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The FDIC's Special Assessment: Basing Deposit Insurance on Assets Instead of Deposits

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The FDIC's Special Assessment: Basing Deposit Insurance on Assets Instead of Deposits

I. INTRODUCTION

In 2007, only three FDIC-insured institutions failed. In the following year, the number increased to twenty-six, and as the full force of the financial crisis hit banks, 140 failed in 2009. The FDIC insures failed banks' deposits through the Deposit Insurance Fund (DIF) and is required to maintain the DIF's reserve ratio, the ratio between the total amount of deposits insured and the amount in the DIF, at or above 1.15 percent. The recent exponential rise in bank failures has depleted the DIF. During the second quarter of 2009 alone, the DIF decreased by $2.6 billion, falling to $10.4 billion and putting the reserve ratio at .22 percent. This figure represented the lowest reserve ratio for the insurance fund since 1993, and by the end of the third quarter of 2009, the FDIC announced that the insurance fund had a negative balance of $8.2 billion. Under the Federal Deposit Insurance Reform Act of 2005, the FDIC is required to implement a

6. FDIC, Deposit Insurance Fund Trends, supra note 4.
7. Id.
"Restoration Plan" to raise the reserve ratio back up to 1.15 percent if it ever falls below that amount.\(^1\)

In October 2008, the FDIC instituted a Restoration Plan\(^1\) to replenish the depleted DIF.\(^2\) As part of that plan, on May 22, 2009, the FDIC announced that it would impose a five basis point\(^3\) special assessment.\(^4\) This assessment was controversial because it was based on an insured institution's assets instead of deposits.\(^5\)

The FDIC's ultimate decision to charge five basis points per dollar in assets was reasonable, although it is a historic departure from deposit insurance practice.\(^6\) During a time of economic difficulties, the special assessment not only increased the DIF, but also maintained consumer confidence in the banking industry.\(^7\) Part II of this note will briefly describe the historical

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13. This means that every one hundred dollars of assets will be taxed at five cents. One basis point represents 1/100th of a percentage point. See Indep. Cmty. Bankers of Am., FDIC Special Assessment Calculation Example, http://www.icba.org/files/IcBASites/PDFs/FDICSpecialAssessmentEx.pdf.


17. See Joe Adler, FDIC May Seek to Avoid New Assessment, AM. BANKER., Sept. 21, 2009, at 1, available at 2009 WLNR 18395466.
and legal context of the FDIC's mission. Part III will investigate
the statutory authority behind the rule change. Part IV will
discuss the impact of the final rule on small banks as opposed to
large banks, and Part V will discuss the public debate
surrounding the final rule. Finally, Part VI will discuss the
FDIC's motivation to maintain independence during the financial
crisis.

II. THE FEDERAL DEPOSIT INSURANCE SYSTEM AND THE
SPECIFICS OF THE FINAL RULE

A. Introduction to the Federal Deposit System

The FDIC, created by the Banking Act of 1933, protects
bank deposits and prevents bank runs. It insures the deposits of
all banks and savings associations, and when one fails, the FDIC
liquidates it and disposes of its assets. Currently, the FDIC will
insure deposits up to $250,000 funded from the DIF. Insured
institutions finance the DIF through quarterly assessments,
calculated in two steps, and is based on institutional risk and

18. See infra Part II, pp. 383-86.
22. See infra Part VI, pp. 399-401.
23. Banking Act of 1933, ch. 89, 48 Stat. 162 (1933) (codified as amended in
24. Thomas K. McCraw, Regulate, Baby, Regulate, NEW REPUBLIC, Mar. 18,
25. Other options for resolving a failed institution besides liquidating assets
include a purchase and assumption transaction with another institution and open
26. Sandra Block, With CD Rates So Low, Plot Strategy and Shop for Best Deals,
USA TODAY, June 2, 2009, at 7B, available at 2009 WLNR 10407338; see Press
Release, FDIC, Emergency Economic Stabilization Act of 2008 Temporarily
Increases Basic FDIC Insurance Coverage from $100,000 to $250,000 Per Depositor
the insured amount from $100,000 to $250,000 on October 3, 2008); see also Helping
Families Save Their Homes Act, Pub.L. 111-22, 123 Stat. 1632 (2009) (extending the
deadline for increasing the maximum amount covered by the FDIC to December 31,
2013).
amount of deposits. First, capital levels and supervisory ratings determine into which of four risk levels the bank falls. Next, the FDIC gives the bank a CAMELS rating, analyzing six different factors: capital, asset quality, management, earnings, liquidity, and sensitivity to market risk. This analysis determines the appropriate assessment rate for the bank which is then applied to the total amount of deposits.

