

October 3, 2006

MEMORANDUM TO: The Board of Directors

FROM: Douglas H. Jones
Acting General Counsel

SUBJECT: Notice of Initial Regulatory Flexibility Act Analysis
To Supplement Notice of Proposed
Rulemaking for Part 327 – Risk-Based Assessments

Recommendation

On July 24, 2006, the Federal Deposit Insurance Corporation (FDIC) issued a notice of proposed rulemaking with request for comments on the proposed rule to better price deposit insurance for risk (the Pricing NPR) as required by the Federal Deposit Insurance Act, as amended by the Federal Deposit Insurance Reform Act ("Reform Act") (see 71 FR 41910 (July 24, 2006)). The proposed rulemaking included the required section dealing with the Regulatory Flexibility Act (RFA). The RFA requires agencies to consider the impact of their regulatory proposal on small entities, analyze alternatives that minimize impact, and make these analyses available for public comment.

In the RFA section of the Pricing NPR, the FDIC invoked the RFA exemption for rules of particular applicability relating to rates or corporate or financial structures, or practices relating to such rates or structures, which are expressly excluded from the RFA's definition of "rule." 5 U.S.C. § 601. Under the exemption, no RFA analysis is required and none was provided in the Pricing NPR. The FDIC has consistently used this exemption in assessment rulemaking for more than ten years.

The Small Business Administration Office of Advocacy (SBA) is responsible for monitoring agency compliance with the RFA. Recently, SBA staff informally questioned whether the exception applies to this rulemaking. While FDIC staff disagrees with SBA staff's view, we nonetheless recommend publication in order to avoid any issue about whether there has been full RFA compliance. We make this recommendation because, despite our belief that the FDIC's initial position is correct, under these circumstances not publishing would result in an unnecessary risk of an unlikely, but highly undesirable, outcome. To wit, an RFA provision permits small entities adversely affected or aggrieved by final agency action to seek judicial review of agency compliance with the RFA's requirements. 5 U.S.C. 611. The RFA permits remedies that include, but are not limited to, remanding the rule to the agency and deferring enforcement of the rule.

Reviewed by:

Arthur J. Murton
Director
Division of Insurance and Research

Discussion: Under the RFA, the FDIC can perform an initial regulatory flexibility analysis or certify that the proposed rule will have “no significant economic impact on a substantial number of small entities.” (For RFA purposes, insured institutions with \$165 million or less in assets are “small entities”; as of December 2005, there were 5,362 such institutions.)

Staff recommends that the Board approve the attached Federal Register notice that contains an RFA analysis of the proposed pricing rule and also certifies that the rule would have “no significant economic impact on a substantial number of small entities.” The Federal Register notice also makes clear that the FDIC is continuing to assert the rate exemption.

The certification is based on work done by the Division of Insurance and Research which has analyzed the impact of the proposed small bank pricing system and the alternative as set out in the Pricing NPR. The analyses are set forth in the attached Notice of Initial Regulatory Flexibility Analysis. Based on December 2005 data, the statistics showed that, under the proposed small bank pricing method, over 99 percent of the 5,362 small institutions as defined by RFA would have experienced an increase or decrease in assessments amounting to one percent, or less, of annual revenue. For about half of these, the change reflected an assessment decrease. Using the same data, 85 percent of the 5,362 small institutions as defined by the RFA would have experienced an increase or decrease in their annual profits of one percent or less. For about half of these, the change reflected an assessment decrease and a profit increase. Similar results were obtained for the alternative method of risk differentiation for small institutions.

The full analysis is contained in the attached Notice of Initial Regulatory Flexibility Analysis, which staff recommends be published in the Federal Register for a comment period of approximately 10 to 14 days, depending upon the date of the Board’s adoption of staff’s recommendation.

Staff recommends that the Board approve the attached Federal Register notice, authorize its publication in the Federal Register, and accept related comments following such publication.

Attachment