INDEPENDENT COMMUNITY
BANKERS of AMERICA

November 14, 2007

Robert E. Feldman
Executive Secretary
Attention: Comments
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, D.C. 20429

Re: Assessment Dividends: Advance Notice of Proposed Rulemaking

Dear Mr. Feldman:

The Independent Community Bankers of America (ICBA)[1] appreciates the opportunity to offer comments in connection with the Federal Deposit Insurance Corporation's proposals for allocating assessment dividends. The Federal Deposit Insurance Reform Act of 2005 (Reform Act) requires the FDIC to pay dividends to insured banks if the reserve ratio at the end of a calendar year for Deposit Insurance Fund (DIF) exceeds 1.35%. Above 1.35%, the FDIC generally must dividend out half of the excess and if the reserve ratio exceeds 1.50%, it must pay out the entire excess. In its Advance Notice of Proposed Rulemaking (ANPR), the FDIC is soliciting comments on various ways of allocating dividends if the FDIC is required to pay one under the Reform Act.

Summary of ICBA's Position

ICBA believes that the FDIC should manage the DIF so that the reserve ratio rarely exceeds 1.35% and dividend payments are avoided. By conservatively managing the DIF and in the near term gradually increasing its balances over a three to five year period to

[1]*The Independent Community Bankers of America represents 5,000 community banks of all sizes and charter types throughout the United States and is dedicated exclusively to representing the interests of the community banking industry and the communities and customers we serve. ICBA aggregates the power of its members to provide a voice for community banking interests in Washington, resources to enhance community bank education and marketability, and profitability options to help community banks compete in an ever-changing marketplace.*

With nearly 5,000 members, representing more than 18,000 locations nationwide and employing over 268,000 Americans, ICBA members hold more than $908 billion in assets, $726 billion in deposits, and more than $619 billion in loans to consumers, small businesses and the agricultural community. For more information, visit ICBA's website at www.icba.org.

reach the current DRR of 1.25%, we believe that assessments can remain low and steady and the FDIC can avoid having to pay dividends and employing a dividend allocation method that may unfairly favor one set of institutions over another.

Since deposit growth has slowed considerably since the first quarter of 2007 and the DIF reserve ratio has already reached 1.22%, we recommend that assessments be lowered for 2008 so that they would be at or close to the base schedule of assessments which is now at 2-4 basis points for Risk Category I institutions. Next year should be another period of transition to allow banks to gradually use up their one-time assessment credits and to adjust to paying premiums again under the new risk-based assessment system.

Each method of allocating dividends proposed in the ANPR has advantages and disadvantages for community banks. The fund balance method stresses the contribution that older banks made to the fund prior to 1997 and has the advantage of automatically allocating dividends from year to year whereas the payments method would consider more of the contribution that banks have recently made to the DIF and would be relatively easier to administer.

ICBA does not endorse specifically either the payments method or the fund balance method for allocating dividends but does believe that the FDIC should use a method or a combination of methods that considers each bank's total contribution to the DIF in accordance with the statutory requirements of the Reform Act. It is essential for the FDIC to choose a method that recognizes the importance of contributions that older institutions made to the DIF prior to 1997, and that takes into account contributions that newer institutions have made to the fund..

ICBA believes that whatever allocation method that is chosen should be simple enough for the FDIC to use from year to year, clear enough so that all its attributes are spelled out, and not subject to sudden or unexpected changes. We therefore recommend against a method that would permit constant FDIC intervention and decision making. Any method that is chosen should be clearly delineated and future changes to the method, including changes to the relative weight of the factors involved in the allocation method or in the period of time used to determine premium payments, should be subject to notice and comment rulemaking by the FDIC.

With respect to the definition of an "eligible" premium, we favor the third option suggested in the ANPR which would mean that institutions would be credited for premiums charged up to the maximum rate for a Risk Category I institution.