In 2009, the FDIC took a three-pronged approach to deal with the depleting reserve fund. First, the FDIC increased the regular quarterly assessment rate imposed on insured depository institutions. Second, the FDIC imposed a special assessment calculated on assets, instead of deposits, payable by September of 2009. Last, the FDIC accelerated the collection of regular assessments by requiring all insured institutions (absent a waiver) to prepay three years’ worth of regular deposit insurance by the end of 2009.

B. Specifics Regarding the Special Assessment

The FDIC adopted an “interim rule with request for comment” on February 27, 2009 which imposed a special assessment of twenty basis points on insured institutions’ deposits.

29. FDIC, Risk Categories & Risk-Based Assessment Rates, supra note 28.
30. Id.
31. Id.
34. Press Release, FDIC, Board Adopts Restoration Plan, supra note 12.
37. Special Assessments, supra note 10, at 25,640.
and was to be collected by the end of the third quarter. The FDIC Board also reserved the right to impose an additional special assessment of up to 10 basis points. The agency not only requested comments on the interim rule, but also on alternatives for calculating the assessment. Comments included claims that the FDIC was unfairly penalizing community banks, suggestions that the FDIC tap the credit line with the U.S. Treasury, and proposals that any special assessment be based on total assets (minus tangible capital), not on total deposits.

The FDIC changed its position and adopted a final rule very different from the interim rule. Under the final rule, the FDIC calculates the special assessment based on a flat rate on each institution’s assets reduced by any Tier 1 capital as reported by the end of the second quarter. This assessment method is a departure from the traditional calculation of the regular quarterly assessment rate, which is a risk-adjusted rate applied to an institution’s deposits. The FDIC also retained the option of imposing two additional special assessments over the last two quarters of 2009.

The FDIC switched from the interim rule to the final rule in part to reduce the “pro-cyclical” effects of the special assessment because banks were struggling to lend money already. Increased taxes on banks faced with liquidity issues would only exacerbate the problem. By spreading the payments to the FDIC

38. Id.
39. Id.
40. Id.

41. See e.g., Letter from Dennis J. Peters, Operations Officer, Timberwood Bank, to Sheila Bair, Chairman, FDIC (March 3, 2009), available at http://www.fdic.gov/regulations/laws/federal/2009/09c475AD35.PDF; see id. at 25643.
42. See id., at 25,640.
43. Tier 1 Capital is comprised by the following elements: (1) Common stockholder’s equity; (2) Noncumulative perpetual preferred stock and related surplus; and (3) Minority interests in the equity accounts of consolidated subsidiaries. See 12 C.F.R. pt. 3 app. A (2009).
44. FDIC, Deposit Insurance Fund Trends, supra note 4; Press Release, FDIC, FDIC Adopts Final Rule, supra note 33.
45. See FDIC: Deposit Insurance Assessment, Sample 1 Invoice, supra note 32; see supra pp. X-Y and notes 28-32.
46. Special Assessments, supra note 10, at 25,642.
47. Id. at 25,641.
out over time, the assessment might have a lesser negative impact on a bank’s earnings in any one quarter. The FDIC, however, ultimately decided to make banks prepay three years worth of regular assessments to address pro-cyclical effects instead of collecting additional special assessments. Under this plan, banks could record prepayments as an asset and then record each quarter’s assessment as an expense as it became due. Prepayment will not negatively impact bank earnings, but it will negatively impact banks’ liquidity. The efforts to reduce pro-cyclical effects of the special assessment were appropriate because bank failures surged as problems in the financial sector continued into the fall of 2009.

III. STATUTORY AUTHORITY

The FDIC has an express delegation of authority to regulate and establish and risk-based assessments system based on 12 U.S.C.A. § 1817. The FDIC also claims that it has implied authority to impose a special assessment based on assets under Section 7(b)(5) of the Federal Deposit Improvement Act (FDIA). The FDIA provides that the FDIC may “impose one or more special assessments on insured depository institutions” for any necessary purpose in an amount determined by the FDIC.

