem. In addition to making certain their own systems were "Y2K-compliant," bank regulators incorporated Y2K standards into the bank examination process. Banks not making adequate progress in evaluating, fixing and testing their systems were subject to regulatory sanctions. Vendors providing information processing and services to banks also were subject to these requirements. The FDIC expected some number of "technological" bank failures to occur shortly before or after the Year 2000 date change. The actual number of Y2K failures was impossible to predict, however. Because of the uncertainties, the FDIC and the other federal banking agencies were be prepared if the problems and failures became widespread. In addition to other Y2K initiatives, the FDIC established a Failed Financial Institutions Y2K Action Plan. The problem presented some unprecedented challenges. At the end of the 20th Century, banking was much more interconnected than it was the last time a major crisis was faced. This meant, more than ever, that regional problems would not be as typical. With Y2K, a failure in North Carolina could impact institutions in Idaho in a way that would have been unthinkable in previous decades.

As an example of the potential problems identified by the group, the traditional methods used to verify deposit records would be complicated if a failed bank's computer systems are inoperable or unreliable. A critical need in this contingency planning process was to identify all people within the FDIC with experience in handling failed institutions because, with the decline in failures in the decade of the '90's,, many former resolution specialists had moved to other positions. To be prepared for a worst-case Y2K scenario, the group identified other FDIC employees with applicable experience, personnel at the other federal banking agencies and contractors.

Consolidation and Bank Failures

The five largest banking company mergers in U.S. history all were announced or completed in 1998. The largest of these - Travelers Group and Citicorp - resulted in a company with total assets of approximately $700 billion, more than double the assets of the largest U.S. banking company at the end of 1997. The combination of NationsBank and BankAmerica resulted in a company with total assets of approximately $525 billion. These and other large, complex financial conglomerates present new challenges to the FDIC and other bank regulators. The consolidation of banks serving different product and geographic markets can diversify risk and decrease earnings volatility, thereby decreasing the likelihood of failure. Regional recessions and sectoral downturns contributed to many of the bank and thrift failures in the late 1980s and early 1990s. Many of the institutions that failed or were troubled tended to have either geographic or product concentrations. Broader diversification of risk through mergers of institutions serving different markets can moderate the effects of economic downturns on these institutions. Consolidation of banking organizations also may be able to reduce duplicative back-office and other administrative costs, although the actual value of these cost savings remains uncertain.

The resources and broader array of activities of these banks should enable them to compete more effectively in international markets. However, no banking organization is immune to failure. Certainly, the deposit insurance funds face larger potential losses from the failure of a single large, consolidated institution. Insurance is based on the concept of diversifying risk. If an institution gets too large relative to the industry as a whole, it becomes increasingly difficult to diversify risk. Larger institutions also are more complex and tend to be involved in more nontraditional activities. Large banks pose more challenges when they fail, and the failure of a very large bank has the potential for creating systemic risk, although measures enacted in FDICIA, though as yet untested, were designed to improve the ability of the government to handle situations involving systemic risk. The unprecedented failures of a number of very large financial institutions simultaneously would be more problematic, but it is questionable whether it would be appropriate to maintain insurance funds that are large enough to address an absolute worst-case scenario.

Effective supervisory oversight remains the regulators' most important tool. The recent implementation of risk-focused examinations by the federal banking agencies and the programs already in place for coordinated oversight of large, complex institutions provide a strong foundation for addressing the challenges of industry consolidation. Regulators ensure that proper controls and practices are in place and assess management's ability to identify measure, monitor and control risk within an institution. Going forward, the agencies will determine whether examiners needed additional training to address new activities and whether supervisory programs needed to be modified. (Testimony of Andrew C. Hove, Jr., Acting Chairman, Federal Deposit Insurance Corporation, on Mergers in the Financial Services Industry before the Committee on Banking and Financial Services, United States House of Representatives, April 29, 1998)

Merger of the Insurance Funds

The Deposit Insurance Funds Act of 1996 contained provisions to merge the BIF and the SAIF, effective January 1, 1999. However, the merger could become effective only if there were no insured savings associations in existence on that date. This condition apparently was included to force consideration of bank and thrift charter issues and the perceived unfair advantages of the thrift charter. Thus, Congress recognized the desirability of merging the two deposit insurance funds, but it tied the merger to largely unrelated issues. Arguments against a merger of the funds emanated primarily from bankers who were opposed to exposing their insurance fund to a repeat of the thrift losses of the 1980s.

The FDIC consistently supported a merger of the two insurance funds. The FDIC argued that the SAIF insured far fewer and more geographically concentrated, institutions than did the BIF and consequently faced greater long-term structural risks. A combined BIF and SAIF would have a larger membership and a broader distribution of geographic and product risks and would be stronger than either fund alone. In 1998, both funds were fully capitalized and their members were healthy and profitable, and the BIF and SAIF reserve ratios were very close and are were expected to remain so in the near future. That meant that a merger of the funds at that time would not

result in a material dilution of either. (Testimony of Donna Tanoue, Chairman, Federal Deposit Insurance Corporation, on Financial Modernization before the Committee on Banking, Housing and Urban Affairs, United States Senate, June 25, 1998)

The FDIC was required to set assessment rates independently for each of the insurance funds. At the time, the assessment rate schedules for the two funds were identical. However, the funds' memberships had quite different risk profiles, and it was likely that rates would differ at some time in the future. Before the capitalization of the SAIF in 1996, the FDIC had experience with differing rates for BIF- and SAIF-assessable deposits. The result was the shifting of deposits between BIF- and SAIF-insured institutions. Such market distortions had an economic cost as institutions devoted resources to countering artificial statutory distinctions. As well, the maintenance of two insurance funds resulted in additional administrative costs to the FDIC and to the insured institutions that held both BIF- and SAIF-insured deposits, which were tracked, reported and assessed separately.