Background and Proposal

The Reform Act requires the FDIC to prescribe by regulation the method for the payment of dividends from the Deposit Insurance Fund or DIF. As noted above, if the DIF reserve ratio rises above 1.35% of insured deposits, the FDIC must dividend out half of the excess and if the DIF rises above 1.5% of insured deposits, the FDIC must pay out the entire excess. For purposes of determining a payment method, the Reform Act says that the FDIC is to take into account (1) an institution's assessment base at the end of 1996 (the last year premiums were assessed) compared to the total assessment base at the end of 1996, (2) assessments paid since 1996, and (3) amounts paid for higher risk. However, the FDIC has broad discretion in determining the proper balance of these factors.

In its ANPR, the FDIC is proposing two general approaches to allocating dividends—the fund balance method and the payments method. The two different methods differ in the way they balance the statutory factors described above and thus in the way each method treats older institutions (e.g., those chartered before 1997) versus newer institutions (e.g., those chartered since 1997).

Under the fund balance method, each bank's share of dividends would be based on its share of the fund balance expressed as a percentage. Under the basic form of the fund balance method, a bank's share of dividends would include its portion of the 1996 assessment base (as a proxy for assessments paid before 1997) and would take account of premiums paid going forward. Returns on investments and ineligible premiums would tend to increase allocations whereas fund losses, operating expenses, and dividends paid out would tend to decrease allocations.

If the FDIC chose this method, it would not have to make further decisions about how to allocate dividends between older and newer institutions. Absent large and continuing fund losses, the fund balance method would likely benefit older institutions for decades while newer institutions would take decades to obtain a relatively similar share of dividends**.**

Under the "payments method," each bank's share of dividends would depend on its premium payments to FDIC over some period of time. Because the FDIC could vary the period of time that premiums payments would be considered, the payments method could be structured to benefit older institutions for many years, or it could be structured to put newer institutions on an equal footing quickly.

ICBA's Position

Industry consensus on a dividend allocation method will be difficult to achieve since most banks will prefer the method that favors their institution depending on whether they are older institutions or newer institutions. To avoid employing a dividend allocation method that may unfairly favor one set of institutions over another, **ICBA believes that the FDIC should manage the DIF so that the reserve ratio rarely exceeds 1.35% and dividend payments are avoided**. In our letter to the FDIC concerning the proposal to establish the DRR at 1.25% for 2007 [2], we recommended that the FDIC use the maximum flexibility it has under the Reform Act to keep premiums small and build up DIF reserves to meet the designated reserve ratio steadily and gradually over a three- to five-year period to avoid unnecessarily high assessment rates. One advantage of gradually increasing the DIF reserves is that the FDIC can avoid overshooting its goal and significantly exceeding the DRR which has been established for next year as 1.25%. By conservatively managing the DIF and gradually increasing its balances, the FDIC can avoid ever having to pay dividends.

[2] See our letter dated September 22, 2006 concerning the FDIC proposal to establish the DRR at 1.25%.

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Since deposit growth has slowed considerably since the first quarter of 2007 and the DIF reserve ratio has already reached 1.22%, we recommend that assessments be lowered for 2008 from the 5-7 basis points for Risk Category I institutions so that they would be at or close to the base schedule of assessments which has been established as 2-4 basis points for Risk Category I institutions. We expect that the slower housing market will impede growth in the overall economy next year resulting in a continuation of stagnant deposit growth. Even though there have been two recent bank failures, we still believe that the DIF risk exposure will remain low enough next year that losses will not significantly affect the reserve ratio. ICBA also believes that 2008 should be another period of transition to allow banks to gradually use up their one-time assessment credits and to adjust to paying premiums again under the new risk-based assessment system.

Each method of allocating dividends proposed in the ANPR has advantages and disadvantages for community banks. The fund balance method stresses the contribution that older banks made to the fund prior to 1997 and has the advantage of automatically allocating dividends from year to year without any need for further decision making about the relative importance to assign the 1996 assessment base compared to post-1996 premiums. Absent significant fund losses, each bank's share of the fund would also not change much from year to year so that banks could predict how much a dividend they would receive. The main disadvantage with the fund balance method is that it would take years for newer institutions to catch up with older institutions.

The payments method, on the other hand, would consider more of the contribution that banks have recently made to the DIF and would be relatively easier to administer, particularly if only the most recent payments were considered (e.g., those made in the last three to five years). The payments method would require less data to administer than the fund balance method and dividends would be less affected by fund gains and losses.