To assess the validity of a federal agency’s interpretation of a statute where the statutory language is silent or ambiguous, the agency’s interpretation will control if it is a “permissible

49. Labaton, Banks to Prepay Assessments, supra note 36. The final rule reduces the assessment amount from a one-time twenty basis point assessment to a five basis point assessment with the possibility of two additional assessments of the same rate. Special Assessments, 74 Fed. Reg. 25,639 at 25,639-40.
50. See Labaton, Banks to Prepay Assessments, supra note 36.
51. Id.
54. 12 U.S.C.A § 1817 (2009); Special Assessments, supra note 10, at 25,641 (explaining how the statute does not define the assessment base to be used when imposing a special assessment).
55. Special Assessments, supra note 10, at 25,641.
construction of the statute." The statute does not define the assessment base for making a special assessment; however, Congress’s statutory delegation of authority implicitly permits the FDIC to define the appropriate assessment base for the special assessment by rulemaking. Often when Congress delegates authority to a regulatory agency, it gives the agency discretion to administer the statute. The agency’s interpretation of the authorizing statute is controlling unless the interpretation is "capricious, or manifestly contrary to the statute." Furthermore, the FDIC Improvement Act (FDICIA) of 1991 repealed provisions which defined "assessment" in any specific way, and this seems to justify the FDIC’s use of discretion to interpret the statute. Because no specific definition of assessment was put in place afterwards, Congress intended to give the FDIC more discretion.

Several major banks disagree with the FDIC’s interpretation of the statute. Norman Nelson, general counsel for The Clearing House, a trade group representing some of the United State’s largest banks, argues that the FDIC’s imposition of the special assessment “inappropriate” under the relevant statutes. According to Nelson, a threat of systemic risk is the only situation where the FDIC can base an emergency special assessment on insured institutions’ total assets. A systemic risk determination involves a number of agencies and actors: the Treasury Secretary can determine systemic risk after consultation

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57. See Special Assessments, supra note 10, at 25,641.
58. See Chevron USA, 467 U.S.at 843; Special Assessments, supra note 10, at 25,641.
60. Id. at 843-44.
65. Id.
with the President and input from the FDIC Board and the Board of Governors of the Federal Reserve. Instead, the FDIC bases its authority to impose the special assessment on its general authority to recapitalize the DIF when the reserve ratio drops below 1.15 percent.

Nelson also argues that the agency acted inconsistently with the FDIA. The FDIA, which provides that "[n]o insured depository institution shall be barred from the lowest-risk category solely because of size," was intended to prevent discriminatory assessments on large depository institutions. If the special assessment were based on assets, larger banks, with disproportionately more assets than smaller banks, would pay a greater share of the special assessment used to rebuild the DIF.

The discrepancy between the FDIC and the Clearing House's interpretations of the agency's authority exists because the two sides focus on different statutory provisions. The Clearing House looks to 12 U.C.S. § 1823, while the FDIC justifies the special assessment under its general authority in 12 U.S.C.A. § 1817.

The Clearing House's argument that the FDIC is acting inappropriately focuses on lack of process in the FDIC's decision: the relevant agencies have not officially determined that a systemic risk emergency exists. The special assessment statute, relied on

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66. A situation of systemic risk is an emergency determination by the Secretary of the Treasury. Other agencies that are involved in determining whether a systemic risk situation exists are the board of directors of the FDIC, the Board of Governors of the Federal Reserve System. See 12 U.S.C.A. § 1823(c)(4)(G)(2009); see Letter from Norman R. Nelson to Robert E. Feldman, supra note 16, at 2.


69. Id. at 2-3.


72. Another reason the FDIC switched from the interim rule to the final rule is because larger banks which hold a higher proportion of assets to deposits than smaller banks, would pay a greater proportion of the special assessment to increase the DIF. See Special Assessments, supra note 10, at 25,644. See Appelbaum, supra note 5.


by the FDIC, however, does not require a finding of systemic risk.\textsuperscript{76}

