D. Measures of Success

If the Agency decides to develop a policy for tailored incentives for new owners, EPA intends to develop a three-year pilot program to test the effectiveness of such incentives. In order to objectively, effectively and promptly evaluate the pilot program and this approach, EPA must have already identified clearly measurable outcomes and efficient assessment methodologies. The main goal of this program, and the most important measure of success, would be to show that compliance with environmental laws and regulations has improved, and that significant environmental benefit has been attained. However, there are different approaches for determining how well these goals have been met. What measures of success should the Agency adopt for the evaluation of a pilot program? Important outcomes to consider could be the number of disclosures made under the pilot program, the significance of the violations involved, and the significance of the pollutant reductions that can be attributed to or associated with these disclosures. Transparency of the program, efficiency in administration, and low transaction costs are also issues to be considered in evaluating the tailored incentive approach. EPA is seeking comment on any potential measures, and on the methodologies necessary to accurately measure them.

III. Public Process

As part of EPA’s effort to obtain input on whether to offer tailored incentives for new owners self-disclosing under the Audit Policy, the Agency is planning to hold two public comment sessions. At those two meetings, interested parties may attend and provide oral and written comments on the issues. The first meeting is scheduled for Washington, DC at the J.W. Marriott Hotel, 1331 Pennsylvania Ave., NW, on June 12, 2007. The second one is scheduled for San Francisco at the Palace Hotel, 2 New Montgomery St., on June 20, 2007. Both meetings will begin at 10 a.m. and end at 4 p.m.

The Agency is especially interested in comments relating to the issues specified in this Notice. After the comment period closes, the Agency plans to review and consider all comments. If EPA decides to develop a pilot program offering tailored incentives to new owners beyond those currently available under the Audit Policy, the Agency would then publish a second Federal Register notice to seek comment on such a proposed pilot program. After a second round of public comment, the Agency would publish in the Federal Register: The final description of the pilot program; an announcement of its start date; and a description of how its success in achieving increased self-auditing and disclosure and significant improvement to the environment will be evaluated. EPA encourages parties of all interests, including State and local government, industry, not-for-profit organizations, municipalities, public interest groups, and private citizens to comment, so that the Agency can hear from as broad a spectrum as possible.

IV. What Should I Consider as I Prepare My Comments for EPA?

1. Submitting CBI. Do not submit this information to EPA through www.regulations.gov or e-mail. Clearly mark the part or all of the information that you claim to be CBI. For CBI information in a disk or CD ROM that you mail to EPA, mark the outside of the disk or CD ROM as CBI and then identify electronically within the disk or CD ROM the specific information that is claimed as CBI. In addition to one complete version of the comment that includes information claimed as CBI, a copy of the comment that does not contain the information claimed as CBI must be submitted for inclusion in the public docket. Information so marked will not be disclosed except in accordance with procedures set forth in 40 CFR Part 2.

2. Tips for Preparing Your Comments. When submitting comments, remember to:
   • Identify the Notice; Request for Comments by docket number and other identifying information (subject heading, Federal Register date and page number).
   • Follow directions—The Agency may ask you to respond to specific questions.
   • Explain why you agree or disagree; suggest alternatives and language.
   • Describe any assumptions and provide any technical information and/or data that you used.
   • If possible, provide any pertinent information about the context for your comments (e.g., the size and type of acquisition transaction you have in mind).
   • If you estimate potential costs or burdens, explain how you arrived at your estimate in sufficient detail to allow for it to be reproduced.

• Provide specific examples to illustrate your concerns, and suggest alternatives.

• Explain your views as clearly as possible.

• Submit your comments on time.

Granta Y. Nakayama,
Assistant Administrator, Office of Enforcement and Compliance Assurance.
[FR Doc. E7–9197 Filed 5–11–07; 8:45 am]
BILLING CODE 6560–50–P

EQUAL EMPLOYMENT OPPORTUNITY COMMISSION

Notice of Sunshine Act Meeting

CHANGE IN THE MEETING:
Open Session:
Item Nos. 3. Full-Service Publication Storage and Distribution Center Contract has been removed from the Agenda.
CONTACT PERSON FOR MORE INFORMATION:
Stephen Llewellyn, Acting Executive Officer, on (202) 663–4070.
Stephen Llewellyn,
Acting Executive Officer, Executive Secretariat.
[FR Doc. 07–2386 Filed 5–10–07; 8:45 am]
BILLING CODE 6570–01–M

FEDERAL DEPOSIT INSURANCE CORPORATION

Assessment Rate Adjustment Guidelines for Large Institutions and Insured Foreign Branches in Risk Category I

AGENCY: Federal Deposit Insurance Corporation (FDIC).
ACTION: Final guidelines.
SUMMARY: The FDIC is publishing the guidelines it will use for determining how adjustments of up to 0.50 basis points would be made to the quarterly assessment rates of insured institutions defined as large Risk Category I institutions, and insured foreign branches in Risk Category I, according to the Assessments Regulation. These guidelines are intended to further clarify the analytical processes, and the
controls applied to these processes, in making assessment rate adjustment determinations.

DATES: Effective Date: May 8, 2007.

FOR FURTHER INFORMATION CONTACT: Miguel Browne, Associate Director, Division of Insurance and Research, (202) 898–6789; Steven Burton, Senior Financial Analyst, Division of Insurance and Research, (202) 898–3539; and Christopher Bellotto, Counsel, Legal Division, (202) 898–3801.

SUPPLEMENTARY INFORMATION:

I. Background

Under the Assessments Regulation (12 CFR 327.91), assessment rates of large Risk Category I institutions are first determined using either supervisory and long-term debt issuer ratings, or supervisory ratings and financial ratios for large institutions that have no publicly available long-term debt issuer ratings. While the resulting assessment rates are largely reflective of the rank ordering of risk, the Assessments Regulation indicates that FDIC may determine, after consultation with the primary federal regulator, whether limited adjustments to these initial assessment rates are warranted based upon consideration of additional risk information. Any adjustments will be limited to no more than 0.50 basis points higher or lower than the initial assessment rate and in no case would the resulting rate exceed the maximum rate or fall below the minimum rate in effect for an assessment period. In the Assessments Regulation, the FDIC acknowledged the need to further clarify its processes for making adjustments to assessment rates and indicated that no adjustments would be made until additional guidelines were approved by the FDIC’s Board.

On February 21, 2007, the FDIC published in the Federal Register, for a 30-day comment period, a set of proposed guidelines that would be used by the FDIC to evaluate when an assessment rate adjustment is warranted as well as the magnitude of that adjustment. 72 FR 7878 (Feb. 21, 2007). The FDIC sought public comment on the proposed guidelines and received seven comment letters: three from trade organizations whose membership is comprised of banks and savings associations (one of these letters was submitted jointly on behalf of three trade organizations), three from large banking organizations, and one from a small community bank.2 The comments received and the final guidelines governing the assessment rate adjustment process are discussed in later sections.

