Center on
Federal Financial
Institutions

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The Center on Federal Financial Institutions (COFFI) is a nonprofit, nonpartisan, non-ideological policy institute focused on federal insurance and lending activities.

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Federal Deposit Insurance Corporation

The FDIC preserves and promotes public confidence in the U.S. financial system. The organization's stated goals are (i) insuring deposits in banks and thrift institutions up to $100,000; (ii) identifying, monitoring, and addressing risks to the deposit insurance funds; and, (iii) limiting the effect on the economy and the financial system when a bank or thrift institution fails.

The banking system is of unique importance for government oversight due to its central role in the financial payments system, its provision of liquidity to credit and deposit markets, as well as its vulnerability to sudden waves of loan defaults and deposit withdrawals.

FDIC

Insured Deposits: $3.7 trillion

Reserves: $47 billion

Reserve Ratio: 1.28%

Statutory Taxpayer Exposure*: $77 billion

Budget Cost FY 2004: Nothing

*Note: Reflects total federal losses in a worst case scenario given current law and current financial commitments

The FDIC has a long history of responding to banking crises. The Federal Deposit Insurance Corporation was created with the Banking Act of 1933 in order to protect depositors from the conditions that had caused thousands of bank failures in the 1920s and early 1930s. The FDIC was significantly reorganized and strengthened in 1991 in response to the savings and loan crisis that saw the collapse of 1,043 banks and thrifts, and which necessitated a massive taxpayer bailout of approximately $124 billion.

Structure and Functions

Nuts and bolts. The FDIC is an independent agency of the federal government. It is governed by a five-person Board of Directors, all of whom are appointed by the President and confirmed by the Senate. No more than three are from the same political party. FDIC deposit coverage, premiums, and regulatory functions are set by Congress pursuant to 12 U.S.C 16. The FDIC is overseen in Congress by the House's Financial Services committee and the Senate's Banking, Housing, and Urban Affairs committee.

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The FDIC is responsible for three main functions. First, it provides deposit insurance to customers at member banks and financial institutions. The agency is structured around two main funds, the Bank Insurance Fund (BIF) and the Savings Association Insurance Fund (SAIF). These two are completely separate entities with their own members, resources, and expenses. There are current legislative proposals to merge these two funds (See 'Current Issues' below). Credit unions are covered by a separate but similar agency, the National Credit Union Association (NCUA).

Second, in a related role, the FDIC manages the receivership of bankrupt and failed financial institutions. It often organizes the sale of the failed institution to another bank.

Third, the FDIC is responsible for supervision and consumer protection with relation to the nation's banking system. It is the primary federal financial regulator for state-chartered institutions not part of the Federal Reserve System. The FDIC has a secondary role in regulating all other insured bank and thrift institutions for the purpose of deposit insurance. It may work independently or in conjunction with the federal or state agency that is the primary regulator for the institution in question.

Federal Financial Institution Regulation and Supervision Structure

Coordinated through the Federal Financial Institutions Examination Council, these five agencies are responsible for examination, supervision, and regulation of the nation's financial institutions:

Federal Deposit Insurance Corporation: Primary regulator of insured state-chartered banks that are not members of the Federal Reserve System; a secondary regulator of all insured institutions for deposit insurance purposes

Board of Governors of the Federal Reserve System: Primary regulator of: (i) state-chartered banks that are members of the Federal Reserve System; (ii) state-chartered bank holding companies; and, (iii) U.S. offices of Foreign Banks

National Credit Union Association: Charters credit unions and is the primary regulator of credit unions

Office of the Comptroller of Currency: Charters national banks and is the primary regulator of these nationally-chartered banks

Office of Thrift Supervision: Charters savings and loan institutions and is the primary regulator of these thrifts and their holding companies

Resolving bank failures. The FDIC has several choices when resolving institution failures. The one most commonly used is the sale of deposits and loans of the failed institution to another institution. Customers of the failed institution automatically become customers of the assuming institution. Most times, this transition is seamless from the depositor's point of view.

Bank mergers. When two or more insured banks merge, the deposits from the assumed bank continue to be insured separately for at least six months after the merger. This grace period gives a depositor the opportunity to restructure accounts, if necessary.

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Finances

Overall size. The FDIC has insurance funds, the BIF and the SAIF, with about $47 billion in assets. The FDIC insures more than $3.7 trillion of deposits, out of an assessable deposit base – roughly the total volume of deposits – of $5.6 trillion, in 8,943 U.S. banks and thrifts. See Table 1.