Even if the Clearing House is correct that a finding of systemic risk is a necessary precondition for the imposition of a special assessment, arguably, this condition was fulfilled when the FDIC established the Temporary Liquidity Guarantee Program (TLGP).\textsuperscript{77} The FDIC introduced this program to avoid serious risks associated with the economic and financial crisis after October 13, 2008 when the Treasury Secretary (after consultation with the President, following recommendations from the FDIC Board and the Board of Governors of the Federal Reserve) determined that systemic risk existed.\textsuperscript{78} The only remaining issue is whether this systemic risk determination expired by the time the FDIC imposed the special assessment.\textsuperscript{79} Assuming that the systemic risk determination has not expired as of May 2009, then the Clearing House has no argument to delegitimize the statutory authority of the Special Assessment. Overall, the FDIC's interpretation of section 1817\textsuperscript{80} is a permissible interpretation of the agency's implicit authority to make special assessments.\textsuperscript{81}

IV. IMPACT ON LARGE BANKS AND SMALL BANKS

A. The General Impact on Large and Small Banks

The FDIC's final rule will have a greater impact on large banks than on small banks\textsuperscript{82} because large banks will pay a greater proportion of the special assessment.\textsuperscript{83} Small banks "tend to have

\textsuperscript{77} See 12 C.F.R. § 370 (2008).
\textsuperscript{78} Id.
\textsuperscript{79} Mike Krimminger, Senior Policy Advisor to the Chairman, FDIC, Speech on Systemic Risk to Professor Lissa Broome's Banking Law class, University of North Carolina School of Law, (Nov. 13, 2009).
\textsuperscript{81} See Chevron USA, 467 U.S. at 843. Chevron held that if a statute is silent or ambiguous with respect to a specific issue in an agency's construction of the statute it administers, the question is whether the agency's answer is based on a permissible interpretation. Id.
\textsuperscript{82} Large banks are generally banks with more than $100 billion in assets and small banks are those with less than $100 billion in assets. Appelbaum, supra note 5.
\textsuperscript{83} Special Assessments, supra note 10, at 25,644.
roughly the same amount of assets and deposits, because they lend to borrowers what they collect from depositors." Large banks lend from multiple sources, such as borrowed money, so their assets may exceed their deposits by a greater percentage than smaller banks which do not typically use alternative sources of funding. Thus, when the FDIC made the decision to change the assessment base from deposits to assets, small banks were benefitted because they will pay a lower proportion of the special assessment than under the interim rule. News sources hailed this as a victory for smaller banks.

B. Projected and Actual Results on Larger Banks

Financial estimates show the disparate way in which the special assessment would impact small and large banks. Citibank estimated it would pay a premium ranging from $578 to $809 million under the final rule. If the assessment was based on deposits, Citibank’s premium would fall between $120 and $168 million. State Street Bank and Trust is projected to pay an additional $10 million in premiums under the final rule. Goldman Sachs Group was projecting an increase of $5 million under the final rule. JPMorgan Chase & Co. has paid $675 million out of second quarter earnings and Wells Fargo & Co.,

84. Appelbaum, supra note 5.
85. Large banks more readily than small banks hold other assets such as commercial paper and securities. Daniel K. Tarullo, Member of Board of United States Federal Reserve Board, Large Banks and Small Banks in an Era of Systemic Risk Regulation, Speech at the North Carolina Bankers Association Annual Convention (June 15, 2009), http://www.federalreserve.gov/newsevents/speech/tarullo20090615a.htm; Krimminger, supra note 79; Appelbaum, supra note 5 (defining what is a large bank).
86. Special Assessments, supra note 10, at 25,643-44.
87. Appelbaum, supra note 5; Adler, Big Bank Groups Protest FDIC-Planned Asset Levy, supra note 63.
88. Adler, Assessment to Penalize Large Banks, supra note 15, at 1.
89. Id.
91. Id.
which has more than ten thousand branches, has paid $565 million to the FDIC under the final rule.\textsuperscript{93} By changing the assessment base, the FDIC would collect $500 million more in assessments from large banks than what it would have collected under the interim rule.\textsuperscript{94} Because of the significant impact on larger banks, the ensuing debate focused on whether this was a prudent decision given economic conditions.

