FDIC views on HR 4879 - to exempt IBFs from Coverage

Statement by

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on

H.R. 4879 - A Bill to amend the Federal Deposit Insurance Act to clarify the treatment of international banking facility deposits for purposes of deposit insurance assessments.

Presented to

Subcommittee on Financial Institutions Supervision, Regulation and Insurance
of the
Committee on Banking, Finance and Urban Affairs
House of Representatives

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Mr. Chairman, I appreciate the opportunity to appear this morning on behalf of the FDIC to present our views on the Bill which would exempt deposits in IBF's from deposit insurance coverage and assessments. The Corporation favors enactment of the bill with two qualifying comments.

First, certain technical amendments are necessary to make clear that the FDIC, as the insuring agency, is the proper party to determine which obligations should not be insured. The amendments also would authorize the Corporation to issue regulations requiring insured banks to identify to the public any of their uninsured obligations, including IBF obligations, that may cause confusion to the public with respect to their insured status. The proposed amendments are attached.

Second, we believe that the current statutory framework for assessing deposits of insured banks deserves a comprehensive review by the Congress at an early date. For this reason, this bill should be adopted with a sunset provision not to exceed two years from the date of enactment.

In reviewing the Corporation's legislative history, we note that Congress in 1935 addressed the issue of assessing deposits held in foreign offices of U.S. banks (Hearings before the Committee on Banking and Currency, House of Representatives, 74th Congress, 1st Sess., on H.R. 5357, pp. 71-72). Congress deliberately omitted such a provision on the grounds that the additional operating cost of insurance would place U.S. banks at a competitive disadvantage vis-a-vis their foreign bank counterparts. Although not explicitly

stated in the legislative history, we can surmise that foreign office activities of U.S. banks were minimal and this omission did not represent a large loss of assessment revenue. Over the last two decades, the international activities of U.S. banks have grown dramatically. At year-end 1980, assets in foreign offices represented a significant 17.4 percent of consolidated assets of the banking system. When considering the overall risk of an individual bank, all activities, domestic and foreign, must be included in evaluating the potential exposure of the Corporation in the event of bank failure. Under the current statutory framework, the Corporation is precluded from basing its premium on all the activities of an institution because assessments are limited solely to domestic deposits.

When we consider the customary remedies used by the Corporation in resolving financial difficulties of failing banks, the current assessment mechanism becomes more difficult to rationalize. As you know, when a bank encounters financial difficulty or fails, the Corporation has several options for resolving the situation. One option is to pay off insured depositors up to the statutory maximum. Under this procedure, depositors with balances in excess of $100,000, other general creditors of the bank and, if applicable, foreign office depositors would share pro rata with the Corporation the proceeds of the failed bank receivership estate.

In lieu of a deposit payoff, the Corporation has increasingly utilized remedies available under Section 13(c) "direct assistance" and 13(e) "purchase and assumption" of the FDI Act, particularly in the case of large banks which are likely to have foreign offices. In these instances, the Corporation must by statute determine that the transaction "will reduce the risk or avert a threatened loss" to the FDIC (Section 13(e)) or render a finding that the institution is "essential" to its community (Section 13(c)). Under either procedure, uninsured creditors, including foreign office depositors and other general creditors, directly benefit. While we cannot state definitely because of the statutory tests that all large bank failures would be handled under Sections 13(c) or 13(e), there is a high probability of using either of these methods. Given this hypothesis, it seems incongruous that an assessment premium is not exacted for the implied coverage afforded by the Corporation.

Our position of favoring enactment of the pending bill is largely predicated on the argument that under current law U.S. banks may face competitive obstacles due to the fact that many foreign banks would operate IBFs without deposit insurance coverage. As such, these institutions do not face assessment costs which could make serious inroads to the profitability of business conducted by IBFs. We believe this competitive imbalance should be addressed promptly while more permanent solutions are sought.

The Corporation's staff has already begun analysis of the issues raised herein, and we hope to bring these matters to the attention of the Congress at an early date. We are currently engaged in a variety of studies relating to risk-related insurance premiums, co-insurance of larger accounts, and related matters. Our ultimate objective is to find ways, if possible, to induce public confidence in our institutions based on management policies and individual institution performance rather than having the public rely completely on the deposit insurance system. We believe these studies are consistent with the overall theme of deregulating our institutions to the maximum practicable extent consistent with safety and soundness and instilling a fair degree of discipline in our depository institutions.

In conclusion, while the Corporation favors enactment of H.R.4879 with the suggested technical amendments, a sunset provision not to exceed two years from the date of enactment should be written into the bill. This provision would insure that the broader issues involving the assessment and insurance of deposits, discussed heretofore, will be accorded timely consideration by the Congress. We believe that the sunset provision would allow the Congress ample time to consider these matters.

Mr. Chairman, this concludes my statement. I would be pleased to respond to the subcommittee's questions.

FDIC CHANGES TO H.R. 4879

Be it enacted by the Senate and House of Representatives of the United States of American in Congress assembled.

Section 1. Subsection 5 of Section 3 (1) of the Federal Deposit Insurance Act (12 U.S.C. § 1813 (1)) is hereby amended to read in its entirety as follows:

(5) such other obligations of a bank as the Board of Directors, after consultation with the Comptroller of the Currency and the Board of Governors of the Federal Reserve System, shall find and prescribe by regulation to be deposit liabilities by general usage: Provided further, that any obligation of a bank which is:

(A) payable only at an office of the bank located outside of the States of the United States, the District of Columbia, Puerto Rico, Guam, American Samoa, and the Virgin Islands, or

(B) defined to be an international banking facility deposit by the Board of Directors, after consultation with the Board of Governors of the Federal Reserve System,

shall not be a deposit for any purposes of this Act or be included as part of total deposits or of an insured deposit.

Section 2. Section 18 (a) of the Federal Deposit Insurance Act (12 U.S.C. § 1828 (a)) is hereby amended by adding, after the second sentence, a new sentence which reads as follows:

> Whenever it determines that the creation of a class of uninsured obligations by one or more insured banks may confuse the public regarding the scope of insured coverage under this Act, the Board of Directors may require by regulation that insured banks holding such obligations shall give notice of their uninsured status.

Section 3. The provisions of this Act shall terminate on December 31, 1983. On January 1, 1984, provisions of law amended by this Act shall be further amended to read as they did on the day before the date of the enactment of these amendments.