FDIRA

In February, 2006, the Federal Deposit Insurance Reform Act of 2005 was signed into law. The FDIRA contained technical and conforming changes to implement deposit insurance reform, as well as a number of study and survey requirements. Among the highlights of this law was merging the Bank Insurance Fund (BIF) and the Savings Association Insurance Fund (SAIF) into a new fund, the **Deposit Insurance Fund** (DIF). This change was made effective March 31, 2006. The amount each institution was assessed for the fund was based both on the balance of insured deposits as well as on the degree of risk the institution posed to the insurance fund. A March 2008 memorandum to the FDIC Board of Directors showed a 2007 year-end Deposit Insurance Fund balance of about $52.4 billion. The FDIC’s Deposit Insurance Fund recovered from the Financial Crisis of 2008. Through elevated assessments and recapturing reserves, the fund recapitalized ahead of schedule. The DIF grew to $83.2 billion in 2016. Assessment income was $2.7 billion, which included temporary assessment surcharges on large banks. Operating expenses of $437 million and unrealized losses on available-for-sale securities of $317 million partially offset the increase in the fund balance. Cumulatively the DIF balance has risen by almost $104.1 billion from its negative $20.9 billion low in the third quarter of 2009. Banks, not taxpayers, were entirely responsible for covering all of the FDIC’s expenses, including recapitalization of the fund. In fact, banks have paid over $155 billion in assessments since the inception of the fund, ensuring that no one has ever lost a penny of an insured deposit.

Definition of the Assessment Base

Assessment rates are set semiannually, and institutions pay assessments at the end of each quarter. The deposit base against which assessments are charged can be defined simply as total domestic deposits, less a downward adjustment for "float." Since float is more applicable to transaction accounts than to time and savings accounts, commercial banks typically have a larger float adjustment than do thrifts. The float adjustment, which is performed by the FDIC rather than reported by insured institutions, is quite complex. Also, because the assessment base is derived from total domestic deposits, institutions pay assessments on deposits in accounts that exceed the insurance coverage limit, currently $250,000.

The deposit insurance assessment base—average consolidated total assets minus average tangible equity—increased by 1.1 percent in the fourth quarter and by 3.0 percent over 12 months. Total estimated insured deposits increased by 0.8 percent in the fourth quarter of 2017 and by 3.5 percent year-over-year. The DIF's reserve ratio (the fund balance as a percent of estimated insured deposits) rose to 1.30 percent on December 31, 2017, from 1.28 percent at September 30, 2017, and 1.20 percent four quarters ago. The December 31, 2017, reserve ratio is the highest for the DIF since December 31, 2004, when the reserve ratio was 1.31 percent. By law, the reserve ratio must reach a minimum of 1.35 percent by September 30, 2020. The law also requires that, in setting assessments, the FDIC offset the effect of the increase in the reserve ratio from 1.15 to 1.35 percent on banks with less than $10 billion in assets. To satisfy these requirements, large banks are subject to a temporary surcharge of 4.5 basis points of their assessment base, after making certain adjustments.34 Surcharges began in the third quarter of 2016 and will continue through the quarter in which the reserve ratio first meets or exceeds 1.35 percent. If, however, the reserve ratio has not reached 1.35 percent by the end of 2018, large banks will pay a shortfall assessment in early 2019 to close the gap. Small banks will receive credits to offset the portion of their assessments that help to raise the reserve ratio from 1.15 percent to 1.35 percent. When the reserve ratio is at or above 1.38 percent, the FDIC will automatically apply a small bank’s credits to reduce its regular assessment up to the entire amount of the assessment.

Optimal Size of the Insurance Fund

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 provides that a minimum Designated Reserve Ratio (DRR) of 1.35 percent of estimated insured deposits or the comparable percentage of the new assessment base, average consolidated total assets minus average tangible equity. The FDIC Board has the authority to raise either fund's DRR for a calendar year if the Board foresees a significant risk of loss. The Act required the Board to set assessment rates at a level that maintains the reserve ratio at the DRR. If the ratio fell below the DRR and remains there for more than one year, assessment rates were to be set at a minimum of 23 basis points until the fund recovered. If the BIF reserve ratio exceeded the DRR, there were provisions to refund assessments to the best-rated banks. There were no refund provisions for the SAIF. Assessment refunds were not possible because the best-rated banks were not paying assessments. There were two related concerns. First, should the law have been modified to permit refunds of amounts above the DRR regardless of assessments paid? Second, was 1.25 percent the appropriate target for the size of the fund?

Refunds- If the refund law were liberalized, the result could be a "pay-as-you go" insurance system. This would permit rates to fluctuate widely during periods of adversity, and banks would be forced to pay significantly higher rates at times when many could least afford it. FDIC staff determined that assessment rates as high as 62 basis points would have been required during the 1980s if such a policy had been in effect. If there were some cushion in the fund above the DRR, assessment-rate increases could be forestalled or lessened when a downturn occurs. Rate increases also could be forestalled or lessened if the FDIC had more flexibility in setting rates when the reserve ratio falls below 1.25 percent.

Reserve ratio- In 1980, legislation established 1.25 percent as the midpoint of the range in which the reserve ratio was to be maintained. If the ratio surpassed 1.40 percent, refunds were required; and if the ratio fell below 1.10 percent, additional assessments were required. The 1996 Act eliminated the range and set the specific target at 1.25 percent. This topic has engendered much discussion - and disagreement - among regulators, bankers and analysts. The issue is at the heart of proposals to reform deposit insurance, both by those who wish fundamental changes and those who wish more modest improvements. Recent FDIC research found that in periods of very high losses, with assessment rates at 23 basis points, there is only a small chance of the BIF becoming insolvent. However, the reserve ratio is likely to fall well below the statutory minimum. It also was determined that increasing the minimum reserve ratio (to 1.50 percent, for example) would not permit substantially lower assessment rates in these circumstances. (Kevin P. Sheehan, "Capitalization of the Bank Insurance Fund," *FDIC Working Paper 98-1*, Federal Deposit Insurance Corporation, Division of Research and Statistics (1998), pp. 29-31)

The paper cautions that the research was based on the BIF's historical loss experience and that there is no guaranty that future banking crises will mirror historical events, given industry consolidation and other developments. If the industry were to encounter severe problems, it may be preferable to allow a deficient insurance fund to recapitalize more slowly and with lower assessment rates than are possible under current law.