V. THE DEBATE SURROUNDING THE SPECIAL ASSESSMENT

After the FDIC announced its interim rule, different groups and individuals sent 14,000 comment letters in response.\textsuperscript{95} The interim rule proposed an assessment base similar to regular quarterly assessments, but the FDIC specifically asked for comments regarding the use of a different assessment base.\textsuperscript{96} The potential for a historic break from deposit insurance practice polarized large banks and small banks.\textsuperscript{97}

A. Equity Concerns Regarding the Special Assessment.

Banks favoring the final rule argued that it was fair because of the role and treatment of larger banks in the financial collapse,\textsuperscript{98} believing that smaller community lenders had a more limited role in subprime lending which was at the heart of the financial collapse.\textsuperscript{99} Karen Thomas, director of government relations at the Independent Community Bankers of America (ICBA), believes

\textsuperscript{93} Id.
\textsuperscript{94} See Appelbaum, supra note 5.
\textsuperscript{96} See Letter from Norman R. Nelson to Robert E. Feldman, supra note 16, at 7 (responding to the prospect of a special assessment at the FDIC's request).
\textsuperscript{97} See Appelbaum, supra note 5.
that large banks are getting what they deserve. She argues that large banks' risky lending and investment practices caused the increase in bank failures which has in turn depleted the DIF. In 2008, most of the cost to the DIF came from the resolution of IndyMac Bank F.S.B. which had $32 billion in assets and $19 billion in deposits. Furthermore, making large banks pay higher special assessment fees is more equitable because larger banks generally had earlier and easier access to the Troubled Access Relief Program (TARP) money than smaller banks. Smaller banks had to go through more onerous procedures to receive TARP assistance.

The ICBA also stated that a special assessment based on deposits, even if it were just ten basis points per dollar of deposits, will unfairly penalize community banks who are trying to increase lending in their communities. According to ICBA surveys, thirty-two percent of member banks estimated that the special assessment based on deposits will absorb between sixteen and twenty-five percent of their 2009 earnings, and seventeen percent estimated it will consume between twenty-six and forty percent of earnings. The survey showed that thirty-one percent of respondents believe the assessment under the interim rule will noticeably affect their ability to lend to local communities. Overall, community bankers felt the interim rule punished them for financial turmoil that they did not create.

100. See Adler, Big Bank Groups Protest FDIC-Planned Levy, supra note 63, at 16.
101. See id.
104. See id.
105. See id. at 3.
106. See id.
107. See id.
108. See id. at 3.
Chairman Sheila Bair agreed stating that collecting more money from the largest banks was a "step back toward equity." According to Bair, "[o]ver the past eighteen months, large banks, as a group, have posed much greater risks to the banking system than small banks have." The interim rule's charge of twenty basis points on deposits significantly hurt smaller banks disproportionately because they are less diversified and have fewer sources of income to absorb the assessment fee than larger banks.

In contrast, the Comptroller of the Currency, John Dugan, a member of the FDIC board of directors, voted against the final rule because he believes that the financial crisis was caused in part by smaller banks' excessive lending in the commercial real estate market rather than financial instability caused by large banks. He believes large banks were not responsible for smaller banks making loans secured by commercial real estate funded by brokered deposits. This combination contributed to the fact that many of the bank failures in 2008 and 2009 were smaller banks. Only one institution that has failed since January 2008, Washington Mutual Incorporated (Washington Mutual), had more than $50 billion in assets. In fact, the average size of assets held by the other fifty-seven bank failures between January 2008 and mid-May 2009 was $1.5 billion. Recently, the FDIC has experienced losses between forty and fifty percent after selling small banks that it took over. By contrast, the failure of

109. Appelbaum, supra note 5.
110. Id.
111. Glasser, supra note 99.
113. Id.
117. Id.
Washington Mutual produced no loss to the DIF when the FDIC sold it to JPMorgan Chase & Co. Looking solely at 2009, all banks that failed had less than $50 billion in assets with the largest failure being Colonial BancGroup Incorporated which had $25 billion in assets.

Large banks are also mitigating costs to the DIF and the overall impact of the financial crisis by purchasing failed institutions. For example, Bank of America Corporation (Bank of America) acquired Countrywide Financial Corporation, JPMorgan Chase & Co. acquired Washington Mutual, and Wells Fargo & Co. acquired Wachovia Corporation. Without these actions, the FDIC would have made larger payouts to insured depositors at these banks. For example, Washington Mutual which was the largest bank failure in U.S history, had $188.3 billion in deposits insured by the FDIC before it failed.

B. Why Small Banks Continue to Fail

If larger banks have caused the financial crisis, and not small banks, as stated by the ICBA, why are most of the institutions failing small banks? The answer is twofold: 1) smaller banks have had disproportionately more exposure to commercial real-estate loans than larger banks; and 2) larger banks have received federal aid in the form of preferred stock purchases before small institutions were given similar access.

