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Testimony by

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Chairman, Board of Governors of the Federal Reserve System

before the

Subcommittee on Commerce, Consumer, and Monetary Affairs

of the

Committee on Government Operations

U.S House of Representatives

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I am pleased to appear before the Committee to discuss deposit insurance reform. The issue has increasingly come to the attention of the Congress and the media as the cost of resolution of failed thrift institutions becomes more apparent, and as various government and private reports focus on the potential liabilities facing the Bank Insurance Fund. Last year the Congress mandated a study of the issues by the Treasury. This study, in which the Federal Reserve, the FDIC, the OCC, the OTS, and other agencies will be active participants, will be published later this year or early next. But hearings on the issues now by this and several other Committees of the Congress will, I hope, sharpen the focus on the need for legislation promptly after the release of the Treasury report.

Your letter of invitation, Mr. Chairman, focuses on the issues associated with the feasibility, benefits, and risks of some reduction in insurance coverage and the associated potential for enhanced depositor discipline. The Board has considered these highly complex and important questions on several occasions. My statement today will summarize our views on this approach to the problem, but the Board believes it is important for the Congress to review options other than reduced insurance coverage in order to address the root cause of the taxpayer exposure and the potential financial market distortions associated with our present deposit insurance and supervisory approaches.

As you know, Mr. Chairman, the Board also believes that deposit insurance reform is intimately related to the pressing need to modernize our banking system in other ways. The erosion of the domestic and international competitive position of U.S. banks must be addressed by

expanded permissible activities and wider geographical branching powers, and we believe that legislation in this area should be joined with deposit insurance reform. I have presented the Board's proposals on these subjects before the Senate and House Banking Committees this summer. Given the narrower focus of the hearings today, and the additional witnesses this morning, I have omitted a detailed delineation of the Board's modernization proposals, but I nevertheless want to underline their importance, with the strong endorsement that these issues should, in the Board's view, be considered jointly with deposit insurance reform by this Committee and by both Houses of the Congress.

The fundamental problems with our current deposit insurance program are clearly understood and are, I believe, subject to little debate among those with drastically different prescriptions for reform. The safety net--deposit insurance, as well as the discount window--has so lowered the risks perceived by depositors as to make them relatively indifferent to the soundness of the depository recipients of their funds, except in unusual circumstances. With depositors exercising insufficient discipline through the risk premium they demand on the interest rate they receive on their deposits, the incentive of some banks' owners to control risk-taking has been blunted. Profits associated with risk-taking accrue to owners, while losses in excess of bank capital that would otherwise fall on depositors are absorbed by the FDIC.

Weak depositor discipline and this moral hazard of deposit insurance have two important implications. First, the implicit deposit insurance subsidy has encouraged banks to enhance their profitability by increasing their reliance on deposits rather than capital to fund their

assets. In effect, the deposit insurance funds have been increasingly substituted for private capital as the cushion between the asset portfolios of insured institutions and their liabilities to depositors. A hundred years ago, the average equity-capital-to-asset ratio of U S banks was almost 25 percent, approximately four times the current level. Much of the decline over the past century no doubt reflects the growing efficiency of our financial system. But it is difficult to believe that many of the banks operating over recent decades would have been able to expand their assets so much, with so little additional investment by their owners, were it not for the depositors' perception that, despite the relatively small capital buffer, their risks were minimal. Regulatory efforts over the last 10 to 15 years have stabilized and partially reversed the sharp decline in bank equity capital-asset ratios. This has occurred despite the sizable write-off of loans and the substantial build-up in loan-loss reserves in the last three years or so. But the capital ratios of many banks are still too low.

Second, government assurances of the liquidity and availability of deposits have enabled some banks with declining capital ratios to fund riskier asset portfolios at a lower cost and on a much larger scale, with governmental regulations and supervision, rather than market processes, the major constraint on risk-taking. As a result, more resources have been allocated to finance risky projects than would have been dictated by economic efficiency.

In brief, the subsidy implicit in our current deposit insurance system has stimulated the growth of banks and thrifts. In the process the safety net has distorted market signals to depositors and bankers about

the economics of the underlying transactions. This has led depositors to be less cautious in choosing among institutions and has induced some owners and their managers to take excessive risk. In turn, the expanded lending to risky ventures has required increased effort and resources by supervisors and regulators to monitor and modify behavior.

But in reviewing the list of deficiencies of the deposit insurance system, particularly if an increased role for depositor discipline is contemplated, we should not lose sight of the contribution that deposit insurance has made to macroeconomic stability. The existence and use of the safety net has shielded the broader financial system and the real economy from instabilities in banking markets. More specifically, it has protected the economy from the risk of deposit runs, especially the risk of such runs spreading from bank to bank, disrupting credit and payment flows and the level of trade and commerce. Confidence in the stability of the banking and payments system has been the major reason why the United States has not suffered a financial panic or systemic bank run in the last half century.

There are thus important reasons to take care as we modify our deposit insurance system. Reform is required. So is caution. The ideal is an institutional framework that, to the extent possible, induces banks both to hold more capital and to be managed as if there were no safety net, while at the same time shielding unsophisticated depositors and minimizing disruptions to credit and payment flows.

The congressional increase in the deposit insurance level in 1980 from \$40,000 to \$100,000 was intended to permit depository institutions to

have access to deposits not subject to the rate ceilings then in force. Disintermediation especially suggested the need to facilitate the access of thrifts to funds that would substitute for the retail deposits that were at the time bleeding off to higher yielding market instruments at rates that thrift portfolios would not permit them to match. Large time deposits--defined by the regulators as those over \$100,000--were exempt from rate ceilings on the thought that their size--over twice the then insured level--implied sophisticated holders familiar with market instruments and the evaluation of financial assets. It was argued that an increase in deposit insurance coverage to the level that would exempt such deposits from rate ceilings would open up access by smaller and weaker depository institutions to large denomination time deposits that previously had been limited to a smaller set of depositories for whom the market was willing to provide significant uninsured funding. Such funding at market rates, it was contemplated, would not require raising yields for the retail depositors willing to remain at lower rates. The extension of deposit insurance was thus an increase in a subsidy in lieu of the removal of regulations that were phased out some time later by the Depository Institutions Deregulation Act. But, as in virtually all other cases, the subsidy remained.