TROUBLED ASSET RELIEF PROGRAM

On October 3, 2008, the Emergency Economic Stabilization Act was signed into law. The act established the Office of Financial Stability (OFS) within the Department of the Treasury (Treasury) and authorized the Troubled Asset Relief Program (TARP). Under the law, every 60 days, the U.S. Comptroller General was required to report on a variety of areas associated with oversight of TARP. The report reviewed (1) the activities undertaken through TARP as of November 25, 2008; (2) the structure of OFS, its use of contractors, and its system of internal controls; and (3) indicators of TARP's performance.

Steps Taken

The U.S. Treasury took a number of steps to stabilize U.S. financial markets and the banking system, including injecting billions of dollars in financial institutions. Through the capital purchase program (CPP)-a preferred stock and warrant purchase program-Treasury provided more than $150 billion in capital to 52 institutions as of November 25, 2008. As a part of this process, Treasury had to address a number of critical issues, including determining how it would ensure that CPP was achieving its intended goals and monitoring compliance with limitations on executive compensation and dividend payments. It could not be determined whether the program was having the intended effect on credit and financial markets. Moreover, given that U.S. regulators as well as foreign governments were continuing to take a variety of actions aimed at stabilizing markets and the economy, separately evaluating the impact of Treasury's efforts under TARP was difficult.

Treasury Strategies to Mitigate Mortgage Foreclosures

Having decided against large purchases of troubled mortgage assets under TARP, Treasury stated that the agency was considering other ways to meet Congress' expectation that Treasury would work with lenders "to achieve aggressive loan modification standards" to mitigate foreclosures. OFS established and hired a chief for the Office of the Chief of Homeownership Preservation within OFS. They stated that the OFS was working with other federal agencies, including FDIC, HUD, and FHFA, to explore alternatives to help homeowners under TARP. As OFS reviewed foreclosure mitigation program options, it considered a number of factors, including the cost of the program, the extent to which the program minimized the recidivism of borrowers helped out of default, and the number of homeowners the program helped or was projected to help remain in their homes. A senior OFS official stated that the agency had considered loan modification strategies such as the program FDIC developed to convert nonperforming mortgages owned or serviced by IndyMac Federal Bank into affordable loans. Possible loan modification measures under such programs include interest rate reductions, extended loan terms, and deferred principal.

Sorry, I Cannot Pay

A Wall Street Journal story of 12/03/08 asked what you do if you have spent your career encouraging mortgage loans to people who cannot repay them. This question was aimed at the creators of the 2008 mortgage mess. The time had come to pay the piper. At a hearing of the Financial Services Committee, FDIC Chair Sheila Bair outlined a plan to prevent an estimated 1.5 million foreclosures by the end of 2009. The idea was to modify more than two million loans at an estimated cost to taxpayers of $24 billion. The article observes that the real-world evidence suggests it will be far more difficult and expensive.
The live-fire test had been going on at failed lender IndyMac Bank since August. IndyMac hurt itself with sloppy underwriting and then was wounded further when Senator Charles Schumer released letters warning that "the bank could face a failure." A subsequent wave of withdrawals killed IndyMac, and the FDIC took over. The FDIC soon launched a program to modify IndyMac's troubled mortgages, and this was the basis for what Ms. Bair wanted to do nationwide.

Marketwatch.com reported on the FDIC's experience at IndyMac as well as industry-wide data from Lender Processing Services (LPS), which manages payments for much of the banking industry. It turned out that the FDIC was moving very slowly in modifying loans, but perhaps not slowly enough, because of the likelihood of further defaults. Three months into the IndyMac experiment, the FDIC modified 5,400 delinquent loans. Even the modified monthly payments could consume up to 38% of borrowers' pretax income, and many failures were expected. The FDIC used a re-default rate of 40% in its models but believed the actual rate would be lower. LPS said more than 50% of loans typically go delinquent again after modification.

To roll out its plan nationwide, the FDIC wanted to offer private loan servicers a new incentive to modify troubled loans. The private firms would do the same thing the feds had been doing at IndyMac, except they would move the monthly payment down to 31% of pretax income, instead of 38%. The FDIC would pay servicers $1,000 for every loan they modify, and taxpayers would share the losses if loans re-default. To get to 31%, lenders could offer borrowers lower rates, longer terms or even "principal forbearance." This meant that part of the original loan would be converted to an interest rate of zero, and it would not have to be repaid until the home was sold or refinanced -- or the loan matured. In other words, the borrower would get lower payments but may have a problem again later if home values did not rise and the mortgagee needed to sell. Other modifications might have created a lower interest rate that increased over time, again squeezing borrowers at some future date. The article goes on to observe that this sounded like "subprime" loans.

Under the FDIC plan, a borrower would have to stay current for at least six months under the modified terms to make sure that lenders were not just dumping their losers on taxpayers. Well, not all of their losers anyway. The FDIC was still assuming a 33% re-default rate, even at the lower debt-to-income ratio. All of this is why the White House estimated Ms. Bair's plan would cost as much as $70 billion -- not $24 billion.

Some (those who were still paying the rent or mortgage on time) asked why anybody who borrowed or lent above the payment maximum of 33% of income threshold should receive assistance from taxpayers. Others might wonder how lenders would know what a borrowers' income is in order to set the new ratio. False or undocumented income was the reason many of these loans failed the first time. At IndyMac, the feds were checking reported incomes against IRS data, but private lenders who participated in the new program were to have more flexibility in "verifying" income. Such 'flexibility' lead to the Great Mortgage Market Meltdown. The article observes that this was another uncharted voyage into the land of taxpayer risk, and for little economic gain. It was hoped that news of the FDIC program did not encourage more people to stop paying their mortgages as they awaited rescue from the government.