119. Id.
121. Id.
122. See Adler, Assessment to Penalize Large Banks, supra note 15, at 1.
123. See id.
126. See, e.g., Adler, Big Bank Groups Protest FDIC-Planned Asset Levy, supra note 63, at 16 (explaining how the average size of 57 of 58 banks that failed since January of 2008 was only $1.5 billion in assets).
127. See Wei, supra note 114.
During the housing boom smaller and medium-sized banks lent to home builders and commercial property developers because they could not compete in the home mortgage market with large banks and Wall Street firms. Over-development of commercial real estate and the housing crisis came to bear on all parts of the economy, and many of the loans made by these smaller banks defaulted. Unlike the larger banks who were holding problematic mortgage-backed securities, small banks got into trouble because their traditional loans went into default. Based on stress test results in the spring of 2009, federal regulators predicted that an estimated 581 small banks were at risk of collapse by 2011 when applying only the commercial real estate loss assumptions. On the other hand, none of the nation's nineteen largest banks, and only about five percent of the next 100 lenders at risk of collapse, faced significant commercial real estate losses.

Larger banks may be indirectly responsible for the failure of smaller banks if they forced smaller banks out of the home mortgage market and into the commercial real estate market. Arguably, however, being "forced out" is merely a function of fair competition. More importantly, it is not true that one market was clearly better than another because home mortgage defaults meant write downs of the value of the toxic securities leading to the demise of larger banks and Wall Street firms. Nevertheless, even though both types of institutions held problematic assets, larger institutions received earlier assistance from the federal government. It is within this context that the FDIC imposed a higher proportion of the special assessment on larger institutions.

129. Wei, supra note 114.
130. See Cook, supra note 128.
131. See id.
132. Dash, Small Banks Failure Rate Grows, Straining F.D.I.C., supra note 53.
133. See id.
134. See Wei, supra note 114.
135. See Cook, supra note 128.
137. Chadbourn, supra note 95.
C. A Better Reflection of Risk?

Some observers suggested that basing assessments on assets is a better actuarial method of assessing risk to the DIF. Accordingly, a bank's assets is a better measure of risk because bad assets, not deposits, cause bank failures. The FDIC's Problem Bank List estimates that there are approximately $332 billion in loans or leases on which borrowers have stopped making payments as of August 27, 2009. Larger banks such as Citigroup Corporation (Citigroup) and Bank of America are not on this problem list because they receive hundreds of billions of dollars in taxpayer support. Adding them to list, however, would increase the total number of toxic assets tenfold to three trillion dollars. In terms of fairness, basing premiums on assets may be a more accurate measurement because when the FDIC takes over a bank, its losses are based on the value of the assets of the bank. The FDIC does not assume just the deposits of a failed bank but it assumes other liabilities as well.

In response to the idea that premiums based on assets is a better measure of risk, Norman Nelson, General Counsel of the Clearing House group, states that this is "out of line with the FDIC's core mission, which is to insure deposits." Risk to the DIF does not arise from assets but from FDIC insured deposits. Furthermore, an increased ratio of assets to deposits does not

139. Id.
142. Id.
143. Id.
144. Adler, Assessment to Penalize Large Banks, supra note 15, at 1.
146. Adler, Big Bank Groups Protest FDIC-Planned Asset Levy, supra note 63, at 16.
147. Id.
necessarily increase risk to the DIF.\textsuperscript{148} Assets are only dangerous to a bank's stability if they are based on problematic securities like the $55 billion in subprime loans held by Citigroup.\textsuperscript{149} Often, holding other types of assets besides deposits can increase the health of a bank by diversifying risk.\textsuperscript{150}

Many comments submitted to the FDIC argued either that assessments based on assets would decrease the burden on smaller banks, or that assets are a better measure of risk to the DIF.\textsuperscript{151} Evidence supports the former argument more than the latter.\textsuperscript{152} In the final rule, the FDIC explained that it did not favor using a risk based system like that used for regular quarterly assessments.\textsuperscript{153} The primary purpose of the special assessment was to build up the DIF and not to reflect the risk of future failures.\textsuperscript{154} A risk-based special assessment would result in a premium too large for the riskiest institutions because the special assessment would be in addition to the regular assessments.\textsuperscript{155} While FDIC may have considered the role that larger institutions played in the financial collapse, their access to TARP funds, and the vulnerability of smaller-community banks during this economic crisis, it cannot be said that the FDIC based its assessment on assets instead of deposits to more accurately reflect risk to the DIF.