If we were starting from scratch, the Board believes it would be difficult to make the case that deposit insurance coverage should be as high as its current \$100,000 level. However, whatever the merits of the 1980 increase in the deposit insurance level from \$40,000 to \$100,000, it is clear that the higher level of depositor protection has been in place long enough to be fully capitalized in the market value of depository

institutions, and embedded in the financial decisions of millions of households. The associated scale and cost of funding have been incorporated into a wide variety of bank and thrift decisions, including portfolio choices, staffing, branch structure, and marketing strategy. Consequently, a return to lower deposit insurance coverage--like any tightening of the safety net--would reduce insured depository market values and involve significant transition costs. It is one thing initially to offer and then maintain a smaller degree of insurance coverage, and quite another to reimpose on the existing system a lower level of insurance, with its associated readjustment and unwinding costs. This is why the granting of subsidies by the Congress should be considered so carefully. They not only distort the allocation of resources, but also are extremely difficult to eliminate, imposing substantial transition costs on the direct and indirect beneficiaries. For such reasons, the Board has concluded that, should the Congress decide to lower deposit insurance limits, a meaningful transition period would be needed.

Another relevant factor that should be considered in evaluating the \$100,000 insurance limit is the distribution of deposit holders by size of account. Unfortunately, data to analyze this issue by individual account holder do not exist. However, we have been able to use data collected on an individual household basis in our 1983 Survey of Consumer Finances to estimate the distribution of account holders. While these data are seven years old, they are the best available until results from our 1989 Survey of Consumer Finances become available this fall. I have attached as an appendix to this statement summary tables and descriptive text of the 1983 survey results. Briefly, the survey suggests that in

1983 between 1.0 and 1.5 percent of U S. households held deposit balances in excess of \$100,000. The demographic characteristics of these account holders suggest that they are mainly older, retired citizens with most of their financial assets in insured accounts. These characteristics of heads of households owning deposits are remarkably stable as the size of deposits declines to \$50,000.

A 1988 survey of small and medium-size businesses--described in the second appendix to this statement--suggests that 7.1 percent of such businesses had at least one account in excess of \$100,000. These firms are generally of modest size those with uninsured deposits had median sales of \$3.2 million, had less than 50 employees, and over 10 percent of these entities were proprietorships or partnerships. The 1988 small business survey suggests a sharp drop-off in the size of firms as the maximum deposit declines to, say, \$50,000.

Some have suggested a reduction of deposit insurance to that level and the available evidence suggests that persons and small businesses with \$50,000 of deposits would probably be as capable as current depositors with over \$100,000 of assessing the health of their banks or thrifts. As I noted, the demographics of the two household groups are similar, although the business units with balances between \$50,000 and \$100,000 have significantly smaller scale than those with balances over \$100,000. In addition, it is arguable that, should the insured deposit limit be reduced to \$50,000, and policies adopted which make losses by uninsured depositors much more likely than they are today, uninsured depositors with a strong preference for safety would be able to purchase evaluations of banks and thrifts from professional analysts

Such depositors would also have access to alternative safe investments, especially Treasury securities

Nevertheless, the characteristics of households and small businesses with deposits between \$50,000 and \$100,000 do not suggest that they, compared to many other market participants, have the most resources and greatest abilities to bring market discipline to bear on depository institutions. Thus it seems reasonable to question whether such depositors should be assigned a key role in deposit insurance reform. Moreover, as discussed above, the benefits of lowering deposit insurance coverage at this time must be balanced against the readjustment and unwinding costs imposed on individuals, institutions, and markets that have adapted to the \$100,000 deposit insurance level.

A decision by Congress to leave the \$100,000 limit unchanged, however, should not preclude other reforms that would reduce current inequities in, and abuses of, the deposit insurance system, often thwarting its purpose. Serious study should be devoted to the cost and effectiveness of policing the \$100,000 limit so that multiple accounts are not used to obtain more protection for individual depositors than Congress intends. We at the Federal Reserve believe that it is administratively feasible--but not costless--to establish controls on the number and dollar value of insured accounts per individual at one depository institution, at all institutions in the same holding company, and perhaps--at sharply rising cost and complexity--even across unrelated depositories. But we are concerned about the cost and administrative complexity of such schemes, and would urge the careful weighing of benefits and costs before adopting any specific plan.

The same study could consider the desirability of limiting pass-through deposit insurance--under which up to \$100,000 insurance protection is now explicitly extended to each of the multiple beneficiaries of some large otherwise uninsured deposits. Brokered accounts of less than \$100,000 also have been used to abuse deposit insurance protection, particularly by undercapitalized institutions. However, the study should keep in mind the power Congress has already provided the agencies to constrain misuse of brokered accounts.

No matter what the Congress decides on deposit insurance limits, we must be cautious of our treatment of uninsured depositors--whether defined as those in excess of \$50,000 or \$100,000. Such depositors should be expected to assess the quality of their bank deposits just as they are expected to evaluate any other financial asset they purchase. Earlier I noted that our goal should be for banks to operate as much as possible as if there were no safety net. In fact, runs of uninsured deposits from banks under stress have become commonplace.