Insurers Adopt Thrift Holding Company Structure

On November 14, 2008, the deadline for financial institutions to file an application for the Department of the Treasury's Capital Purchase Program (the "CaPP"), as authorized under the Emergency Economic Stabilization Act of 2008 (EESA), four large insurance companies announced proposed acquisitions of distressed thrifts. Hartford Financial Services Group acquired Federal Trust Corporation, which had been ordered by the Office of Thrift Supervision (the "OTS") to find a buyer. Hartford agreed that it would inject a significant amount of capital into the thrift. In addition, Genworth Financial agreed in principle to acquire Inter Savings Bank while Lincoln National Corp. acquired Newton County Savings Bank. Similarly, Aegon NV's U.S. subsidiary, Transamerica Corp., agreed to acquire Suburban Federal Savings and Loan but did not complete the deal. Each of these insurers filed an application to participate in the CaPP.

Eligible for FDIC Liquidity Guarantee

As thrift holding companies, insurance companies became eligible to apply to receive capital infusions under the CaPP and also to participate in the FDIC's Temporary Liquidity Guarantee Program (the "TLGP"). By acquiring a thrift institution and filing an application to become a thrift holding company, these insurance companies became "eligible institutions" under the TLGP. The TLGP was open to FDIC-insured depository institutions (banks and thrifts), U.S. bank holding companies (BHCs), U.S. financial holding companies, and U.S. thrift holding companies that engaged in activities that were permissible for financial holding companies under Section 4(k) of the Bank Holding Company Act (which excludes primarily commercial activities). Affiliates of insured depository institutions could also participate, upon application to, and acceptance by, the FDIC in consultation with the institution's primary federal banking regulator.

The TLGP consisted of two basic components: a temporary guarantee of newly issued senior unsecured debt (the "Debt Guarantee Program") and a temporary unlimited guarantee of funds in noninterest-bearing transaction accounts at FDIC-insured institutions (the "Transaction Account Guarantee Program"). Under the Debt Guarantee Program, the FDIC guaranteed senior unsecured debt newly issued by an eligible institution. The maximum guaranteed amount was 125 percent of the par or face value of senior unsecured debt outstanding as of September 30, 2008 that was scheduled to mature by June 30, 2009. The guarantee expired on December 31, 2012, at which time almost all debt issued under the program had matured. Under the Transaction Account Guarantee Program, the FDIC provided an unlimited guarantee until December 31, 2009 of all funds, regardless of amount, held in non-interest bearing transaction accounts. Both guarantees initially were automatic; however, eligible institutions were required to notify the FDIC by December 5, 2008 whether they wished to opt out of the programs. All commonly controlled institutions had to make the same decision. By choosing to remain in the programs, participants, including the newly-eligible insurance companies, were able to take advantage of the guarantees until the programs terminated, subject to payment of the applicable fees to the FDIC in exchange for the coverage.

In addition, through the CaPP, in light of their new status as thrift holding companies, insurers were eligible to apply to receive infusions of capital from Treasury equal to 1% to 3% of their risk-weighted assets. To qualify for the CaPP, an institution had to be an FDIC-insured depository institution which included U.S. banks and savings associations not controlled by a BHC or thrift holding company, U.S. BHCs and U.S. thrift holding companies that were engaged predominately in Section 4(k) activities under the Bank Holding Company Act (BHCA), or whose depository institution subsidiaries were the subject of an application under Section 4(c)(8) of the BHCA. These capital injections took the form of shares of preferred stock and warrants to purchase common stock. In connection with such infusions, the insurers also were subject to the executive compensation and other limitations associated with the CaPP. For insurance companies, becoming a thrift holding company, even in order to access the EESA programs, could have certain potentially negative consequences that needed to be considered. Conversion subjected the insurers and their non-thrift subsidiaries to regulation by the OTS, and limited the activities in which the insurers could participate. Moreover, inter-affiliate transactions were constrained under applicable banking law, under a different and more rigorous regime than inter-affiliate transactions under applicable insurance law. As a result of their holding company status, the insurance companies and their non-thrift insurance subsidiaries were subject to dual regulation by the OTS and state insurance commissioners.

Financial Holding Companies

Even prior to these decisions to convert to thrift holding company structure, several other insurance companies were already members of organizations that were financial holding companies, subject to federal regulation. Financial holding companies are a type of BHC that, in addition to the activities permitted for BHCs, can engage,

through their affiliates, in certain enumerated financial activities, including insurance. In addition, many insurance companies already hold savings and loans as subsidiaries, again, subjecting them to additional regulation. Considering this, there should be considerable experience with this dual regulation and it is unlikely to raise significant conflicts. The decisions by insurance companies to adopt thrift holding company structures in order to become eligible for federal assistance follows the determination of several other companies to adopt BHC structures for the same or similar purposes.

The federal bailout of American International Group and the conversion of Goldman Sachs and Morgan Stanley (each of which have insurance company subsidiaries) to BHCs expanded the number of insurance company organizations subject to the consequent regulation by a federal regulator, such as the OTS or the Federal Reserve. Although there was no direct regulation of the insurance operations of such institutions, exposure to these regulators may ease concerns over federal oversight of insurance in place of traditional state insurance regulation. Familiarity with federal regulation also may strengthen calls for a consolidated form of federal insurance regulation. In addition to centralized information-sharing, such proposals included the issuance of optional federal charters to insurers. Generally, insurance industry trade associations representing large multi-state insurance companies favored such an approach, although state insurance regulators, concerned that a federal regulator would not be in a position to monitor consumer protection in a targeted fashion, opposed such suggestions. Thus, although regulation by federal bank regulators will not resolve the efficacy of uniform insurance regulation across state boundaries, proponents are likely to seize upon the economic and financial factors underlying these conversions to federally regulated status and any positive experience under such regimes as additional support for consolidated regulation

Bank Practices and Supervisory Ratings

In the discussion of risk-based premiums mentioned previously, it was stated that institutions are categorized in the rate-cell matrix according to their capital subgroup and their supervisory subgroup. The former is determined semiannually, using the most recent Report of Condition. The latter is determined primarily from an institution's most recent examination rating, although other factors sometimes are considered. As required by law, institutions generally are examined every 12 to 18 months. Those undertaking unacceptable risks, therefore, would not be penalized by the assessment system unless and until the risk-taking resulted in a supervisory rating downgrade. The FDIC is concerned about eroding underwriting standards and other such practices that often appear late in a business cycle in an effort to sustain high profits. However, this has not yet been reflected in any appreciable movement of institutions out the best-rated, 1A cell of the assessment rate matrix. This may be due, in part, to the unavoidable lag in the examination process.