\textbf{D. \textit{Additional Criticisms of the Final Rule}}

1. Lack of Notice

Some critics claimed that the final rule violated due process because it was an abrupt change from the former interim rule

\textsuperscript{148} \textit{Id.}
\textsuperscript{149} \textit{See, e.g., In re Citigroup Inc. Shareholder Derivative Litigation, 964 A.2d 106, 113 (Del. Ch. 2009) (explaining how Citigroup faced billions of dollars in losses because of its extensive use of collateralized debt obligations).}
\textsuperscript{150} \textit{See Letter from Norman R. Nelson to Robert E. Feldman, supra note 16, at 4-5.}
\textsuperscript{151} Special Assessments, \textit{supra} note 10, at 25,643-44.
\textsuperscript{152} \textit{Id.} at 25,643-44.
\textsuperscript{153} \textit{Id.} 25,643.
\textsuperscript{154} \textit{Id.}
\textsuperscript{155} \textit{Id.} at 25,643-44.
without sufficient time for public comment.\footnote{See Adler, Big Bank Groups Protest FDIC-Planned Asset Levy, supra note 63, at 16.} Given the dramatic change from seventy-five years of deposit insurance history,\footnote{Letter from Norman R. Nelson to E. Feldman, supra note 16, at 1.} large banks believe it is unfair to change the assessment base without an opportunity for all interested parties to present meaningful comments on a detailed proposal.\footnote{See Adler, Big Bank Groups Protest FDIC-Planned Asset Levy, supra note 63, at 16.} After the FDIC made the final rule, no formal means existed by which interested parties could convince the agency that it had made a mistake.\footnote{See Letter from Norman R. Nelson to Robert E. Feldman, supra note 16, at 7. See Special Assessments, supra note 10, at 25,644. Id. at 25,643. Id.} The FDIC believed, however, that it provided the public and the banking industry with sufficient opportunity to comment.\footnote{Id. at 25,643.} Although the final rule meant the special assessment was based on assets, the FDIC specifically asked for comments regarding whether assessments should be based on assets or some other measure and whether the special assessments should account for assistance being provided to systemically important institutions.\footnote{Id. at 25,643. See Letter from Norman R. Nelson to Robert E. Feldman, supra note 16, at 7. See Special Assessments, supra note 10, at 25,644.} In response, many commentators agreed that the special assessment should be based on assets because it both reduced the burden on smaller banks and was a more accurate measure of risk.\footnote{Id.} Thus, the claim that the FDIC’s switch to the final rule based on lack of notice is unjustified.\footnote{Press Release, OCC News, supra note 15.}

2. Perverse Incentives

Another criticism was that the final rule introduced perverse incentives for the banking industry.\footnote{Adler, Big Bank Groups Protest FDIC-Planned Asset Levy, supra note 63, at 16.} Taxing assets instead of deposits could entice institutions to move assets off of their balance sheets into nonbank entities making those assets unavailable to cushion the bank when it is at risk of failing.\footnote{Adler, Big Bank Groups Protest FDIC-Planned Asset Levy, supra note 63, at 16.}
Also, banking supervisors historically encourage institutions to diversify their funding bases beyond deposits, but the final rule would punish banks that use alternative funding sources. Furthermore, this policy may give off the false impression that assets are insured instead of deposits. The mission of the FDIC has always been to insure deposits so that the public will keep its money in banks, not to protect against other assets a bank might hold. The fact that the FDIC has recently decided not to collect any more special assessments based on assets precludes this from being a legitimate concern.

VI. POLICY IMPLICATIONS

Critics of Chairman Bair have stated that the FDIC's decision to base the special assessment on assets represents changed policy objectives among FDIC leadership. Some evidence suggests that the FDIC is taking a more active role in economic recovery but for the most part, the FDIC's decision to impose the special assessment is a reaction against the practice of bailing out banks deemed "too big to fail." Imposition of the special assessment also reemphasizes the agency's traditional mission of maintaining public confidence in the nation's banking industry.