So far, the pressure transmitted from such episodes to other banks whose strength may be in doubt has been minimal. Nevertheless, the clear response pattern of uninsured depositors to protect themselves by withdrawing their deposits from a bank under pressure raises the very real risk that in a stressful environment the flight to quality could precipitate wider financial market and payments distortions. These systemic effects could easily feed back to the real economy, no matter how open the discount window and how expansive open market operations. Thus, while deposits in excess of insurance limits should not be protected by the safety net at any bank, reforms designed to rely mainly on increased

market discipline by uninsured depositors raise serious stability concerns

An example of one such approach is depositor co-insurance or a deductible under which a depositor at a failed institution receives most, but not all, of his or her deposit in excess of a reduced (or the current) insurance limit. This option has some attractions, coupling depositor market discipline with relatively modest possible losses to depositors. The Board believes, however, that an explicit policy that requires imposition of uninsured depositor loss--no matter how small--is likely to increase the risk of depositor runs and to exacerbate the depositor response to rumors.

Another option to rely more on private-market incentives without necessarily reducing the size of insurance coverage is the use of private deposit insurance as a replacement for FDIC insurance. This would require, of course, that all relevant supervisory information--much of which is now held confidential--be shared with private insurers who would be obligated to use that information only to evaluate the risk of depositor insurance and not for the purposes of adjusting any of their own portfolio options. In addition, it is clearly unreasonable to impose on private insurers any macro-stability responsibilities in their commercial underwriting of deposit insurance. Private insurers' withdrawal of coverage in a weakening economy, or their unwillingness to forebear in such circumstances would be understandable but counterproductive. Private insurers' inability to meet their obligations after an underwriting error would be disruptive at best and involve taxpayer responsibility at worst. Private insurance and public responsibility unfortunately are not always

compatible. Many of these concerns are mitigated if private insurance is used as a supplement to FDIC insurance, say to cover a co-insurance portion above some minimum. However, we would remain concerned about mutual assurance among groups of banks who would seek to evaluate each other's risk exposure and discipline overly risky entities by expulsion from their mutual guarantee syndicate. In addition, a system of mutual guarantees by banks could raise serious anti-competitive issues

There has also been support for the increased use of subordinated debentures in the capital structure of banking organizations. Intriguing attractions of this option are the thoughts that non-runnable, but serially maturing, debt would provide both enhanced market discipline and a periodic market evaluation of the bank. The Board continues to support the use of subordinated debt for these reasons, as well as the fact that it provides supplementary capital to act as an additional buffer to the FDIC over and above that provided by the owners' equity capital. But, in our view, subordinated debentures can only be supporting players and not be awarded the central role in reform. This is a limited source of capital and one that may prove difficult and expensive to obtain when advertised as having limited returns like debt, but whose holders are expected to absorb losses for the FDIC like equity. Adding features to make it more attractive adds complications which perhaps are best met directly by additional pure equity and other reforms.

A promising approach that seeks to simulate market discipline with minimal stability implications is the application of risk-based deposit insurance premiums by the FDIC. The idea is to make the price of

insurance a function of the bank's risk, reducing the subsidy to risk-taking and spreading the cost of insurance more fairly across depository institutions. In principle, this approach has many attractive characteristics, and could be designed to augment risk-based capital. For example, banks with high risk-based capital ratios might be charged lower insurance premiums. But the range of premiums necessary to induce genuine behavioral changes in portfolio management might well be many multiples of the existing premium, thereby raising practical concerns about its application. Risk-based premiums also would have to be designed with some degree of complexity if they are to be fair and if unintended incentives are to be avoided. In any event, the potential additional benefits on top of an internationally negotiated risk-based capital system, while positive, require further evaluation.

Another approach that has induced increasing interest is the insured narrow bank. Such an institution would invest only in high quality, short-maturity, liquid investments, recovering its costs for checking accounts and wire transfers from user fees. The narrow bank would thus require drastic institutional changes, especially for thousands of our smaller banks and for virtually all households using checking accounts. Movement from the present structure for delivery of many bank services would be difficult and costly, placing U.S. banks at a disadvantage internationally. In addition, this approach might shift and possibly focus systemic risk on larger banks. Banking organizations would have to locate their business and household credit operations in nonbank affiliates funded by uninsured deposits and borrowings raised in money and capital markets. Only larger organizations could fund in this way and

these units, unless financed longer term than banks today, would, even with the likely higher capital ratio imposed on them by the market, be subject to the same risks of creditor runs that face uninsured banks, with all of the associated systemic implications. If this were the case, we might end up with the same set of challenges we face today, refocused on a different set of institutions. We at the Board believe that while the notion of a narrow bank to insulate the insurance fund is intriguing, in our judgment further study of these systemic and operational implications is required.

If, in fact, proposals that rely on uninsured depositor discipline, private insurance, subordinated debentures, risk-based premiums, and structural changes in the delivery of bank services raise significant difficulties, reform should then look to other ways to curb banks' risk appetites, and to limit the likelihood that the deposit insurance fund, and possibly the taxpayer, will be called on to protect depositors. The Board believes that the most promising approach is to reform both bank capital and supervisory policies. This would build upon the groundwork laid in FIRREA, in which Congress recognized as key components of a sound banking system the essentiality of strong capital plus effective supervisory controls. Both would be designed to reduce the value of the insurance subsidy. Neither would rule out either concurrent or subsequent additions to deposit insurance reform, such as the changes discussed previously, other proposals, or new approaches that may emerge in the years ahead. In fact, higher capital, by reducing the need for, and thereby the value of, deposit insurance would make subsequent reform easier. There would be less at stake for the participants in the system

At the end of this year, the phase-in to the International Capital Standards under the Basle Accord will begin. This risk-based capital approach provides a framework for incorporating portfolio and off-balance sheet risk into capital calculations. Most U.S. banks have already made the adjustment required for the fully phased-in standard that will be effective at the end of 1992. However, the prospective increasingly competitive environment suggests that the minimum level of capital called for by the 1992 requirements may not be adequate, especially for institutions that want to take on additional activities. As a result of the safety net, too many banking organizations, in our judgment, have travelled too far down the road of operating with modest capital levels. It may well be necessary to retrace our steps and begin purposefully to move to capital requirements that would, over time, be more consistent with what the market would require if the safety net were more modest. The argument for more capital is strengthened by the necessity to provide banking organizations with a wider range of service options in an increasingly competitive world. Indeed, projections of the competitive pressures only intensify the view that if our financial institutions are to be among the strongest in the world, let alone avoid an extension of the taxpayers' obligation to even more institutions, we must increase capital requirements. Our international agreements under the Basle Accord permit us to do so.