Rebuilding the DIF, Resolving Failed Banks and FDIC Resources

Under a long-term plan based on the Dodd-Frank Act requirements to rebuild the DIF, the FDIC has had a steady increase in the year-end fund balance from 2011 through 2016. Recently, lower than estimated losses for past bank failures, together with assessment income, have contributed to the increase in the fund balance to $83.2 billion as of December 31, 2016. The fund is on track to reach a reserve ratio (the ratio of the DIF fund balance to estimated insured deposits) of 1.35 percent by September 2020, as mandated by statute. The reserve ratio was 1.2 percent as of year-end 2016. Bank failures in 2016 totaled 5, down dramatically from a peak of 157 in 2010, while the number of banks on the problem bank list fell to 123 at the end of 2016 from a high of 888 in March 2011. The FDIC continues to manage receiverships, examine problem institutions, and implement provisions of the Dodd-Frank Act. During 2016, the FDIC continued to successfully use various resolution strategies to protect insured depositors of failed institutions at the least cost to the DIF. The FDIC actively marketed failing institutions and sold a large majority to other financial institutions. These strategies protected insured depositors and preserved banking relationships in many communities, providing depositors and customers with uninterrupted access to essential banking services.

Chart FDIC Key Statistics

Estimated Insured Deposits and the Deposit Insurance Fund, December 31, 1934, through September 30, 2016[1]

		Deposits in Insured Banks ($ Millions)				Insurance Fund as a Percentage of-	
Year[4]	Insurance Coverage	Total Domestic Deposits	Estimated Insured Deposits [2]	Percentage of Insured Deposits	Deposit Insurance Fund	Total Domestic Deposits	Estimated Insured Deposits
2016	$250,000	$11,505,053	$6,822,885	59.3	80,704.0	0.70	1.18
2015	250,000	10,950,090	6,528,125	59.6	72,600.2	0.66	1.11
2014	250,000	10,408,068	6,203,524	59.6	62,780.2	0.60	1.01
2013	250,000	9,825,398	6,010,854	61.2	47,190.8	0.48	0.79
2012	250,000	9,474,585	7,405,043	78.2	32,957.8	0.35	0.45
2011	250,000	8,782,134	6,973,468	79.4	11,826.5	0.13	0.17
2010	250,000	7,887,733	6,301,528	79.9	(7,352.2)	(0.09)	(0.12)
2009	250,000	7,705,353	5,407,773	70.2	(20,861.8)	(0.27)	(0.39)
2008	100,000	7,505,408	4,750,783	63.3	17,276.3	0.23	0.36
2007	100,000	6,881,843	4,241,307	61.6	51,754.4	0.75	1.22
2006	100,000	6,595,357	4,151,966	63.0	50,165.3	0.76	1.21
2005	100,000	6,168,146	3,890,911	63.1	48,596.6	0.79	1.25
2004	100,000	5,686,680	3,623,713	63.7	47,506.8	0.84	1.31
2003	100,000	5,182,016	3,451,117	66.6	46,022.3	0.89	1.33
2002	100,000	4,857,327	3,387,799	69.7	43,797.0	0.90	1.29
2001	100,000	4,481,888	3,210,727	71.6	41,373.8	0.92	1.29
2000	100,000	4,149,355	3,054,360	73.6	41,733.8	1.01	1.37
1999	100,000	3,802,744	2,868,881	75.4	39,694.9	1.04	1.38
1998	100,000	3,747,809	2,850,227	76.1	39,452.1	1.05	1.38
1997	100,000	3,507,493	2,746,006	78.3	37,660.8	1.07	1.37
1996	100,000	3,350,856	2,690,537	80.3	35,742.8	1.07	1.33
1995	100,000	3,318,513	2,663,560	80.3	28,811.5	0.87	1.08
1994	100,000	3,184,636	2,588,686	81.3	23,784.5	0.75	0.92
1993	100,000	3,220,109	2,602,043	80.8	14,277.3	0.44	0.55
1992	100,000	3,273,180	2,675,081	81.7	178.4	0.01	0.01
1991	100,000	3,330,738	2,734,073	82.1	(6,934.0)	(0.21)	(0.25)
1990	100,000	3,415,668	2,759,640	80.8	4,062.7	0.12	0.15
1989	100,000	3,414,066	2,756,757	80.7	13,209.5	0.39	0.48
1988	100,000	2,330,768	1,750,259	75.1	14,061.1	0.60	0.80
1987	100,000	2,201,549	1,658,802	75.3	18,301.8	0.83	1.10
1986	100,000	2,167,596	1,634,302	75.4	18,253.3	0.84	1.12
1985	100,000	1,974,512	1,503,393	76.1	17,956.9	0.91	1.19
1984	100,000	1,806,520	1,389,874	76.9	16,529.4	0.92	1.19
1983	100,000	1,690,576	1,268,332	75.0	15,429.1	0.91	1.22
1982	100,000	1,544,697	1,134,221	73.4	13,770.9	0.89	1.21
1981	100,000	1,409,322	988,898	70.2	12,246.1	0.87	1.24
1980	100,000	1,324,463	948,717	71.6	11,019.5	0.83	1.16