II. Summary

For purposes of making assessment rate adjustment decisions as transparent as possible, the final guidelines describe in detail the steps that will be used by the FDIC to identify possible inconsistencies between the rank orderings of risk suggested by initial assessment rates and other risk information, the types of risk measures that will be considered in these comparisons, the relative importance that the FDIC will attach to various types of risk measures, and the controls to ensure any decision to make an adjustment is justified and well-informed.

The first six guidelines describe the analytical processes and considerations that will determine whether an assessment rate adjustment is warranted as well as the magnitude of any adjustment. In brief, the FDIC will compare the risk ranking of an institution’s initial assessment rate, as compared to the assessment rates of other large Risk Category I institutions, with the risk rankings suggested by other risk measures. The purpose of these comparisons is to identify possible material inconsistencies in the rank orderings of risk suggested by the initial assessment rate and these other risk measures. Comparisons will encompass risk measures that relate to both the likelihood of failure and loss severity in the event of failure. The analytical process will consider all available risk information pertaining to an institution’s risk profile including supervisory, market, and financial performance information as well as quantitative loss severity estimates, qualitative indicators that pertain to potential resolutions costs in the event of failure, and information pertaining to the ability of an institution to withstand adverse conditions.

The next four guidelines described the controls that will govern the analytical process to ensure adjustment decisions are justified, well supported, and appropriately take into account additional information and views held by the primary federal regulator, the appropriate state banking supervisor, and the institution itself. These guidelines include a requirement to consult with an institution’s primary federal regulator and appropriate state banking supervisor before making an adjustment, and to provide an institution with advance notice of, and an opportunity to respond to a pending upward adjustment.

The timing of an assessment rate adjustment will depend on whether it is an upward or a downward adjustment. Any upward adjustment would not be reflected in an institution’s assessment rates immediately, but rather in the first assessment period after the assessment period that prompted the notification of an upward adjustment. The purpose of this advance notice is to provide an institution being considered for an upward adjustment an opportunity to respond with additional information should the institution disagree with the stated reasons for the upward adjustment. Downward adjustments will be applied immediately within the assessment period being considered. Any implemented upward or downward adjustment will remain in effect until the FDIC determines the adjustment is no longer warranted. The removal of a downward adjustment is subject to the same advance notification requirements as an upward adjustment.

Underlying the FDIC’s adjustment authority is the need to preserve consistency in the orderings of risk indicated by these assessment rates, the need to ensure fairness among all large institutions, and the need to ensure that assessment rates take into account all available information that is relevant to the FDIC’s risk-based assessment decision. As noted in the proposed guidelines, the FDIC expects that such adjustments will be made relatively infrequently and for a limited number of institutions. This expectation reflects the FDIC’s view that the use of agency and supervisory ratings, or the use of supervisory ratings and financial ratios when agency ratings are not available, will sufficiently reflect the risk profile and rank orderings of risk in large Risk Category I institutions in most cases.

Comments on the General Intent of the Adjustment Guidelines

A joint letter submitted on behalf of three trade organizations (referred to hereafter as the “joint letter”) agrees that it is critical for the FDIC to identify inconsistencies and anomalies between initial assessment rates and relative risk levels posed by large Risk Category I institutions. The joint letter also urges the FDIC to closely monitor assessment rates produced by the Assessment Rule and to consider modifying the base methodology for determining initial assessment rates if a large number of assessment rate adjustments were deemed necessary. The FDIC agrees

1 71 FR 69282 (November 30, 2006).
2 The trade organizations included the American Bankers Association, America’s Community Bankers, the Financial Services Roundtable, the Clearing House, and the Committee for Sound Lending.
with these observations and has stated that it would likely reevaluate the assessment rate methodology applied to large Risk Category I institutions if assessment rate adjustments were to occur frequently and for more than a limited number of institutions.

A comment from a small community bank indicates its opposition to further reductions in the assessment rates of large banks. The guidelines discussed below allow for both increases and decreases in assessment rates of large Risk Category I institutions.

III. The Assessment Rate Adjustment Process

The process for determining whether an assessment rate adjustment is appropriate, and the magnitude of that adjustment, entails a number of steps. In the first step, an initial risk ranking will be developed for all large institutions in Risk Category I based on their initial assessment rates as derived from agency and supervisory ratings, or the use of supervisory ratings and financial ratios when agency ratings are not available, in accordance with the Assessment Rule.

In the second step, the FDIC will compare the risk rankings associated with these initial assessment rates with the risk rankings associated with broad-based and focused risk measures as well as the risk rankings associated with other market indicators such as spreads on subordinated debt. Broad-based risk measures include each of the inputs to the initial assessment rate considered separately, other summary risk measures such as alternative publicly available debt issuer ratings, and loss severity estimates, which are not always sufficiently reflected in the inputs to the initial assessment rate or in other debt issuer ratings. Focused risk measures include financial performance measures, measures of an institution’s ability to withstand financial adversity, and individual factors relating to the severity of losses to the insurance fund in the event of failure.

In the third step, the FDIC will perform further analysis and review in those cases where the risk rankings from multiple measures (such as broad-based risk measures, focused risk measures, and other market indicators) appear to be inconsistent with the risk rankings associated with the initial assessment rate. This step will include consultation with an institution’s primary federal regulator and state banking supervisor. Although information or feedback provided by the primary federal regulator or state banking supervisor will be considered in the FDIC’s ultimate decision concerning such

adjustments, participation by the primary federal regulator or state banking supervisory in this consultation process should not be construed as concurrence with the FDIC’s deposit insurance pricing decisions.

In the final step, the FDIC will notify an institution when it proposes to make an upward adjustment to that institution’s assessment rate. Notifications involving an upward adjustment in an institution’s initial assessment rate will be made in advance of implementing such an adjustment so that the institution has an opportunity to respond to or address the FDIC’s rationale for proposing an upward adjustment.3 Adjustments will be implemented after considering institution responses to this notification along with any subsequent changes either to the inputs to the initial assessment rate or any other risk factor that relates to the decision to make an assessment rate adjustment.

IV. Final Guidelines Governing Assessment Rate Adjustment Determinations

To ensure consistency, fairness, and transparency, the FDIC will apply the following guidelines to its processes for determining when an assessment rate adjustment appears warranted, the magnitude of the adjustment, and controls to ensure adjustments are justified and take into consideration any additional information or views held by the primary federal regulator, state banking supervisor, and the institutions themselves. Guidelines 1 through 6 relate to the analytical process that will govern assessment rate adjustment decisions. Guidelines 7 through 10 relate to the operational controls that will govern assessment rate adjustment decisions.