There are three objectives of a higher capital requirement. First, higher capital would strengthen the incentives of bank owners and managers to evaluate more prudently the risks and benefits of portfolio choices because more of their money would be at risk. In effect, the

moral hazard risk of deposit insurance would be reduced. Second, higher capital levels would create a larger buffer between the mistakes of bank owners and managers and the need to draw on the deposit insurance fund. For too many institutions, that buffer has been too low in recent years. The key to creating incentives to behave as the market would dictate, and at the same time creating these buffers or shock absorbers, is to require that those who would profit from an institution's success have the appropriate amount of their own capital at risk. Third, requiring higher capital imposes on bank managers an additional market test. They must convince investors that the expected returns justify the commitment of risk capital. Those banks unable to do so would not be able to expand.

We are in the process in the Federal Reserve System of developing more specific capital proposals, including appropriate transition arrangements designed to minimize disruptions. However, at the outset I would like to anticipate several criticisms. For many banks, raising significant new capital will be neither easy nor cheap. Maintaining return on equity will be more difficult, and those foreign banks that only adhere to the Basle minimums may have lower capital costs relative to some U-S banks. Higher capital requirements also will tend to accelerate the move toward bank consolidation and slow bank asset growth. However, these concerns must be balanced against the increasing need for reform now, the difficulties with all the other options, and both the desire of, and necessity for, banking organizations to broaden their scope of activities in order to operate successfully.

More generally, many of the arguments about the competitive disadvantages of higher capital requirements are short-sighted. Highly

leveraged banks are less able to respond to rapidly changing situations. In fact, well-capitalized banks are the ones best positioned to be successful in the establishment of domestic and foreign long-term relationships, to be the most attractive counterparties for a large number of financial transactions and guarantees, and to expand their business activities to meet new opportunities and changing circumstances. Indeed, many successful U.S. and foreign institutions would today meet substantially increased risk-based capital standards. In addition, the evidence of recent years suggests that U.S. banks can raise sizable equity. The dollar volume of new stock issues by banking organizations has grown at a greater rate since the late 1970s than the total dollar volume of new issues by all domestic corporate firms. The recent declines in bank stock prices, reflecting market concerns about the quality of bank assets, will make the capital building process more difficult and costly. However, over time, banks with sound management policies will be able to continue to build their capital base.

Higher capital standards should go a long way toward inducing market-like behavior by banks. However, the Board believes that, so long as a significant safety net exists, additional inducements will be needed through an intensification of supervisory efforts to deter banks from maintaining return on equity by acquiring riskier assets. Where it is not already the practice, full in-bank supervisory reviews--focusing on asset portfolios and off-balance sheet commitments--should occur at least annually, and the results of such examinations should promptly be shared with the board of directors of the bank and used to evaluate the adequacy of the bank's capital. The examiner should be convinced after a rigorous

and deliberate review that the loan-loss reserves are consistent with the quality of the portfolio. If they are not, the examiner should insist that additional reserves be created with an associated reduction in the earnings or equity capital of the bank.

This method of adjusting and measuring capital by reliance on examiner loan evaluations does not depend on market value accounting to adjust the quality of the assets. Some day, perhaps, we may be able to apply generally accepted market value accounting precepts to both the assets and liabilities of a financial going concern with a wide spectrum of financial assets and liabilities. But the Board is not comfortable with the process as it has developed so far, either regarding market value accounting's ability accurately to reflect market values over reasonable periods or to avoid being overly sensitive to short-run events. For most banks, loans are the predominant asset, assets that do not have ready secondary markets but that the examiners can evaluate in each of the proposed annual in-bank supervisory reviews. We at the Federal Reserve believe that the examiners' classification of loan quality should, as I noted, be fully reflected in the banks' loan loss reserves by a diversion of earnings or a reduction in capital. If the resultant capital is not consistent with minimum capital standards, the board of directors and the bank's regulators should begin the process of requiring the bank either to reduce those assets or to rebuild equity capital.

If credible capital raising commitments are not forthcoming, and if those commitments are not promptly met, the authorities should pursue such responses as lowered dividends, slower asset growth or perhaps even asset contraction, restrictions on the use of insured brokered deposits,

if any, and divestiture of affiliates with the resources used to recapitalize the bank. What is important is that the supervisory responses occur promptly and firmly and that they be anticipated by the bank. This progressive discipline or prompt corrective action of a bank with inadequate capital builds on our current bank supervisory procedures and is designed to simulate market pressures from risk-taking--to link more closely excessive risk-taking with its costs--without creating market disruptions. It is also intended to help preserve the franchise value of a going concern by acting early and quickly to restore a depository to financial health. In this way, the precipitous drop in value that normally occurs when a firm is placed in conservatorship or receivership would, for the large majority of cases, be avoided.

While some flexibility is certainly required in this approach, the Board believes there must be a prescribed set of responses and a presumption that these responses will be applied unless the regulator determines that the circumstances do not warrant them. Even though prompt corrective action implies some limit on the discretion of supervisors to delay for reasons that they perceive to be in the public interest, the Board is of the opinion that it would be a mistake to eliminate completely the discretion of the regulator.

Accordingly, the Board believes that a system that combined a statutorily prescribed course of action with an allowance for regulatory flexibility would result in meaningful prompt resolution. For example, if a depository institution failed to meet minimum capital requirements established by its primary regulatory agency, the agency might be required by statute to take certain remedial action, unless it determined on the

basis of particular circumstances that such action was not required. The presumption would thus be shifted toward supervisory action, and delay would require an affirmative act by the regulatory agency.