A. Evidence of More Active Role for the FDIC?

The FDIC inevitably plays a more significant role if the financial system is in trouble because of its duty to insure

167. Id.
168. See supra p. 383 and notes 23-25.
169. See supra p. 386 and note 50.
170. See Appelbaum, supra note 5.
To fulfill this duty, the FDIC must shore up the DIF so that funds are available for failed banks. One analyst estimated that the FDIC will have to collect as much as $45 billion through 2013 to raise the DIF’s reserve ratio to 1.15 percent, the amount that is required by law. Additionally, Chairman Bair has publicly opined on the need to depart from the “too-big to fail” system. Instead of resorting to federal bail-outs, she argues that financial firms generally, not just banks and thrifts, should go through FDIC insolvency procedures should they fail. Bair wants to bring these institutions directly within the FDIC’s traditional regulatory powers through a system that deals with failures outside of the bankruptcy process. Bair’s statements suggest that the FDIC’s desire for an increased regulatory presence during the economic crisis is more reactionary than reflective of a fundamental shift in policy objectives.

B. Desire for Regulatory Independence

While Chairman Bair’s leadership may indicate a desire for a more active role during this financial crisis, throughout the interim rule’s comment period, the FDIC reiterated its unwillingness to borrow from its line of credit with Treasury to fund expected losses. The FDIC has never taken any tax money to fulfill its mission, and it does not want to change that. The FDIC has always been funded by the insured institutions, and it

176. See, e.g., Crittenden, supra note 173 (recounting Blair’s statements to the Senate Banking Committee that “a ‘handful of giant institutions with global reach’ and a single regulator is a recipe for mistakes.”).
177. Id.
178. Id.
179. Special Assessments, supra note 10, at 25,643.
THE FDIC'S SPECIAL ASSESSMENT

does not want to depend on taxpayers to fund the deposit insurance system.\textsuperscript{181} Furthermore, Bair is concerned that borrowing from the Treasury would harm the FDIC's public image because the public may view this reliance as another taxpayer bailout for the banking industry.\textsuperscript{182} On the day that the FDIC collected the special assessment, Bair announced that the FDIC would not levy further special assessments.\textsuperscript{183} Instead, the FDIC required banks to prepay three years' of their regular assessments by December 31, 2009 to show the public that the industry "will not simply tap the shoulder of the increasingly weary taxpayer."\textsuperscript{184}

VII. CONCLUSION

The FDIC's decision to impose a special assessment based on banks' assets instead of deposits to shore up the DIF was a rational decision despite being a break with deposit insurance practice. First, the FDIC wanted larger banks to bear more of the burden in building up the DIF primarily because larger banks benefitted from federal assistance before most small banks and because of smaller banks' unstable financial position.\textsuperscript{185} Second, the FDIC wanted to avoid pro-cyclical effects of a special assessment by charging only five basis points minus Tier-1 capital and allowing for subsequent special assessments spread out over time.\textsuperscript{186} These were reasonable concerns because banks continued to fail well into the fall of 2009.\textsuperscript{187} Third, the FDIC wanted to maintain public confidence by not exercising its option to borrow from the Treasury.\textsuperscript{188} The FDIC's decision to make banks prepay three years worth of regular assessments instead of borrowing

\textsuperscript{181} See Labaton, \textit{Banks to Prepay Assessments}, supra note 36.

\textsuperscript{182} See Adler, \textit{FDIC May Seek to Avoid New Assessment}, supra note 17, at 1 (explaining how Bair has been reluctant to borrow from the Treasury); see also Labaton, \textit{Banks to Prepay Assessments}, supra note 36 (showing how Bair believes that making banks prepay assessments will signal to the public that the federal government will not bail out the banking industry).

\textsuperscript{183} See Labaton, \textit{Banks to Prepay Assessments}, supra note 36.

\textsuperscript{184} Id.

\textsuperscript{185} See supra pp. 389-93 and notes 82-111.

\textsuperscript{186} See supra pp. 385-86 and notes 47-49.

\textsuperscript{187} See supra p. 386 and notes 50-53.

\textsuperscript{188} See supra pp. 400-01 and notes 179-183.
from the Treasury emphasized its commitment to agency independence. 189 How banks, large and small, will fare from this special assessment and whether the FDIC will be able to successfully increase the reserve ratio remains to be seen.

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189. See supra p. 401 and note 184.