Analytical Guidelines

Guideline 1: The analytical process will focus on identifying inconsistencies between the rank orderings of risk associated with initial assessment rates and the rank orderings of risk indicated by other risk measures. This process will consider all available information relating to the likelihood of failure and loss severity in the event of failure.

The Rank Ordering Analysis

The purpose of the analytical process is to identify institutions whose risk measures appear to be significantly different than other institutions with similarly assigned initial assessment rates. The analytical process will identify possible inconsistencies between the rank orderings of risk associated with the initial assessment rate and the risk rankings associated with other risk measures. The intent of this analysis is not to override supervisory evaluations or to question the validity of agency ratings or financial ratios when applicable. Rather, the analysis is meant to ensure that the assessment rates, produced from the combination of either supervisory ratings and long-term debt issuer ratings (the debt rating method), or supervisory ratings and financial ratios (the financial ratio method) result in a reasonable rank ordering of risk that is consistent with risk profiles of large Risk Category I institutions with similar assessment rates.

The FDIC will consider adjusting an institution’s initial assessment rate when there is sufficient information from a combination of broad-based risk measures, focused risk measures, and other market indicators to support an adjustment. An adjustment will be most likely when: (1) The rank orderings of risk suggested by multiple broad-based measures are directionally consistent and materially different from the rank ordering implied by the initial assessment rate; (2) there is sufficient corroborating information from focused risk measures and other market indicators to support differences in risk levels suggested by broad-based risk measures; (3) information pertaining to loss severity considerations raise prospects that an institution’s resolution costs, when scaled by size, would be materially higher or lower than those of other large institutions; or (4) additional qualitative information from the supervisory process or other feedback provided by the primary federal regulator or state banking supervisor is consistent with differences in risk suggested by the combination of broad-based risk measures, focused risk measures, and other market indicators.

A detailed listing of the types of broad-based risk measures, focused risk measures, and other market indicators that will be considered during the analysis process are described in detail in the Appendix. The listing of risk measures in the Appendix is not intended to be exhaustive, but represents the FDIC’s view of the most important focused risk measures to consider in the adjustment process. The development of risk measurement and monitoring capabilities is an ongoing and evolving process. As a result, the FDIC may revise these risk measures considered in its analytical processes over time as a result of these

3 The institution will also be given advance notice when the FDIC determines to eliminate any downward adjustment to an institution’s assessment rate.
development activities and consistent with the objective to consider all available risk information pertaining to an institution’s risk profile in its assessment rate decisions. The FDIC will inform the industry if there are material changes in the types of information it considers for purposes of making assessment rate adjustment decisions.

General Comments on Analytical Guideline 1

A comment from a large banking organization indicates that the market and supervisory ratings already encompass many of the risk measures that will be considered by the FDIC in making assessment rate adjustment decisions. As a result, the commenter questions why the FDIC’s judgment about the risk inherent in these measures should ever be substituted in place of the views of the market or supervisors. Another comment from a large banking organization suggests that the guidelines are redundant with supervisory evaluations from the primary federal regulator.

The analytical approach described in these guidelines does not substitute FDIC views of risk in place of either market or supervisory ratings. The initial assessment rates of large Risk Category I institutions are determined from a combination of supervisory ratings and long-term debt issuer ratings or from a combination of supervisory ratings and financial ratios when long-term debt issuer ratings are not available. Combining these risk measures can produce risk rank orderings of assessment rates that do not align with the risk rank orderings of supervisory ratings considered in isolation. As a result, the consideration of additional risk factors is not redundant with supervisory risk measurement processes and will, in the FDIC’s view, help preserve a reasonable and consistent ordering of risk among large Risk Category I institutions as indicated by the range of assessment rates applied to these institutions.

Consideration of Quantitative Loss Severity Factors

The loss severity factors the FDIC will consider include both quantitative and qualitative information. Quantitative information will be used to develop estimates of deposit insurance claims and the extent of coverage of those claims by an institution’s assets. These quantitative estimates can in turn be converted into a relative risk ranking and compared with the risk rankings produced by the initial assessment rate. Factors that will be used to produce loss severity estimates include: estimates for the amount of insured and non-insured deposit funding at the time of failure; estimates of the extent of an institution’s obligations that would be subordinated to depositor claims in the event of failure; estimates of the extent of an institution’s obligations that would be secured or would otherwise take priority over depositor claims in the event of failure; and the estimated value of assets in the event of failure.

Comments on Quantitative Loss Severity Considerations

One comment letter, the joint letter, objects to the inclusion of Federal Home Loan Bank (FHLB) borrowings in producing loss severity estimates and requests that the FDIC not include these funding sources in the calculation of secured liabilities for purposes of making such estimates. While acknowledging that such advances reduce the level of assets available to the FDIC to satisfy depositor claims in the event of failure, the commenter argues that FHLB borrowings provide a stable and reliable source of funding that reduces the likelihood of failure. The final guidelines do not single out FHLB borrowings, either as a negative or a positive risk factor. The FDIC recognizes that while larger volumes of such funding could result in a lower level of recoveries on failed institution assets, the presence of such funding can also reduce liquidity risks. The FDIC believes it is appropriate to take both factors into account. Specifically, the FDIC believes it should include FHLB borrowings in its calculation of secured borrowings since their exclusion would lead to incomplete and possibly erroneous loss severity estimates. However, the FDIC agrees with the point raised in the joint letter that it is also appropriate to consider the stabilizing influence of such funding while evaluating liquidity risks. Accordingly, the Appendix to the final guidelines makes such liquidity risk considerations more explicit (see qualitative and mitigating liquidity factors under the Liquidity and Market Risk Indicators section).

Another comment from a large banking organization argues that the FDIC’s Assessment Rule assumes a worst-case scenario that all deposits will be insured and therefore that any adjustments should result in lower not higher assessment rates. The FDIC acknowledges that uninsured deposits would serve to reduce the level of losses sustained by the insurance funds in the event of failure. However, the FDIC believes that meaningful loss severity estimates need to take into account a number of considerations beyond determining current levels of insured and uninsured deposits. These considerations include the prospects for ring-fencing of uninsured foreign deposits (discussed further below) and how the mix of deposit and non-deposit liabilities might change from current levels in a failure scenario. To the extent the FDIC uses loss severity estimates to support an adjustment decision, either up or down, it will document and support the assumptions and the bases for these estimates.

Consideration of Qualitative Loss Severity Factors

In addition to quantitative loss severity factors, the FDIC will also consider other qualitative information that would have a bearing on the resolution costs of a failed institution. These qualitative factors include, but are not limited to, the following:

- The case with which the FDIC could make quick deposit insurance determinations and debtor payments as evidenced by the capabilities of an institution’s deposit accounting systems to place and remove holds on deposit accounts en masse as well as the ability of an institution to readily identify the owner(s) of each deposit account (for example, by using a unique identifier) and identify the ownership category of each deposit account;
- The ability of the FDIC to isolate and control the main assets and critical business functions of a failed institution without incurring high costs;
- The level of an institution’s foreign assets relative to its foreign deposits and prospects of foreign governments using these assets to satisfy local depositors and creditors in the event of failure; and
- The availability of sufficient information on qualified financial contracts to allow the FDIC to identify the counterparties to, and other details about, such contracts in the event of failure.