Table 1: Deposit Funds

	FDIC Overall	BIF	SAIF
Coverage			
Member Institutions (Sept 2004)	8,935	7,785	1,150
Insured Deposits (March 2005) *in billions*	$ 3,711	$ 2,745	$ 966
Balance			
Fund Balance (March 2005) *in billions*	$ 47	$ 34	$ 12
Reserve Ratio (March 2005)	1.28	1.27	1.32
Selected Institutions			
Problem Institutions (CY 2004)	80	69	11
Assets (CY 2004) *in millions*	$ 28,250	$ 27,161	$ 1,089
Failed Institutions (CY 2004)	4	3	1
Assets (CY 2004) *in millions*	$ 167	$ 151	$ 15
Average Annual Assets *in millions*		$ 857	$ 455

Source: FDIC Annual Report 2004 and Quarterly Banking Report March 2005

Statutory taxpayer exposure. The FDIC receives no Congressional appropriations. It is completely self-supporting financially. While deposits are not secured by the full faith and credit of the government, any money borrowed or obligations sold by the FDIC are. It has up to a $30 billion line of credit from the Treasury. It can also sell obligations, such as securities, through the Federal Financing Bank to FDIC members. The maximum the FDIC may have in outstanding obligations, either through the Treasury or through the FFB, is approximately the total value of the BIF's and SAIF's assets ($47 billion as of March 2005) plus the Treasury credit line. The maximum statutory limit on FDIC borrowing is currently around $77 billion.

How is it financed? The FDIC is funded by three main sources: (i) interest earned by its insurance funds' investments in U.S. Treasuries; (ii) premiums assessed on members in order to maintain a reserve ratio (ratio of fund assets to deposits insured, in percent) of 1.25; and, (iii) assets recovered from failed banks. All FDIC activities – including insurance, supervision, receivership, and the Inspector General's Office – are paid for by the money earned by the three means listed above. See Table 2.

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Table 2: Budget Costs

Fiscal Years	BIF		SAIF		Total FDIC	
	2004 Act.	2005 Est.	2004 Act.	2005 Est.	2004 Act.	2005 Est.
Costs *in millions*						
Insurance	$ 84	$ 153	$ 20	$ 22	$ 104	$ 175
Supervision	$ 510	$ 477	$ 60	$ 70	$ 570	$ 547
Receivership	$ 128	$ 155	$ 21	$ 21	$ 149	$ 176
General and Administrative	$ 100	$ 93	$ 17	$ 16	$ 117	$ 109
Case Resolution Losses	$ 18	$ 23	$ 0	$ 8	$ 8	$ 31
Other	$ 97	$ 90	$ 12	$ 32	$ 109	$ 122
	$ 937	$ 991	$ 130	$ 169	$ 1,067	$ 1,160
Revenues *in millions*						
Discretionary						
Transfers (to Inspector General's Office)	$ -23	$ -25	$ -3	$ -4	$ -26	$ -29
Mandatory						
Interest on Federal Securities	$ 1,410	$ 266	$ 522	$ 67	$ 1,932	$ 333
Asset Recoveries	$ 424	$ 258	$ 11	$ 140	$ 435	$ 398
Premium Assessments	$ 96	$ 113	$ 9	$ 29	$ 105	$ 142
Other	$ 13	$ 0	$ 0	$ 0	$ 13	$ 0
	$ 1,920	$ 612	$ 539	$ 232	$ 2,459	$ 844
Balance *in millions*						
Balance from previous year	$ 31,418	$ 32,401	$ 11,543	$ 11,952	$ 42,961	$ 44,353
Total Costs	$ -937	$ -991	$ -130	$ -169	$ -1,067	$ -1,160
Total Revenues	$ 1,920	$ 612	$ 539	$ 232	$ 2,459	$ 844
Balance carried forward	$ 32,401	$ 32,022	$ 11,952	$ 12,015	$ 44,353	$ 44,037

Source: President's FY2006 Budget Appendix

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What deposits are insured. FDIC deposit insurance covers the balance of each depositor's account, dollar-for-dollar, up to the insurance limit, including principal and any accrued interest through the date of the insured bank's closing.

Savings, checking, CDs, NOW, money market deposit, and other deposit accounts, when combined, are generally insured up to $100,000 per depositor in each bank or thrift the FDIC insures.

There exist qualifications to this rule, as well as provisions for additional coverage:

- Deposits held in different categories of ownership – such as joint accounts – may be separately insured.
- Separate coverage is generally provided for self-directed retirement accounts, such as individual retirement accounts (IRAs) and Keoghs under IRS code, section 401.
- Also, a participant's share of some employee benefit plan accounts (pension or profit-sharing) are insured up to $100,000.
- Trusts are typically insured up to $100,000 per beneficiary.
- Corporations, partnerships, and associations are covered up to $100,000, regardless of their membership.

What is not insured. Securities, mutual funds or similar types of investments that banks and thrift institutions may offer are not insured.

Premium levels. Deposit insurance premiums are charged only to the riskiest and least stable institutions. Currently, fewer than 10% of institutions pay premiums. Since 1996, the FDIC has been prohibited by law from charging premiums to well-capitalized and stable institutions. See Table 3.