Unlike the fund balance method, the FDIC would also have considerably more options regarding the allocation of dividends between older and newer institutions. The FDIC would have to determine (1) how much weight to accord the 1996 assessment base compared to premiums paid under the new system; (2) whether that weight should change over time, and (3) whether all payments under the new system should be considered or only more recent payments. The main disadvantages of the payments method is that contributions made prior to 1997 would not have as much weight as under the fund balance method and the FDIC might retain too much flexibility with regard to allocating dividends, potentially resulting in inconsistent dividend allocations from year to year.

While ICBA does not specifically endorse any particular method of allocation, the FDIC should use a method or a combination of methods that considers each bank's contribution to the DIF both before 1997 and after 1996 and is in accordance with the statutory requirements of the Reform Act. The statute requires that the FDIC take into account (1) an institution's assessment base at the end of 1996 (the last year premiums were assessed) compared to the total assessment base at the end of 1996, (2) assessments paid since 1996, and (3) amounts paid for higher risk. We believe that a method that recognizes the importance of contributions that older institutions made to the DIF prior to 1997 when assessment rates were often high is essential. However, the FDIC should adopt some method that also takes into account contributions that newer institutions have made to the fund.

ICBA believes that whatever allocation method that is chosen should be simple enough for the FDIC to use from year to year, detailed enough so that community banks understand clearly all its attributes, and not subject to sudden or unexpected changes. We recommend against a method that would permit constant FDIC intervention and decision making as to how to allocate the weight of the 1996 assessment base versus the payments that institutions have made to the DIF since 1996. The method adopted should be sufficiently delineated, and future changes, including changes to the relative weight of the factors involved in the allocation method or in the period of time used to determine premium payments, should be subject to require further notice and comment rulemaking. For instance, if some variation of the payments method was chosen and a payment period was determined, than the FDIC would have to issue a notice of proposed rulemaking and provide time for a comment period prior to changing the payment period.

With respect to the definition of an “eligible” premium, ICBA favors a method that is somewhere between the total premium amount actually paid by an institution and the lowest amount charged a Risk Category I institution. **The third option in the ANPR is preferable where institutions would be credited for premiums charged up to the maximum rate for a Risk Category I institution.** Since approximately 95% of banks are Risk Category I institutions, this option would result in most institutions being credited for the full amount that they pay as a premium. However, this option has the advantage of providing additional incentive as required under the statute to those 5% of institutions that are not Risk Category I institutions to reduce their risk and therefore the amount they are charged for premiums.

Conclusion

ICBA believes that the FDIC should manage the DIF so that the reserve ratio rarely exceeds 1.35% and dividend payments are avoided. In the near term, we recommend that the FDIC use the maximum flexibility it has under the Reform Act to build up DIF reserves to meet the designated reserve ratio steadily and gradually over a three- to five-year period to avoid unnecessarily high assessment rates. For 2008, since deposit growth has slowed considerably since the first quarter of 2007 and the DIF reserve ratio has already reached 1.22%, we recommend that assessments be lowered so that they are at or close to the base schedule of assessments which has been established as 2-4 basis points for Risk Category I institutions.

ICBA does not endorse specifically either the payments method or the fund balance method for allocating dividends. The FDIC should use a method or a combination of methods that considers each bank’s total contribution to the DIF in accordance with the statutory requirements of the Reform Act. While it is essential for the FDIC to choose a method that recognizes the importance of contributions that older institutions made to the DIF prior to 1997, the FDIC should also consider a method that takes into account contributions that newer institutions have made to the fund. ICBA believes that whatever allocation method is chosen should be simple enough for the FDIC to use from year to year, clear enough so that all its attributes are spelled out, and not subject to sudden or unexpected changes. We would therefore recommend against using a method that would require or permit constant FDIC intervention and decision making without notice and comment.

ICBA appreciates the opportunity to offer comments in connection with the FDIC's proposals for allocating assessment dividends. If you have any questions about our letter, please do not hesitate to contact me at 202-659-8111 or Chris.Cole@icba.org.

Sincerely,

Christopher Cole

Christopher Cole

Regulatory Counsel