As with other risk measures, the FDIC will evaluate these qualitative loss severity considerations by gauging the prospects for higher resolutions costs posed by a given institution relative to the same type of risks posed by other large Risk Category I institutions. Where the FDIC lacks sufficient information to make such comparisons, assessment rate adjustment decisions will not incorporate these considerations.

Comments on Qualitative Loss Severity Considerations

Deposit Accounting System Capabilities

Three comment letters (the joint letter, a trade organization, and a large
banking organization) object to the inclusion of qualitative loss severity considerations pertaining to the capabilities of deposit accounting systems in the assessment rate adjustment analysis process. Each commenter indicates that it was premature for the FDIC to incorporate such considerations given the separate proposed rulemaking process under way—the Large-Bank Deposit Insurance Determination Modernization Proposal (the modernization proposal). All three letters suggest that such considerations in the assessment rate adjustment process presume the final outcome of this other rulemaking process. The joint letter also suggests that the consideration of these factors may encourage some institutions to undertake costly systems enhancements that may ultimately prove to be inconsistent with requirements imposed by a final rule stemming from the modernization proposal. The joint letter further argues that such considerations do not lend themselves to risk measurement and would necessarily involve a high degree of subjectivity.

As noted in the proposed guidelines, the FDIC believes that institutions that have the deposit accounting capabilities described above (placing holds en masse and the ability to uniquely identify depositors) present a lower level of risks irrespective of the existence or absence of deposit accounting systems. These capabilities across large Risk Category I institutions will incorporate such information in adjustment decisions.

Finally, a comment from a trade organization contends that considerations pertaining to the capabilities of institutions’ deposit accounting systems are not consistent with the objective of achieving fairness in deposit insurance pricing between large and small institutions since only large institutions would be subject to these types of considerations. The FDIC does not agree that such considerations will necessarily impose a penalty on large institutions relative to small institutions since the evaluation of such factors involves comparisons of the capabilities of one institution’s deposit accounting systems relative to those of other large Risk Category I institutions.

On the contrary, consideration of this factor could possibly result in lower assessment rates for institutions that possess these capabilities when the systems of other large institutions with similar assessment rates do not have these capabilities.

Foreign Deposits

One comment, the joint letter, indicated that the level of foreign deposits should not be a consideration for adjusting premium rates. While acknowledging the existence of ring-fencing risks, the commenter indicated that a mere ranking of foreign deposits does not provide sufficient information with which to evaluate this risk.

The FDIC agrees that the level of foreign deposits by itself offers limited information as to the prospects for ring-fencing risk in the event of failure. Rather, the FDIC believes that an evaluation of foreign assets held relative to foreign deposits is a better measure of potential ring-fencing risks since such a measure identifies the upper boundary of assets that could be obtained by foreign governments to satisfy local deposit claims in the event of failure. If available, the information about the level of foreign assets to foreign deposits on a country-by-country basis would be better still in evaluating prospects for ring-fencing. Although the FDIC believes it is appropriate to consider such prospects in its loss severity estimates, these estimates would never be the sole determinant of an assessment rate adjustment according to Guideline 4 (described below). Moreover, any loss severity estimates used in support of assessment rate adjustment would need to fully support this estimate and any assumptions underlying the estimate, including any assumptions relating to foreign assets and deposits.

Stress Considerations

To the extent possible, the FDIC will consider information pertaining to the ability of institutions to withstand adverse events (stress considerations). Sources of this information are varied but might include analyses produced by the institution or the primary federal regulator, such as stress test results and capital adequacy assessments, as well as detailed information about the risk characteristics of an institution’s lending portfolios and other businesses. Because of the difficulties in comparing this type of information across institutions, those stress considerations pertaining to internal stress test results and internal capital adequacy assessments will not be used to develop quantitative analyses of relative risk levels. Rather, such information will be used in a more qualitative sense to help inform judgments pertaining to the relative importance of other risk measures, especially information that pertains to the risks inherent in concentrations of credit exposures and other material non-lending business activities. As an example, in cases where an institution had a significant concentration of credit risk, results of internal stress tests and internal capital adequacy assessments could obviate FDIC concerns about this risk and therefore provide support for a downward adjustment, or alternatively, provide additional mitigating information to forestall a pending upward adjustment. In addition, the FDIC will not use the results of internal stress tests and internal adequacy assessments to support upward adjustments in assessment rates. It must be emphasized that despite the availability of information pertaining to these stress consideration factors, the FDIC expects that assessment rate adjustments will be made relatively infrequently and for a limited number of institutions.

Comments on Stress Considerations

One comment, the joint letter, indicates that difficult-to-quantify subjective risk factors, such as those pertaining to stress considerations and loss severity, should never be used to increase rates, but only to decrease rates. The FDIC agrees that some of the stress consideration risk factors contained in the proposed guidelines, those pertaining to measures of an institution’s ability to withstand financial stress, are difficult to incorporate into an analytical construct that relies on comparisons of ordinal rankings of risk. This difficulty stems from the range of different approaches and different methodologies used to assess capital needs and the ability to withstand financial shocks.

Because of these difficulties, the FDIC agrees with the need to modify its approach for certain stress consideration risk factors. Specifically, rate adjustment decisions in the near term will not rely on quantitative measures involving internal stress test results or internal capital adequacy assessments. Nevertheless, the FDIC believes its assessment rate adjustment process would be incomplete if it did not consider both the extent to which institutions have sufficient capital, earnings, and liquidity to buffer against adverse financial conditions; and the types of risk management processes and strategies institutions use to determine the appropriate level of these buffers. At a minimum, information from an internal
stress testing exercise or an internal capital adequacy assessment would provide useful, albeit nonquantifiable, insights into management’s perspective on the types and magnitude of the risks faced by the institution. Specifically, the FDIC believes that this type of information, considered in a more qualitative than quantitative sense, will lead to more informed deposit insurance pricing decisions by enhancing its understanding of the relative importance of other, more quantifiable risk measures and especially those risk measures relating to credit, market, and operational risk concentrations.

To illustrate, some institutions may occasionally wish to provide stress testing results and internal capital adequacy evaluations to the FDIC to help foster a better understanding of the relative risk levels inherent in a specific portfolio with concentrated credit risk exposures. The FDIC would evaluate this information, not for purposes of initiating an assessment rate adjustment, but to gain further insights into the nature of the underlying credit concentration. If the information presented effectively mitigates concerns over the concentration risk, the FDIC may decide either not to proceed with a pending upward adjustment being contemplated or to proceed with a downward adjustment.