The prescribed remedial action required in a given case would be dependent upon the adequacy of the institution's capital. As the capital fell below established levels, the supervisor could be required, for example, to order the institution to formulate a capital plan, limit its growth, limit or eliminate dividends, or divest certain nonbank affiliates. In the event of seriously depleted capital, the supervisor could require a merger, sale, conservatorship or liquidation.

In adopting such a statutory framework, Congress should consider designing the system so that forced mergers, divestitures and, when necessary, conservatorships could be required while there is still positive equity capital in the depository institution. While existing stockholders should be given a reasonable period of time to correct deteriorating capital positions, Congress should specifically provide the bank regulators with the clear authority, and therefore explicit support, to act well before technical insolvency in order to minimize the ultimate resolution costs. The presence of positive equity capital, even if at low levels, when combined with any tier 2 capital, would limit reorganization and liquidation costs.

In the Board's view, most of the remedial actions discussed above can be taken, and have been taken, by bank regulators under the current legal framework. Under current law, however, action is discretionary and dependent upon a showing of unsafe or unsound conditions or a violation of law, and implementation of a supervisory remedial action can be extended

over a protracted period of time where the depository institution contests the regulator's determination. What is needed is legislation that would permit a systematic program of progressive action based on the capital of the institution, instead of requiring the regulator to determine on a case-by-case basis, as a precondition to remedial action, that an unsafe or unsound practice exists. This program would introduce a greater level of consistency of treatment into the supervisory process, place investors and managers on notice regarding the expected supervisory response to falling capital levels, and reduce the likelihood of protracted administrative actions challenging the regulator's actions.

The Board is in the process of developing the parameters, processes and procedures for prompt corrective action. One of the principles guiding our efforts is the need to balance rules with discretion. In addition, as is the case for higher capital standards, the Board is mindful of the need for an appropriate transition period before fully implementing such a change in supervisory policy.

Higher capital and prompt corrective action would increase the cost and reduce the availability of credit from insured institutions to riskier borrowers. In effect, our proposal would reduce the incentive some banks currently have to overinvest in risky credits at loan rates that do not fully reflect the risks involved. This implies that the organizers of speculative and riskier ventures will have to restructure their borrowing plans, including possibly paying more for their credit, or seek financing from noninsured entities. Some borrowers may find their proposals no longer viable. However, it is just such financing by some insured institutions that has caused so many of the current difficulties,

and it is one of the objectives of our proposals to cause depositories to reconsider the economics of such credits. As insured institutions reevaluate the risk-return tradeoff, they are likely to be more interested in credit extensions to less risky borrowers, increasing the economic efficiency of our resource allocation

Despite their tendency to raise the average level of bank asset quality, higher capital requirements and prompt corrective action will not eliminate bank failures. An insurance fund will still be needed, but we believe that, with a fund of reasonable size, the risk to taxpayers should be reduced substantially. As I have noted, higher capital requirements and prompt corrective action imply greater caution in bank asset choices and a higher cushion to the FDIC to absorb bank losses. In addition, an enhanced supervisory approach will not permit deteriorating positions to accumulate.

But until these procedures have been adopted and the banking system has adjusted to them, circumstances could put the existing insurance fund under severe pressure. As Chairman Seidman has indicated, the fund is already operating under stress, as its reserves have declined in recent years and now stand, as a percentage of insured deposits, at their lowest level in history. At the same time, there remain all too many problems in the banking system, problems that have been growing of late as many banks, including many larger banks, have been experiencing a deterioration in the quality of their loan portfolios, particularly real estate loans. It thus seems clear that the insurance fund likely will remain under stress for some time to come. Moreover, pressures would

intensify if real estate market conditions were to weaken further or a recession were to develop in the general economy.

It should, however, be clearly underlined that the size or adequacy of the insurance fund does not change the quality of the deposit insurance guarantee made by the federal government; it does allocate the cost of meeting any guarantee between the banking industry, that pays the insurance premiums, and the taxpayers as a whole. It should, in our view, be the policy of the government to minimize the risk to taxpayers of the deposit insurance guarantee, and we believe that our proposal does that. While some increase in insurance premiums is in all likelihood necessary, we must be concerned that attempts to accomplish this end by substantially higher insurance premiums may well end up--especially if accompanied by higher capital requirements--simply making deposits so unattractive that banks are unable to compete. Indeed, the Board is concerned that the levels of premiums contemplated in some quarters will exacerbate both the short- and the long-run problem by reducing the profitability of banks, and hence their ability to attract capital. Avoiding taxpayer costs and maintaining a competitive banking system are just two more reasons why basic deposit insurance reform is so urgent.

Among the deposit insurance reforms that might be considered on the basis of both strengthening the insurance fund and fairness to smaller and regional banks is the assessment of insurance premiums on the foreign branch deposits of U S banks. A substantial proportion of the deposits of the largest U.S banks are booked at branches outside the United States, including offshore centers in the Caribbean. Assessing such deposits could yield significant revenue for the FDIC. However, foreign

deposits may be quite sensitive to a small decline in their yields. Thus imposing premiums on them could lead to deposit withdrawals and funding problems at some U.S. banking organizations, and possibly inhibit the ability of these organizations to raise capital.

Even if no adjustment is made in the insurance assessment on foreign deposits, held almost solely by large banks, other deposit insurance reforms should be equally applicable to banks of all sizes. No observer is comfortable with the inequities and adverse incentives of an explicit or implicit program that penalizes depositors, creditors, and owners of smaller banks more than those of larger ones. The Board believes no bank should assume that its scale insulates it from market discipline, nor should any depositor with deposits in excess of the insurance limit at the largest of U.S. banks assume that he or she faces no loss should their bank fail.