1979	40,000	1,226,943	808,555	65.9	9,792.7	0.80	1.21
1978	40,000	1,145,835	760,706	66.4	8,796.0	0.77	1.16
1977	40,000	1,050,435	692,533	65.9	7,992.8	0.76	1.15
1976	40,000	941,923	628,263	66.7	7,268.8	0.77	1.16
1975	40,000	875,985	569,101	65.0	6,716.0	0.77	1.18
1974	40,000	833,277	520,309	62.5	6,124.2	0.73	1.18
1973	20,000	766,509	465,600	60.7	5,615.3	0.73	1.21
1972	20,000	697,480	419,756	60.2	5,158.7	0.74	1.23
1971	20,000	610,685	374,568	61.3	4,739.9	0.78	1.27
1970	20,000	545,198	349,581	64.1	4,379.6	0.80	1.25
1969	20,000	495,858	313,085	63.1	4,051.1	0.82	1.29
1968	15,000	491,513	296,701	60.2	3,749.2	0.76	1.26
1967	15,000	448,709	261,149	58.2	3,485.5	0.78	1.33
1966	15,000	401,096	234,150	58.4	3,252.0	0.81	1.39
1965	10,000	377,400	209,690	55.6	3,036.3	0.80	1.45
1964	10,000	348,981	191,787	55.0	2,844.7	0.82	1.48
1963	10,000	313,304	177,381	56.6	2,667.9	0.85	1.50
1962	10,000	297,548	170,210	57.2	2,502.0	0.84	1.47
1961	10,000	281,304	160,309	57.0	2,353.8	0.84	1.47
1960	10,000	260,495	149,684	57.5	2,222.2	0.85	1.48
1959	10,000	247,589	142,131	57.4	2,089.8	0.84	1.47
1958	10,000	242,445	137,698	56.8	1,965.4	0.81	1.43
1957	10,000	225,507	127,055	56.3	1,850.5	0.82	1.46
1956	10,000	219,393	121,008	55.2	1,742.1	0.79	1.44
1955	10,000	212,226	116,380	54.8	1,639.6	0.77	1.41
1954	10,000	203,195	110,973	54.6	1,542.7	0.76	1.39
1953	10,000	193,466	105,610	54.6	1,450.7	0.75	1.37
1952	10,000	188,142	101,841	54.1	1,363.5	0.72	1.34
1951	10,000	178,540	96,713	54.2	1,282.2	0.72	1.33
1950	10,000	167,818	91,359	54.4	1,243.9	0.74	1.36
1949	5,000	156,786	76,589	48.8	1,203.9	0.77	1.57
1948	5,000	153,454	75,320	49.1	1,065.9	0.69	1.42
1947	5,000	154,096	76,254	49.5	1,006.1	0.65	1.32
1946	5,000	148,458	73,759	49.7	1,058.5	0.71	1.44
1945	5,000	157,174	67,021	42.4	929.2	0.59	1.39
1944	5,000	134,662	56,398	41.9	804.3	0.60	1.43
1943	5,000	111,650	48,440	43.4	703.1	0.63	1.45
1942	5,000	89,869	32,837	36.5	616.9	0.69	1.88
1941	5,000	71,209	28,249	39.7	553.5	0.78	1.96
1940	5,000	65,288	26,638	40.8	496.0	0.76	1.86
1939	5,000	57,485	24,650	42.9	452.7	0.79	1.84
1938	5,000	50,791	23,121	45.5	420.5	0.83	1.82
1937	5,000	48,228	22,557	46.8	383.1	0.79	1.70
1936	5,000	50,281	22,330	44.4	343.4	0.68	1.54

1935	5,000	45,125	20,158	44.7	306.0	0.68	1.52
1934 [3]	5,000	40,060	18,075	45.1	291.7	0.73	1.61

[1] For 2007, the numbers are as of September 30, and prior years reflect December 31.

[2] Estimated insured deposits reflect deposit information as reported in the fourth quarter *FDIC Quarterly Banking Profile*. Before 1991, insured deposits were estimated using percentages determined from the June 30 *Call Reports*.

[3] Initial coverage was $2,500 from January 1 to June 30, 1934.

[4]For 1989 through 2005, amounts represent sum of separate BIF and SAIF amounts.