Guideline 2: Broad-based indicators and other market information that represent an overall view of an institution’s risk will be weighted more heavily in adjustment determinations than focused indicators as will loss severity information that has bearing on the ability of the FDIC to resolve institutions in a cost effective and timely manner.

The FDIC will accord more weight to risk-ranking comparisons involving broad-based or comprehensive risk measures than focused risk measures. Examples of comprehensive or broad-based risk measures include, but are not limited to, each of the inputs to the underlying credit ranking comparisons within these business line groupings that included processing institutions and trust companies, residential mortgage lenders, non-diversified regional institutions, large diversified institutions, and diversified regional institutions.7 When making assessment rate adjustment decisions, the FDIC will employ risk ranking comparisons with comparable institutions with differing business lines.

The FDIC will consider the effect of business line concentrations in its risk ranking comparisons. The FDIC’s notice of proposed rulemaking for deposit insurance assessments, issued in July 2006, referenced a set of business line groupings that included processing institutions and trust companies, residential mortgage lenders, non-diversified regional institutions, large diversified institutions, and diversified regional institutions.7 When making assessment rate adjustment decisions, the FDIC will employ risk ranking comparisons within these business line groupings to account for normal variations in risk measures that exist among institutions with differing business line concentrations.

The FDIC received no specific comments on Guideline 5.

Guideline 6: Adjustment will be made only if additional analysis suggests a meaningful risk differential, to include both differences in risk rankings and differences in the underlying risk measures, between the institution’s initial and adjusted assessment rates.

Where material inconsistencies between initial assessment rates and other risk indicators are present, additional analysis will determine the magnitude of adjustment necessary to align the assessment rate better with the rates of other institutions with similar risk profiles. The objective of this analysis will be to determine the amount of assessment rate adjustment that would be necessary to bring an institution’s assessment rate into better alignment with those of other

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5 The Appendix contains additional descriptions of broad-based risk measures.

6 The FDIC will take into account considerations relating to the liquidity of a given issue, differing maturities, and other bond-specific characteristics, when making such comparisons.

7 See 71 FR 71251 (July 24, 2006).
institutions that pose similar levels or risk. This process will entail a number of considerations, including: (1) The number of rank ordering comparisons that identify the institution as a potential outlier relative to institutions with similar assessment rates; (2) the direction and magnitude of differences in rank ordering comparisons; (3) a qualitative assessment of the relative importance of any apparent outlier risk indicators to the overall risk profile of the institution, (4) an identification of any mitigating factors, and (5) the materiality of actual differences in the underlying risk measures.

Based upon these considerations, the FDIC will determine the magnitude of adjustment that would be necessary to better align its assessment rate with institutions that pose similar levels of risk. When the assessment rate adjustment suggested by these considerations is not material, or when there are a number of risk comparisons that offer conflicting or inconclusive evidence of material inconsistencies in either risk rankings or the underlying risk measures, no assessment rate adjustment will be made.

Comments on Guideline 6

A comment from a large banking organization indicates that in order to gauge the significance of an outlier condition, one would need to know the relative levels of the risk indicator being measured in addition to the differences in risk rankings along that measure. The FDIC acknowledges that for a given risk indicator, differences in risk rankings across institutions could represent either a material or an immaterial difference in risk. Although, in general, adjustments would only be considered when a preponderance of risk information indicates the need for an adjustment, the FDIC agrees that it is important to consider both the differences in risk rankings and the magnitude of differences in underlying risk measures, and has revised Guideline 6 accordingly.

Other Comments on Analytical Guidelines 1 Through 6

A comment from a large banking organization supported the guidelines as well reasoned, comprehensive, and consistent with other assessment frameworks used by credit rating agencies and credit risk analyses processes used within many financial institutions. The commenter suggests that the FDIC consider the inclusion of certain additional risk factors in the analytical processing such as the diversification and volatility of earnings from major business lines, and the level of net charge-offs to pre-provision earnings. The FDIC agrees with these suggestions and has modified the risk factors in the Appendix accordingly.

A comment from a trade organization objected to the blanket inclusion of “commercial real estate” in the definition of one of the risk factors included in the Appendix entitled higher risk loans to tier 1 capital. The FDIC agrees that risks associated with commercial real estate lending can vary considerably depending on such factors as property type, collateral, the degree of pre-leasing, etc. As with any of the measures listed in the Appendix, the FDIC does not consider any single financial ratio as representative of an institution’s risk profile. Rather, each set of financial performance factors is accompanied by a description of qualitative and mitigating risk considerations. More specifically, the qualitative considerations accompanying the asset quality measures in the Appendix indicate that the FDIC will consider mitigating factors, including the degree of collateral coverage and differences in underwriting standards, when evaluating credit risks related to commercial real estate holdings. These second-order considerations, coupled with any additional information obtained pertaining to the specific risk characteristics of a given portfolio, will help better distinguish the risk contained within any commercial real estate concentrations.

A comment from a large banking organization recommends that the FDIC’s risk ranking analyses be performed without respect to the assessment rate floors in effect for large Risk Category I institutions (i.e., the risk rankings encompassing approximately the 1st through the 46th percentile). The FDIC agrees that the application of the assessment rate floor to the ranking of risk factors results in some loss of information about the magnitude of differences in risk rank levels between institutions in the peer group. Accordingly, the FDIC will initially assign risk rankings to risk measures without respect to how these percentile rankings align with the assessment rate floor. However, the FDIC will continue to view a rank ordering analysis that supports an overall assessment rate risk ranking falling approximately between the lowest 1st and 46th percentiles, as being indicative of minimum risk. The FDIC does not believe this modification to risk ranking comparisons will alter the resulting assessment rate decisions from the analytical process described in the proposed guidelines.

Control Guidelines

Guideline 7: Decisions to adjust an institution’s assessment rate must be well supported.

The FDIC will perform internal reviews of pending adjustments to an institution’s assessment rate to ensure the adjustment is justified, well supported, based on the most current information available, and results in an adjusted assessment rate that is consistent with rates paid by other institutions with similar risk profiles.

Comments on Guideline 7

One comment, the joint letter, agreed that adjustment decisions should be well supported by the preponderance of factors that suggest a change is required. The FDIC believes the final guidelines establish an analytical process and controls over that process that are consistent with this comment.

Guideline 8: The FDIC will consult with an institution’s primary federal regulator and appropriate state banking supervisor prior to making any decision to adjust an institution’s initial assessment rate (or prior to removing a previously implemented adjustment). Participation by the primary federal regulator or state banking supervisor in this consultation process should not be construed as concurrence with the FDIC’s deposit insurance pricing decisions.