Nevertheless, it is clear that there may be some banks, at some particular times, whose collapse and liquidation would be excessively disruptive to the financial system. But it is only under the very special conditions, which should be relatively rare, of significant and unavoidable risk to the financial system that our policies for resolving failed or failing institutions should be relaxed. The benefits from the avoidance of a contagious loss of confidence in the financial system accrue to us all. But included in the cost of such action is the loss of market discipline that would result if large banks and their customers presume a kind of exemption from loss of their funds. The Board's policies of prompt corrective action and higher capital are designed to minimize these costs. Under these policies, the presumption should always

be that prompt and predictable supervisory action will be taken. For no bank is ever too large or too small to escape the application of the same prompt corrective action standards applied to other banks. Any bank can be required to rebuild its capital to adequate levels and, if it does not, be required to contract its assets, divest affiliates, cut its dividends, change its management, sell or close offices, and the resultant smaller entity can be merged or sold to another institution with the resources to recapitalize it. If this is not possible, the entity can be placed in conservatorship until it is

It is, by the way, the largest U S. banks that would be required under our proposals to raise the most additional capital, both absolutely and proportionally. Most banks with assets less than \$1 billion already meet capital requirements considerably above the fully phased-in Basle Capital Accord minimums. In addition, it bears emphasizing that no deposit insurance reform that truly reduces the subsidy existing in the current system will be costless for banks. The issue really is one of achieving maximum benefit from reform at minimum cost. We believe that our proposals achieve this goal

In summary, events have made it clear that we ought not to permit banks, because of their access to the safety net, to take excessive risk with inadequate capital. Even if we were to ignore the potential taxpayer costs, we ought not to permit a system that is so inconsistent with efficient market behavior. In the process of reform, however, we should be certain we consider carefully the implications for macroeconomic stability. The Board believes that higher capital and prompt corrective action by supervisors to resolve problems will go a long way to eliminate

excessive risk-taking by insured institutions, and would not preclude additional deposit insurance reform, now or later. Finally, in considering all proposals, we should remind ourselves that our objective is a strong and stable financial system that can deliver the best services at the lowest cost and compete around the world without taxpayer support. This requires the modernization of our financial system and the weaning of some institutions from the unintended benefits that accompany the safety net. Higher capital requirements may well mean a relatively leaner and more efficient banking system, and they will certainly mean one with reduced inclinations toward risk.

As I noted in my opening remarks, the Board believes that these reforms should be coupled with the modernization of our financial system. As we address reductions in the subsidy to banks from deposit insurance, we should also authorize wider activities for well-capitalized banking organizations and eliminate the outdated statutes that prohibit banks from delivering interstate services in the most cost-effective way, through branching. These combined reforms will go a long way toward ensuring a safer and more efficient financial system and lay the groundwork for other modifications in the safety net in the years ahead.

Appendix 1

Selected Characteristics of Household Account Holders

This appendix provides supporting material on the distribution of household ownership of insured deposits. The most recent reliable disaggregated information available on the size and ownership of accounts comes from the 1983 Survey of Consumer Finances (SCF). This survey consists of interviews with 4,103 U.S. households drawn from two sampling frames: a randomized geographic sample to provide good coverage of broadly distributed characteristics, and a special sample of wealthy households constructed from data at the Statistics of Income Division of the IRS to provide better representation of more narrowly distributed characteristics, such as ownership of corporate stock. Survey experts agree that the SCF provides very reliable estimates of the distribution of financial characteristics.¹ The standard error due to sampling error for a figure of ten percent estimated from the entire survey population is about one-half percent.

The 1983 SCF was sponsored by the Board of Governors of the Federal Reserve System, the Department of Health and Human Services, the Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency, the Federal Trade Commission, the Department of Labor, and the Department of the Treasury. Data were collected through in-person interviews between February and August of 1983 under a contract with the Survey Research Center at the University of Michigan.

1. The survey is discussed in detail in an evaluation study "Measuring Wealth with Survey Data: An Evaluation of the 1983 Survey of Consumer Finances," by Robert B. Avery, Gregory E. Elliehausen, and Arthur B. Kennickell, *Review of Income and Wealth*, December 1988.

For the financial data collected in the survey, the unit of observation lies between the standard Census Bureau definition of a "family" plus "single individuals" and a "household." Generally, the survey excludes information only for individuals who are not related by blood or marriage to the economically dominant core of the household.

Among other items, the survey gathered information on the amount of money held in each of a household's accounts as well as the types of institutions where those accounts were held. There are three important limitations in the survey data. First, there is no information on the ownership of deposits within the household. Second, there is no information on how many accounts households may have at a given institution. Third, information on IRAs and Keoghs and CDs is more limited than for other deposits. For IRAs and Keoghs, the survey gathers only total holdings and the types of institutions where these accounts are held. For CDs, totals were gathered by term of the certificate and no institution information was collected.²

There are a number of different account constructs that can be created for evaluating the distribution of the coverage of household accounts by deposit insurance. Two cases are considered here. In the first case, it is assumed that all accounts held by a given household at a given type of institution are actually accounts owned by the same person and that the accounts are held at the same institution. This

2. In the 1989 SCF, from which preliminary information is expected around the end of October, more detailed institutional data were collected. In that survey, it will be possible to identify accounts that are held by households at the same institution. In addition, the institutions where certificates of deposit are held will be known. However, it will still not be possible to disaggregate accounts by different owners within the household.

construct is referred to below as the "synthetic account" definition. In the second case, it is assumed that all accounts are either owned by different household members or are held at different financial institutions. This measure is referred to below as the "individual account" definition. The former construct will almost surely overstate the amount of uninsured deposits, while the second may understate that number. Because of data limitations noted below, the second construct is not quite a polar case.

Synthetic Account Definition

In the synthetic account measure, accounts and institution are synonymous. The creation of this account proceeds in several steps. First, all checking, savings, and money market deposit accounts are summed by the type of institution where the account was held.³ Second, IRA and Keogh accounts are allocated equally to each type of institution where the accounts were held.⁴ Finally, because no information is available on the institutions where CDs were held, it is assumed that they were held at the institution type that otherwise had the largest

³ For example, suppose a household had four such accounts, one of \$50,000 at a commercial bank, one of \$30,000 at a savings and loan, and two accounts of \$20,000 (one belonging to the head of the household and the other to his mother) at a credit union. In this case, the household would then have synthetic accounts of \$50,000 at a commercial bank, \$30,000 at a savings and loan, and \$40,000 at a credit union.