Premiums are set twice a year, in May (for effect in July through December) and in November (for effect in January through June). The rates reflect the Congressional mandate that the reserve ratio stay above 1.25. If the ratio should fall below 1.25, the FDIC is required to raise premiums to close the gap within a year. Currently, premiums range from 0 to 27 basis points (hundredths of a percent).

Premiums are charged to institutions on the basis of two ratings: capitalization and supervisory subgroup (an aggregation of factors relating to on-site reviews of the institution). Currently 93% of institutions, holding 98% of insured deposits, are in the highest capitalization and supervisory groupings. These institutions pay no premiums. Only 2 institutions currently pay the highest premiums of 27 basis points.

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Table 3: Premium Levels

	Supervisory Subgroups		
	A	**B**	**C**
Well Capitalized			
Assessment Rate *in basis points*	0	3	17
Institutions	8,352	448	68
Institutions *in %*	93.4%	5.0%	0.8%
Total Assessable Deposits *in %*	98.4%	1.0%	0.3%
Adequately Capitalized			
Assessment Rate *in basis points*	3	10	24
Institutions	60	3	8
Institutions *%*	0.7%	0.0%	0.0%
Total Assessable Deposits *in %*	0.1%	0.0%	0.0%
Undercapitalized			
Assessment Rate *in basis points*	10	24	27
Institutions	1	1	2
Institutions *in %*	0.0%	0.0%	0.0%
Total Assessable Deposits *in %*	0.0%	0.0%	0.0%

Note: Figures are for the BIF and SAIF combined, as of March 31, 2005
Source: FDIC March 2005 Quarterly Banking Report

Current Issues

Proposed reforms. In the last 5 years the FDIC, in conjunction with other government agencies such as the Treasury, has been researching possible reforms to make the corporation more flexible, efficient, and responsive. In 2003, the House approved legislation that advocated significant reforms. This legislation was never passed in the Senate before its adjournment. The Administration's FY2006 budget proposes many of the same reforms. As of August 2005, the Federal Deposit Insurance Reform Act of 2005 (H.R. 1185) sponsored by Representatives Bachus and Hooley has passed the House and is awaiting committee review in the Senate. This legislation is similar to the Administration's proposal but also includes increased deposit coverage, outlined in the fourth point below.

Federal Deposit Insurance Reform Act of 2005. This proposed legislation would:

- Merge the BIF and SAIF into a single fund called the Federal Deposit Insurance Fund.
  - Pro: A merger could strengthen, diversify, and make consistent the FDIC's two funds.
  - Con: Gains might be small.
- Allow the FDIC to price premiums to risk on all banks regardless of capitalization.
  - Pro: A handful of large banks hold a majority of insured deposits and new deposits, as well as a significant and identifiable risk, yet are not required to pay into the fund.
  - Con: This will most likely increase premiums to the 93% of institutions that currently pay none.

- Allow the FDIC to target a range of reserve ratios, rather than a current fixed target of 1.25 which must be met within a year should reserves fall below that.
    - Pro: Upper and lower bounds on reserve ratios (effectively 1.15 to 1.375) could allow the FDIC more flexibility to avoid pro-cyclical effects such as sharply increased premiums in a recession.
    - Con: FDIC flexibility to set reserve ratios might unnecessarily let the funds diminish, and only requires a 10 year plan to return to the minimum reserve ratio.
- Alter deposit qualifications by: (i) raising the maximum ceiling to $130,000 and indexing it to inflation every 5 years after 2007; (ii) including some previously excluded deferred compensation plans under IRS section 457; and (iii) providing double the maximum coverage for deposits in qualified accounts pursuant to IRS sections 401, 408, 457 (IRAs, Keoghs, etc.).
    - CBO estimates that this will increase insured deposits by about $330 billion by 2007.
    - Pro: Current (unchanged since 1991) and future maximum coverage levels would be indexed to inflation in order to provide adequate insurance.
    - Con: Increasing coverage could reduce the incentive of depositors to monitor their banks, and could increase a bank's risk-taking.

Basel II Capital Standards. The Basel Committee made recommendations on risk-based capital standards in June 2004. These recommendations are an effort to create international guidelines that will allow institutions to more effectively and consistently price risk. The FDIC is currently working on a strategy to incorporate these standards into its regulatory and deposit insurance functions.

Sources

FDIC: 2004 Annual Report; March 2005 Quarterly Banking Profile; The Cost of the Savings and Loan Crisis; available via http://www.fdic.gov

FFIEC: Annual Report 2004; available via http://www.ffiec.gov

OMB: President's FY2006 Budget; available via http://www.whitehouse.gov/omb

U.S. Code: Full Text of 12 U.S.C. 16; available via http://uscode.house.gov

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