Consistent with existing practices, the FDIC will continue to maintain an ongoing dialogue with primary federal regulator concerning large institution risks. When assessment rate adjustments are contemplated, the FDIC will notify the primary federal regulator and the appropriate state banking supervisor of the pending adjustment in advance of the first opportunity to implement any adjustment. This notification will include a discussion of why the adjusted assessment rate is more consistent with the risk profiles...
Comments on Guideline 8

A comment from a trade organization indicates that the guidelines do not apply a significant and explicit weight to the views of the primary federal regulator. The FDIC agrees that its adjustment decisions should weigh heavily the views of the primary federal regulator, as well as the views of the appropriate state banking supervisor. As noted under Guideline 1, the intent of any assessment rate adjustment is not to override supervisory evaluations. Rather, the consideration of additional risk information is meant to ensure that assessment rates, produced from a combination of supervisory ratings and agency ratings or supervisory ratings and financial ratios (when applicable), result in a reasonable rank ordering of risk. Guideline 8 also indicates that no adjustment decision will be made until the FDIC consults with the primary federal regulator and the appropriate state banking supervisor. If the primary federal regulator or state banking supervisor choose to express a view on the appropriateness of the adjustment, the FDIC will accord such views significant weight in its decision of whether to proceed with an adjustment.

Guideline 9: The FDIC will give institutions advance notice of any decision to make an upward adjustment to its initial assessment rate, or to remove a previously implemented downward adjustment.

The FDIC will notify institutions when it intends to make an upward adjustment to its initial assessment rate (or remove a downward adjustment). This notification will include the reasons for the adjustment, when the adjustment would take effect, and provide the institution up to 60 days to respond. Adjustments would not become effective until the first assessment period after the assessment period that prompted the notification of an upward adjustment. During this subsequent assessment period, the FDIC will determine whether an adjustment is still warranted based on an institution’s response to the notification. The FDIC will also take into account any subsequent changes to an institution’s weighted average CAMELS, long-term debt issuer ratings, financial ratios (when applicable), or other risk measures used to support the adjustment. In other words, both an adjustment determination and a determination of the amount of the adjustment will be made with respect to information and risk factors pertaining to the assessment period being assessed—that is, the first assessment period after the assessment period that prompted the notification. The FDIC will also consider any actions taken by the institution, during the period for which the institution is being assessed, in response to the FDIC’s concerns described in the notice.

Comments on Guideline 9

One comment, the joint letter, supported this advance notification requirement for upward adjustments, which will give institutions an opportunity to respond to and address the FDIC’s concerns.

Guideline 10: The FDIC will continually re-evaluate the need for an assessment rate adjustment.

The FDIC will re-evaluate the need for the adjustment during each subsequent quarterly assessment period. These evaluations will be based on any new information that becomes available, as well as any changes to an institution’s weighted average CAMELS, long-term debt issuer ratings, financial ratios (when applicable), or other risk measures used to support the adjustment. Re-evaluations will also consider the appropriateness of the magnitude of an implemented adjustment, for example, in cases where changes to the initial assessment rate inputs result in a change to the initial assessment rate. Consistent with Guideline 9, the FDIC will not increase the magnitude of an adjustment without first notifying the institution of the proposed increase.

The institution can request a review of the FDIC’s decision to adjust its assessment rate. It would do so by submitting a written request for review of the assessment rate assignment, as adjusted, in accordance with 12 CFR 327.4(c). This same section allows an institution to bring an appeal before the FDIC’s Assessment Appeals Committee if it disagrees with determinations made in response to a submitted request for review.

The FDIC received no specific comment on Guideline 10.

Comments on Control Guidelines

One comment, the joint letter, indicated that institutions should have the opportunity to petition the FDIC for a reduction in assessment rates. The commenter argues that the guidelines only allow the FDIC to initiate changes in assessment rates, and that institutions may have evidence of lower risk that is not captured in either the initial assessment rate or the risk information considered for purposes of determining whether an adjustment is appropriate.

The FDIC believes that the final guidelines, coupled with existing assessment rate rules, give institutions a number of opportunities to argue for lower assessment rates. For instance, institutions have 90 days from the date of receiving an assessment rate invoice to request a review of that rate. This request for review procedure is available whether or not an adjustment is reflected in the assessment rate. Additionally, institutions can appeal decisions made in response to these requests for review to the FDIC’s Assessment Appeals Committee.

Another comment from a large banking organization argues that the guidelines should include a greater level of due process for upward adjustments than is available under the existing Assessment Rule to include the opportunity to present counter arguments. The FDIC believes the guidelines provide multiple such opportunities, which are consistent in many respects with the commenter’s recommendation. First, an institution will receive advance notification of the FDIC’s grounds for considering an upward adjustment. At this point, an institution will have the opportunity to provide information that challenges the appropriateness of an upward assessment rate adjustment. Second, once the FDIC has considered an institution’s response to the advance notice of a pending upward adjustment, the FDIC will provide the institution with a written response and rationale for any decision to proceed with the upward adjustment. At this point, the institution will have an opportunity to request a review of a decision to impose a higher assessment rate and will be able to present evidence to challenge the decision in accordance with the Assessment Rule. Third, an institution

13 Any requests for review or appeals would be subject to the limitations contained within the Assessment Rule, namely that assessment rate adjustments would be limited to no more than ½ basis point, and that no adjustment may cause an institution’s rate to fall below the minimum assessment rate or rise above the maximum assessment rate in effect for a given assessment period.
will be able to appeal the outcome of this request for review to the FDIC’s Assessment Appeals Committee. In short, institutions will have multiple opportunities to dispute an upward adjustment, and the institution’s position will be considered at increasingly higher levels within the Corporation. The FDIC believes it is neither necessary nor appropriate for it to provide for third party review of decisions made by the FDIC under its statutory authority.

Other Comments on the Guidelines
Incorporation of Basel II Information Into Assessment Rate Adjustment Decisions

One comment, from a large banking organization, recommends that the FDIC table its guidelines pending finalization of rulemaking for the new risk-based capital framework (Basel II). The commenter argues that a risk-differentiation system using Basel II information may produce different results than a system that does not incorporate this information.

The underlying objective of the guidelines is to evaluate all available information for purposes of ensuring a reasonable and consistent rank ordering of risk. The FDIC does not believe that the adoption of Basel II will produce information that conflicts with the risk information being evaluated as part of these guidelines. Rather, the FDIC believes that risk information obtained from advanced risk measurement systems should serve to complement the analysis process described in these final guidelines.

Considerations of Parent Company or Affiliate Support

Two comments (the joint letter and a large banking organization) recommended that the FDIC consider parent company support in its assessment rate adjustment determinations. Both comments suggested that the existence of a financially strong parent should be a consideration only in reducing rates.