⁴ Continuing the example of the previous footnote, suppose the household has a total of \$50,000 in IRA and Keogh accounts and that those accounts are held at commercial banks and savings and loans. Then \$25,000 is attributed to both the commercial bank and the savings and loan synthetic accounts for a total of \$75,000 in commercial banks, \$55,000 in savings and loans, and \$40,000 in credit unions.

level of deposits ⁵

Table 1 presents information based on this account concept. Households are classified in the columns by the largest of their synthetic accounts.⁶ As shown in rows 1 and 2, only 2.6 percent (2.2 million) households are estimated to have an account of \$75,000 or more at an insured institution. However, as shown by row 6, this same group is estimated to hold 38.6 percent of all deposits owned by households. Even when compared to the universe of deposits (computed as gross deposits from the June 1983 call reports for the appropriate types of institutions), the same group is estimated to hold 14.5 percent of all deposits (row 7).⁷ This group is also estimated to hold 27.7 percent of insured household deposits (row 9).⁸ Note that the aggregation of accounts will tend to understate the amount of insured deposits held by these groups.

Data in rows 11 to 26 of table 1 provide other characteristics of the classes of account holders. The data indicate that households with an account of \$75,000 or more tend to have higher income, financial assets, and net wealth than the whole population (shown in the last

⁵ Again, continuing the example, suppose the household has CDs totaling \$125,000 (\$110,000 in short-term certificates and \$15,000 in long-term certificates). Because the largest synthetic account at this stage of aggregation is the commercial bank account, the entire amount of the CDs is added to this account for a total of \$200,000.

⁶ In the example, the household would be included in the column "≥100K" because its largest synthetic account (the commercial banks account) is \$200,000.

⁷ The call report is a regular report of balance sheet, income, and other data made by depository institutions to the regulatory agencies.

⁸ "Insured deposits" includes only the part of accounts that is \$100,000 or less. In the example, the household has total deposits at insured institutions of \$295,000 of which \$195,000 (\$55,000 in savings and loans, \$40,000 in credit unions, and the first \$100,000 of the \$200,000 in commercial banks) would be insured deposits.

column) While they hold a substantial part of their financial assets and net wealth in insured depository accounts, as a group they are also much more likely than the general population to have diversified their holdings into corporate stock, a business, or investment real estate. The top two groups also tend to be older and more likely to be retired.

The groups with their largest accounts between \$25,000 and \$75,000 are more like the top groups than like the group with accounts under \$25,000 and the group with no accounts. The principal differences between the \$25,000-\$75,000 group and the top two groups are the facts that their levels of financial assets and net worth are lower. Like the top two groups, they are more likely to be older and retired and to have a diversified portfolio.

Individual Account Definition

In the individual account definition, each reported account is treated separately so far as the data allow. Each checking, savings, and money market deposit account is counted as a separate account for purposes of deposit insurance coverage.⁹ As before, IRAs and Keoghs are divided equally by the number of types of institutions where such accounts were held.¹⁰ Finally, long-term and short-term CDs are allocated to the type of institution where the household otherwise had its largest account.¹¹ Note that this definition does not constitute

⁹ For example, assuming the same household-level data as in the example beginning in footnote 3, the household would have four accounts, one of \$50,000 at a commercial bank, one of \$30,000 at a savings and loan, and two of \$20,000 each at a credit union.

¹⁰ Thus, in the example, the household would now have six accounts, including the four described in the last footnote and two additional accounts of \$25,000 each.

¹¹ In the example, the household would now have eight accounts, the two additional accounts being one of \$110,000 and one of \$15,000 and both held at commercial banks.

the opposite of the synthetic account definition since there is still some aggregation of accounts in the treatment of the IRA and Keogh accounts and the CDs

Table 2 presents estimates using this second definition that are comparable in structure to the estimates reported in table 1. As would be expected, there is an overall shift of households away from the top groups compared to table 1. By the individual account definition, 1.4 percent (1.1 million) of all households have accounts of \$75,000 or more (rows 1 and 2). Correspondingly, the estimated amount of insured deposits increases to \$865.9 billion (row 8).¹² While there is some shifting of the characteristics reported in the bottom two blocks of the table, the overall picture is very similar to that in table 1.

Estimated Household Share of Insured and Uninsured Deposits

Table 3 gives the estimated coverage of deposit insurance for the current and lower hypothetical ceilings on insurance coverage for each of the two account definitions. According to the synthetic account measure (which provides the greatest understatement of the amount of insured deposits), at the current ceiling of \$100,000, 84.8 percent of total household accounts are estimated to have been covered in 1983. If the ceiling were dropped to \$50,000, it is estimated that 72.3 percent would still have been covered. By the individual account measure, the

¹² In the example, the household has \$295,000 of deposits at insured institutions as before, of which \$285,000 would be insured (the sum of the initial \$50,000 account at a commercial bank, \$30,000 at a savings and loan, two accounts of \$20,000 at a credit union, two accounts of \$25,000 each at a commercial bank and a savings and loan, one CD of \$15,000 at a commercial bank, and the first \$100,000 of the \$110,000 CD at a commercial bank)

percent of household deposits insured at the current ceiling rises to 91.3 percent

Household accounts represent only a part of insured deposits. As noted in the last column in row 7 of either of the first two tables, roughly 37.6 percent of total deposits was held by households in 1983. According to call report data tabulated in the 1988 *Annual Report* of the FDIC, in 1983 deposits of \$1,268 billion out of \$1,691 billion (75.0 percent) at commercial banks were insured.¹³ The proportion of insured deposits was 75.1 percent in 1988. However, this is a limited definition of insured deposits. The underlying data contain no information on either multiple accounts at one institution or pass-through accounts, and thus, on net may overstate the amount of insured deposits. Using the closest possible survey definition, the individual account definition of table 2, the data suggest that \$63.6 billion (not shown in the tables), or 15.0 percent of the FDIC's estimate of uninsured deposits at commercial banks, may belong to households.¹⁴ However, this estimate is rather rough. The figure may tend to overstate the true amount of uninsured household deposits by the limited FDIC definition because of the aggregation of IRAs and Keoghs and CDs, but may also tend to understate the true figure because of underreporting in the survey.