Income and Expenses, Deposit Insurance Fund, from Beginning of Operations, September 11, 1933, through December 31, 2016 Dollars in Millions											
Income						**Expenses and Losses**					
Year[7]	Total	Assessment Income	Assessment Credits	Investment and Other Sources	Effective Assessment Rate[1]	Total	Provision for Losses	Administrative and Operating Expenses[2]	Interest and Other Insurance Expenses	Funding Transfer from the FSLIC Resolution Fund	Net Income/ (Loss)
Total	**$230,629.4**	**$165,000.2**	**$11,392.9**	**$77,022.1**		**$147,747.9**	**$108,474.3**	**$29,809.6**	**$9,464.0**	**$139.5**	**$83,021.0**
2016	10,674.1	9,986.6	0.0	687.5	0.0699%	150.6	(1,567.9)	1,715.0	3.5	0	10,523.5
2015	9,303.5	8,846.8	0.0	456.7	0.0647%	(553.2)	(2,251.3)	1,687.2	10.9	0	9,856.7
2014	8,965.1	8,656.1	0.0	309.0	0.0663%	(6,634.7)	(8,305.5)	1,664.3	6.5	0	15,599.8
2013	10,458.9	9,734.2	0.0	724.7	0.0775%	(4,045.9)	(5,659.4)	1,608.7	4.8	0	14,504.8
2012	18,522.3	12,397.2	0.2	6,125.3	0.1012%	(2,599.0)	(4,22.6)	1,777.5	(153.9)	0	21,121.3
2011	16,342.0	13,499.5	0.9	2,834.4	0.1115%	(2,915.4)	(4,413.6)	1,625.4	(127.2)	0	19,257.4
2010	13,379.9	13,611.2	0.8	(230.5)	0.1772%	75.0	(847.8)	1,592.6	(669.8)	0	13,304.9
2009	24,706.4	17,865.4	148.0	6,989.0	0.2330%	60,709.0	57,711.8	1,271.1	1,726.1	0	(36,002.6)
2008	7,306.3	4,410.4	1,445.9	4,341.8	0.0418%	44,339.5	41,838.8	1,033.5	1,467.2	0	(37,033.2)
2007	3,196.2	3,730.9	3,088.0	2,553.3	0.0093%	1,090.9	95.0	992.6	3.3	0	2,105.3
2006	2,643.5	31.9	0.0	2,611.6	0.0005%	904.3	(52.1)	950.6	5.8	0	1,739.2
2005	2,420.5	60.9	0.0	2,359.6	0.0010%	809.3	(160.2)	965.7	3.8	0	1,611.2
2004	2,240.4	104.3	0.0	2,136.1	0.0019%	607.6	(353.4)	941.3	19.7	0	1,632.8
2003	2,174.0	95.2	0.0	2,078.8	0.0019%	(67.7)	(1,010.5)	935.5	7.3	0	2,241.7
2002	1,795.9	108.0	0.0	2,276.9	0.0022%	719.6	(243.0)	945.1	17.5	0	1,076.3
2001	2,729.7	82.8	0.0	2,646.9	0.0019%	3,123.4	2,199.3	887.9	36.2	0	(393.7)
2000	2,569.9	64.1	0.0	2,505.8	0.0016%	945.2	28.0	883.9	33.3	0	1,624.7
1999	2,416.6	48.3	0.0	2,368.3	0.0013%	2,047.0	1,199.7	823.4	23.9	0	369.6
1998	2,584.3	36.7	0.0	2,547.6	0.0010%	817.5	(5.7)	782.6	40.6	0	1,766.8
1997	2,165.6	38.7	0.0	2,126.9	0.0015%	247.3	(505.7)	677.2	75.8	0	1,918.3
1996	7,157.3	5,294.7	0.0	1,862.6	0.1627%	353.6	(417.2)	568.3	202.5	0	6,803.7
1995	5,229.1	3,876.9	0.0	1,352.2	0.1242%	202.2	(354.2)	510.6	45.8	0	5,026.9

1994	7,682.0	6,722.6	0.0	959.4	0.2185%	(1,825.1)	(2,459.4)	443.2	191.1	0	9,507.1
1993	7,356.8	6,684.3	0.0	672.5	0.2146%	(6,744.4)	(7,660.4)	418.5	497.5	0	14,101.2
1992	6,480.5	5,759.8	0.0	720.7	0.1807%	(596.8)	(2,274.7)	614.8[3]	1,063.1	35.4	7,112.7
1991	5,887.0	5,254.5	0.0	632.5	0.1605%	16,925.3	15,496.2	326.1	1,103.0	42.4	(10,995.9)
1990	3,856.3	2,873.3	0.0	983.0	0.0867%	13,059.3	12,133.1	275.6	650.6	56.1	(9,146.9)
1989	3,496.6	1,885.0	0.0	1,611.6	0.0001%	4,352.2	3,811.3	219.9	321.0	5.6	(850.0)
1988	3,347.7	1,773.0	0.0	1,574.7	0.0833%	7,588.4	6,298.3	223.9	1,066.2	0	(4,240.7)
1987	3,319.4	1,696.0	0.0	1,623.4	0.0833%	3,270.9	2,996.9	204.9	69.1	0	48.5
1986	3,260.1	1,516.9	0.0	1,743.2	0.0833%	2,963.7	2,827.7	180.3	(44.3)	0	296.4
1985	3,385.4	1,433.4	0.0	1,952.0	0.0833%	1,957.9	1,569.0	179.2	209.7	0	1,427.5
1984	3,099.5	1,321.5	0.0	1,778.0	0.0800%	1,999.2	1,633.4	151.2	214.6	0	1,100.3
1983	2,628.1	1,214.9	164.0	1,577.2	0.0714%	969.9	675.1	135.7	159.1	0	1,658.2
1982	2,524.6	1,108.9	96.2	1,511.9	0.0769%	999.8	126.4	129.9	743.5	0	1,524.8
1981	2,074.7	1,039.0	117.1	1,152.8	0.0714%	848.1	320.4	127.2	400.5	0	1,226.6
1980	1,310.4	951.9	521.1	879.6	0.0370%	83.6	(38.1)	118.2	3.5	0	1,226.8
1979	1,090.4	881.0	524.6	734.0	0.0333%	93.7	(17.2)	106.8	4.1	0	996.7
1978	952.1	810.1	443.1	585.1	0.0385%	148.9	36.5	103.3	9.1	0	803.2
1977	837.8	731.3	411.9	518.4	0.0370%	113.6	20.8	89.3	3.5	0	724.2
1976	764.9	676.1	379.6	468.4	0.0370%	212.3	28.0	180.4[4]	3.9	0	552.6
1975	689.3	641.3	362.4	410.4	0.0357%	97.5	27.6	67.7	2.2	0	591.8
1974	668.1	587.4	285.4	366.1	0.0435%	159.2	97.9	59.2	2.1	0	508.9
1973	561.0	529.4	283.4	315.0	0.0385%	108.2	52.5	54.4	1.3	0	452.8
1972	467.0	468.8	280.3	278.5	0.0333%	59.7	10.1	49.6	6.0[5]	0	407.3
1971	415.3	417.2	241.4	239.5	0.0345%	60.3	13.4	46.9	0.0	0	355.0
1970	382.7	369.3	210.0	223.4	0.0357%	46.0	3.8	42.2	0.0	0	336.7
1969	335.8	364.2	220.2	191.8	0.0333%	34.5	1.0	33.5	0.0	0	301.3
1968	295.0	334.5	202.1	162.6	0.0333%	29.1	0.1	29.0	0.0	0	265.9
1967	263.0	303.1	182.4	142.3	0.0333%	27.3	2.9	24.4	0.0	0	235.7
1966	241.0	284.3	172.6	129.3	0.0323%	19.9	0.1	19.8	0.0	0	221.1
1965	214.6	260.5	158.3	112.4	0.0323%	22.9	5.2	17.7	0.0	0	191.7
1964	197.1	238.2	145.2	104.1	0.0323%	18.4	2.9	15.5	0.0	0	178.7