The FDIC believes it is appropriate to take into account all available information in its assessment rate adjustment decisions. Accordingly, the FDIC will consider both the willingness and ability of a parent company to support an insured institution in its adjustment decisions. The willingness of a company to support an insured subsidiary can be evaluated through a review of a company’s financial strength, supervisory and debt ratings, market-based views of risk, and a review of the company’s operating environment and affiliate structure. Although the FDIC will take into account considerations of parent company support, these considerations will not be accorded any greater or lesser weight than other risk considerations. Rather, these considerations will be evaluated in conjunction with the analysis of other risk measures as indicated in the final guidelines. Because many institutions’ initial assessment rates already reflect considerations of parent company support (when it is subject to the debt rating method), the FDIC does not believe it would be appropriate to automatically lower an institution’s assessment rate when an institution is owned by a financially strong parent.

Considerations of Additional Supervisory Information

The proposed guidelines posed a question about whether the FDIC should consider certain additional supervisory information when determining whether a downward adjustment in assessment rates is appropriate. In response to this question, one comment, the joint letter, indicated that only risk-related considerations should be reflected in assessment rate adjustments. More specifically, the commenter argues that technical violations that the commenter believes do not relate to the risk of failure should not preclude a downward assessment rate adjustment.

The FDIC believes that its assessment rate adjustment decisions should be based on risk-related considerations and will incorporate all available supervisory information that has a bearing on the risks posed to the insurance funds into its adjustment decisions.

Disclosure of Assessment Rate Adjustments

One comment, the joint letter, recommends that the FDIC disclose the number (but not the names) of institutions whose assessment rate adjustments have been adjusted and the magnitude of these adjustments. This same comment indicates that it would be appropriate to give the results of the FDIC’s analysis, each time it is performed, to each large Risk Category I institution in order to enhance the dialogue between the FDIC and the institution.

The FDIC plans to provide information about the number of and amount of implemented assessment rate adjustments. The FDIC also intends to determine the appropriate form and extent of analytical results pertaining to its adjustment decisions that will be given to large Risk Category I institutions. At a minimum, the FDIC intends to provide institutions with a summary of its analyses in cases where an adjustment is contemplated.

Need for Further Notice and Comment on Future Modifications

One comment, the joint letter, believes that any modification in the risk factors considered in the adjustment decision should be subject to further notice and comment. The FDIC believes it would be impractical and inefficient to subject every modification in the risk factors considered as part of the adjustment analysis process to further notice and comment. As noted in the proposed guidelines, the risk measures listed in the Appendix are not intended to be either an exhaustive or a static representation of all risk information that might be considered in adjustment decisions. Rather, the list identified what the FDIC believes at this time to be the most important risk elements to consider in its assessment rate adjustment determinations. These elements are likely to change and evolve over time due to changes in reported financial variables (e.g., Call Report changes) and changes in access to new types of risk information. The FDIC believes it is appropriate to seek additional notice and comment for material changes in the methodologies or processes used to make assessment rate adjustment decisions. A material change would be one that is expected to result in a significant change to the frequency of assessment rate adjustments.

Relationship Between Adjustment Decisions and Revenues

A comment from a large banking organization suggests that the lack of transparency in the guidelines give the appearance that the FDIC intends to extract additional premiums from large institutions. To avoid this appearance, the commenter recommends that the FDIC impose revenue neutrality on its adjustment decisions by implementing upward adjustments in amounts not greater than the amount of downward adjustments. The FDIC has no intent to use its adjustment authority for revenue generation purposes. The guidelines are intended to provide as much

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12 Moody’s and Fitch debt issuer ratings explicitly take into account parent company support.
reflect the upward adjustment. Advance notice of a pending upward adjustment, approximately to the invoice date for an assessment period, is needed to be reduced or increased (subject to the 1/2 basis point limitation and the requirement for further advance notification). 14

Downward Adjustments

Decisions to lower an institution’s assessment rate will not be communicated to institutions in advance. Rather, they would be reflected in the invoices for a given assessment period along with the reasons for the adjustment. Downward adjustments may take effect as soon as the first insurance collection for the January 1st through March 31, 2007 assessment period subject to timely approval of the guidelines by the Board of the FDIC. Downward adjustments will remain in effect for subsequent assessment periods until the FDIC determines either that the adjustment is no longer warranted or that the magnitude of the adjustment needs to be increased (subject to the 1/2 basis point limitation) or lowered (subject to advance notification). 15

Appendix—Examples of Risk Measures that Will Be Considered in Assessment Rate Adjustment Determinations 16

Broad-based Risk Measures

• Composite and weighted average CAMELS ratings: The composite rating assigned to an insured institution under the Uniform Financial Institutions Rating System and the weighted average CAMELS rating determined under the Assessments Regulation.

• Long-term debt issuer rating: A current, publicly available, long-term debt issuer rating assigned to an insured institution by Moody’s, Standard & Poor’s, or Fitch.

• Financial ratio measure: The assessment rate determined for large Risk Category 1 institutions without long-term debt issuer ratings, using a combination of weighted average CAMELS ratings and five financial ratios as described in the Assessments Regulation.

• Offsite ratings: Ratings or numerical risk rankings, developed by either supervisors or industry analysts, that are based primarily on off-site data and incorporate multiple measures of insured institutions’ risks.

• Other agency ratings: Current and publicly available ratings, other than long-term debt issuer ratings, assigned by any rating agency that reflect the ability of an institution to perform on its obligations. One such rating is Moody’s Bank Financial Strength Rating BFSR, which is intended to provide creditors with a measure of a bank’s intrinsic safety and soundness, excluding considerations of external support factors that might reduce default risk, or country risk factors that might increase default risk.

• Loss severity measure: An estimate of insurance fund losses that would be incurred in the event of failure. This measure takes into account such factors as estimates of insured and non-insured uninsured funding, estimates of obligations that would be subordinated to depositor claims, estimates of obligations that would be secured or would otherwise take priority claim over depositor claims, the estimated value of foreign assets, prospects for “ring-fencing” whereby foreign assets are used to satisfy foreign obligor claims over FDIC claims, and other factors that could affect resolution costs.

Financial Performance and Condition Measures

Profitability

• Return on assets: Net income (pre- and post-tax) divided by average assets.

• Return on risk-weighted assets: Net income (pre- and post-tax) divided by average risk-weighted assets.

• Core earnings volatility: Volatility of quarterly earnings before tax, extraordinary items, and securities gains (losses) measured over one, three, and five years.

• Net interest margin: Interest income less interest expense divided by average earning assets.

• Earning asset yield: Interest income divided by average earning assets.

• Funding cost: Interest expense divided by interest bearing obligations.

• Provision to net charge-offs: Loan loss provisions divided by losses applied to the loan loss reserve (net of recoveries).

• Burden ratio: Overhead expenses less non-interest revenues divided by average assets.

• Qualitative and mitigating profitability factors: Includes considerations such as earnings prospects, diversification of revenue sources by business line and source, and the volatility of earnings from principal business lines.

Capitalization

• Tier 1 leverage ratio: Tier 1 capital for Prompt Corrective Action (PCA) divided by adjusted average assets as defined for PCA.

• Tier 1 risk-based ratio: Tier 1 capital divided by risk-weighted assets.

13 Since the intent of the notification is to provide advance notice of a pending upward adjustment, the invoice covering the assessment period January 1st through March 31st in this case would not reflect the upward adjustment.

14 The timeframes and example illustrated here would also apply to a decision by the FDIC to remove a previously implemented downward adjustment as well as a decision to increase a previously implemented upward adjustment (the increase could not cause the total adjustment to exceed the 0.50 basis point limitation).

15 As noted in the Assessments Regulation, the FDIC may raise an institution’s assessment rate without notice if the institution’s supervisory or agency ratings or financial ratios (for institutions without debt ratings) deteriorate.

16 This listing is not intended to be exhaustive but represents the FDIC’s view of the most important risk measures that should be considered in the assessment rate determinations of large Risk Category 1 institutions. This listing may be revised over time as improved risk measures are developed through an ongoing effort to enhance the FDIC’s risk measurement and monitoring capabilities.
• Total risk-based ratio: PCA total capital divided by risk-weighted assets.
• Tier 1 growth to asset growth: Annual growth of PCA tier 1 capital divided by annual growth of total assets.
• Regulatory capital to internally determined capital needs: PCA tier 1 and total capital divided by internally-determined capital needs as determined from economic capital models, internal capital adequacy assessments processes (ICAAP), or similar processes.
• Qualitative and mitigating capitalization factors: Includes considerations such as strength of capital planning and ICAAP processes, and the strength of financial support provided by the parent.

**Asset Quality**

• Non-performing assets to tier 1 capital: Nonaccrual loans, loans past due over 90 days, and other real estate owned divided by PCA tier 1 capital.
• ALLL to loans: Allowance for loan and lease losses plus allocated transfer risk reserves divided by total loans and leases.
• Net charge-off rate: Loan and lease losses charged to the allowance for loan and lease losses (loss recoveries) divided by average total loans and leases.
• Earnings coverage of net loan losses: Loan and lease losses charged to the allowance for loan and lease losses (less recoveries) divided by pre-tax, pre-loan loss provision earnings.
• Higher risk loans to tier 1 capital: Sum of sub-prime loans, alternative or exotic mortgage products, leveraged lending, and other high risk lending (e.g., speculative construction or commercial real estate financing) divided by PCA tier 1 capital.
• Criticized and classified assets to tier 1 capital: Assets assigned to regulatory categories of Special Mention, Substandard, Doubtful, or Loss (and not charged-off) divided by PCA tier 1 capital.
• EAD-weighted average PD: Weighted average estimate of the probability of default (PD) for an institution’s obligors where the weights are the estimated exposures-at-default (EAD). PD and EAD risk metrics can be defined using either the Basel II framework or internally defined estimates.
• EAD-weighted average LGD: Weighted average estimate of loss given default (LGD) for an institution’s credit exposures where the weights are the estimated EADs for each exposure. LGD and PD risk metrics can be defined using either the Basel II framework or internally defined estimates.
• Qualitative and mitigating asset quality factors: Includes considerations such as the extent of credit risk mitigation in place, underwriting trends, strength of credit risk monitoring, and the extent of securitization, derivatives, and off-balance sheet financing activities that could result in additional credit exposure.

**Liquidity and Market Risk Indicators**

• Core deposits to total funding: The sum of demand, savings, MMDA, and time deposits under $100 thousand divided by total funding sources.
• Net loans to assets: Loans and leases (net of the allowance for loan and lease losses) divided by total assets.
• Liquid and marketable assets to short-term obligations and certain off-balance sheet commitments: The sum of cash, balances due from depository institutions, marketable securities (fair value), federal funds sold, securities purchased under agreement to resell, and liquidity marketable loans (e.g., securitized mortgage pools) divided by the sum of obligations maturing within one year, undrawn commercial and industrial loans, and letters of credit.
• Qualitative and mitigating liquidity factors: Includes considerations such as the extent of back-up lines, pledged assets, the strength of contingency and funds management practices, and the stability of various categories of funding sources.

**Other Market Indicators**

• Subordinated debt spreads: Dealer-provided quotes of interest rate spreads paid on subordinated debt issued by insured subsidiaries relative to comparable maturity treasury obligations.
• Credit default swap spreads: Dealer-provided quotes of interest rate spreads paid by a credit protection buyer to a credit protection seller relative to a reference obligation on an insured institution.
• Market-based default indicators: Estimates of the likelihood of default by an insured organization that are based on either traded equity or debt prices.
• Qualitative market indicators or mitigating market factors: Includes considerations such as agency rating outlooks, debt and equity analyst opinions and outlooks, the relative level of liquidity of any debt and equity issues used to develop market indicators defined above, and market-based indicators of the parent company.

**Risk Measures Pertaining to Stress Conditions**

**Ability To Withstand Stress Conditions**

• Concentration risk measures: Measures of the level of concentrated risk exposures and extent to which an insured institution’s capital and earnings would be adversely affected due to exposures to common risk factors such as the condition of a single obligor, poor industry sector conditions, poor local or regional economic conditions, or poor conditions for groups of related obligors (e.g., subprime borrowers).
• Qualitative and mitigating factors relating to the ability to withstand stress conditions: Includes results of stress tests or scenario analyses that measure the extent of capital, earnings, or liquidity depletion under varying degrees of financial stress such as adverse economic, industry, market, and liquidity events as well as the comprehensiveness of risk identification and stress testing analyses, the plausibility of stress scenarios considered, and the sensitivity of scenario analyses to changes in assumptions.

**Loss Severity Indicators**

• Subordinated liabilities to total liabilities: The sum of obligations, such as subordinated debt, that would have a subordinated claim to the institution’s assets in the event of failure divided by total liabilities.
• Secured (priority) liabilities to total liabilities: The sum of claims, such as trade payables and secured borrowings, that would have priority claim to the institution’s assets in the event of failure divided by total liabilities.
• Foreign assets relative to foreign deposits: The sum of assets held in foreign units relative to foreign deposits.
• Liquidation value of assets: Estimated value of assets, based largely on historical loss rates experienced by the FDIC on various asset classes, in the event of liquidation.
• Qualitative and mitigating factors relating to loss severity: Includes considerations such as the sufficiency of information and systems capabilities relating to qualified financial contracts and deposits to facilitate quick and cost efficient resolution, the extent to which critical functions or staff are housed outside the insured entity, and prospects for foreign deposit ring-fencing in the event of failure.

By order of the Board of Directors.
Dated at Washington, DC, this 8th day of May, 2007.
Federal Deposit Insurance Corporation.
Robert E. Feldman,
Executive Secretary.