1963	181.9	220.6	136.4	97.7	0.0313%	15.1	0.7	14.4	0.0	0	166.8
1962	161.1	203.4	126.9	84.6	0.0313%	13.8	0.1	13.7	0.0	0	147.3
1961	147.3	188.9	115.5	73.9	0.0323%	14.8	1.6	13.2	0.0	0	132.5
1960	144.6	180.4	100.8	65.0	0.0370%	12.5	0.1	12.4	0.0	0	132.1
1959	136.5	178.2	99.6	57.9	0.0370%	12.1	0.2	11.9	0.0	0	124.4
1958	126.8	166.8	93.0	53.0	0.0370%	11.6	0.0	11.6	0.0	0	115.2
1957	117.3	159.3	90.2	48.2	0.0357%	9.7	0.1	9.6	0.0	0	107.6
1956	111.9	155.5	87.3	43.7	0.0370%	9.4	0.3	9.1	0.0	0	102.5
1955	105.8	151.5	85.4	39.7	0.0370%	9.0	0.3	8.7	0.0	0	96.8
1954	99.7	144.2	81.8	37.3	0.0357%	7.8	0.1	7.7	0.0	0	91.9
1953	94.2	138.7	78.5	34.0	0.0357%	7.3	0.1	7.2	0.0	0	86.9
1952	88.6	131.0	73.7	31.3	0.0370%	7.8	0.8	7.0	0.0	0	80.8
1951	83.5	124.3	70.0	29.2	0.0370%	6.6	0.0	6.6	0.0	0	76.9
1950	84.8	122.9	68.7	30.6	0.0370%	7.8	1.4	6.4	0.0	0	77.0
1949	151.1	122.7	0.0	28.4	0.0833%	6.4	0.3	6.1	0.0	0	144.7
1948	145.6	119.3	0.0	26.3	0.0833%	7.0	0.7	6.3[6]	0.0	0	138.6
1947	157.5	114.4	0.0	43.1	0.0833%	9.9	0.1	9.8	0.0	0	147.6
1946	130.7	107.0	0.0	23.7	0.0833%	10.0	0.1	9.9	0.0	0	120.7
1945	121.0	93.7	0.0	27.3	0.0833%	9.4	0.1	9.3	0.0	0	111.6
1944	99.3	80.9	0.0	18.4	0.0833%	9.3	0.1	9.2	0.0	0	90.0
1943	86.6	70.0	0.0	16.6	0.0833%	9.8	0.2	9.6	0.0	0	76.8
1942	69.1	56.5	0.0	12.6	0.0833%	10.1	0.5	9.6	0.0	0	59.0
1941	62.0	51.4	0.0	10.6	0.0833%	10.1	0.6	9.5	0.0	0	51.9
1940	55.9	46.2	0.0	9.7	0.0833%	12.9	3.5	9.4	0.0	0	43.0
1939	51.2	40.7	0.0	10.5	0.0833%	16.4	7.2	9.2	0.0	0	34.8
1938	47.7	38.3	0.0	9.4	0.0833%	11.3	2.5	8.8	0.0	0	36.4
1937	48.2	38.8	0.0	9.4	0.0833%	12.2	3.7	8.5	0.0	0	36.0
1936	43.8	35.6	0.0	8.2	0.0833%	10.9	2.6	8.3	0.0	0	32.9
1935	20.8	11.5	0.0	9.3	0.0833%	11.3	2.8	8.5	0.0	0	9.5
1933-34	7.0	0.0	0.0	7.0	N/A	10.0	0.2	9.8	0.0	0	(3.0)

[1]The effective rates from 1950 through 1984 vary from the statutory rate of 0.0833 percent due to assessment credits provided in those years. The statutory rate

increased to 0.12 percent in 1990 and to a minimum of 0.15 percent in 1991. The effective rates in 1991 and 1992 vary because the FDIC exercised new authority to increase assessments above the statutory rate when needed. Beginning in 1993, the effective rate is based on a risk-related premium system under which institutions pay assessments in the range of 0.23 percent to 0.31 percent. In May 1995, the BIF reached the mandatory recapitalization level of 1.25 percent. As a result, BIF assessment rates were reduced to a range of 0.04 percent to 0.31 percent of assessable deposits, effective June 1995, and assessments totaling $1.5 billion were refunded in September 1995. Assessment rates for BIF were lowered again to a range of 0 to 0.27 percent of assessable deposits, effective the start of 1996. In 1996, the SAIF collected a one-time special assessment of $4.5 billion that fully capitalized the fund. Consequently, assessment rates for SAIF were lowered to the same range as DIF, effective October 1996. This range of rates remained unchanged for both funds through 2006. As part of the implementation of the Federal Deposit Insurance Reform Act of 2005, assessment rates were increased to a range of 0.05 percent to 0.43 percent of assessable deposits effective at the start of 2007, but many institutions received a one-time assessment credit ($4.7 billion in total) to offset the new assessments.

[2] These expenses, which are presented as operating expenses in the Statements of Income and Fund Balance, pertain to the FDIC in its corporate capacity only and **do not** include costs that are charged to the failed bank receiverships that are managed by the FDIC. The receivership expenses are presented as part of the "Receivables from Resolutions, net" line on the Balance Sheets. The information presented in the "FDIC Expenditures" table on page 108 of this report shows the aggregate (corporate and receivership) expenditures of the FDIC.

[3] Includes $210 million for the cumulative effect of an accounting change for certain postretirement benefits.

[4] Includes $105.6 million net loss on government securities.

[5] This amount represents interest and other insurance expenses from 1933 to 1972.

[6] Includes interest paid on capital stock.

[7] For 1989 through 2005, amounts represent sum of separate BIF and SAIF amounts.