¹³ The total of insured deposits is the sum of all accounts of \$100,000 and under and \$100,000 for each account of more than \$100,000.

¹⁴ Call report data are not available for the calculation of the household share of potentially uninsured deposits for hypothetical lower insurance ceilings.

Table 3

**Estimated Percent of Household Deposits Covered by Deposit Insurance
Various Hypothetical Deposit Insurance Ceilings
Synthetic Account Definition and Individual Accounts Definition**

Account definition	Hypothetical deposit insurance ceiling			
	\$25K	\$50K	\$75K	\$100K
Synthetic accounts	56.5	72.3	80.3	84.8
Individual accounts	71.3	83.5	88.2	91.3

APPENDIX 2

SELECTED CHARACTERISTICS OF SMALL AND MEDIUM-SIZED BUSINESS OWNERS OF INSURED DEPOSITS

This appendix presents information on the ownership of insured checking and other deposit accounts by small and medium-sized business firms. The information is from the National Survey of Small Business Finances (NSSBF), a survey of a nationally representative sample of 3,404 small and medium-sized firms conducted during 1988-89.¹ The NSSBF represents the population of small and medium-sized businesses more accurately and covers their financial relationships more thoroughly than any other available survey. Editing of the survey data, however, is only partially complete. Therefore, statistics presented in this appendix should be viewed as preliminary and used with caution.²

The National Survey of Small Business Finances is a survey of the use of financial services and financial institutions by small and medium-sized businesses. The survey was sponsored by the Board of Governors of the Federal Reserve System and the Small Business

1. For a detailed description of the survey, see Brenda G. Cox, Gregory E. Elliehausen, and John D. Wolken, "The National Survey of Small Business Finances: Final Methodology Report," RTI Report 4131-00F (Research Triangle Park, NC: Research Triangle Institute, September 1989).

2. Dollar amounts have received very little editing so far. Extreme values have been replaced when they appeared to be doubtful, and missing values have been provisionally estimated by substituting mean account balances of the reported values for that employment size class. The dollar estimates are subject to further revision after more rigorous imputation. Account ownership, financial institution information, and firm characteristics such as employment, organization form, and industry are accurate. See Gregory E. Elliehausen and John D. Wolken, Banking Markets and the Use of Financial Services by Small and Medium-Sized Businesses, Staff Studies 160 (Board of Governors of the Federal Reserve System, 1990).

Administration The sample was drawn from the population of all for-profit, nonagricultural, nonfinancial enterprises listed on the Dun's Market Identifier file It consisted of those firms that had fewer than 500 full-time equivalent employees and were in operation at the end of December 1987.³

The Data

The level of detail collected by the NSSBF permits deposit accounts to be disaggregated to the level of a specific financial institution Deposit account balances for accounts reported in this appendix are the sum of all checking, savings and money market deposit accounts, and certificates of deposit at each depository institution used by the firm Thus, all of the deposits held by a sample firm in one depository institution represents one insured account for the purpose of this survey⁴

The statistics presented here are based on the responses of 3,404 businesses, representing 3 510 million small and medium-sized businesses having an estimated 4 157 million deposit "accounts" at commercial banks and thrift institutions All statistics are weighted to provide

³ The Dun's file undercovers very new firms, firms with few employees, and sole proprietorships. Nevertheless, the Small Business Administration estimates that the Dun's file accounts for 93 percent of private employment in the United States See US Small Business Administration, The State of Small Business A Report of the President (Washington, DC US Government Printing Office, 1988)

⁴ Because the unit of observation is the enterprise, account holdings of subsidiaries and branches of a multiple establishment firm in the same financial institution are consolidated Thus, distinct accounts at a particular financial institution held by different establishments of the same firm would be counted as one account. This possibility exists for the eight percent of sampled firms with multiple establishments Hence, the estimate of uninsured deposits is slightly biased upward

appropriate estimates for the population of small and medium-sized nonagricultural, nonfinancial businesses. They do not reflect firms with 500 or more employees, agricultural and financial firms, not-for-profit firms, and firms owned by government entities.

Selected Characteristics of Deposit Accounts and Firms

Table 1 presents the distribution of deposit accounts among small and medium-sized business firms and selected characteristics of these firms classified by size of deposit account. As noted above, all accounts at one institution are combined into one deposit account, the resulting accounts are included in the table for each institution at which the firm has an account. Thus, for example, 2 771 million small and medium-sized business firms (row 1, column 2) are estimated to have 3.255 million accounts with balances under \$25,000 (row 3, column 2)

Distribution of Accounts Among small and medium-sized businesses, large balance accounts are relatively infrequent. About 246,000 (7.1 percent) of these businesses have deposit accounts of \$100,000 or more (rows 1 and 2, respectively). Another 76,000 (2.2 percent) have accounts between \$75,000 and \$99,999. Some small and medium-sized businesses have multiple accounts (that is, they have deposits at more than one institution). The 246,000 businesses with balances of \$100,000 or more have 297,000 accounts in this account size group, the 76,000 firms in the \$75,000 to \$99,999 group have 83,000 accounts of this size (row 3)

Nearly two-thirds of the total deposits of small and medium-sized firms are in large balance accounts. The 297,000 accounts with balances of \$100,000 or more are estimated to sum to \$82 billion (row 5, column

6), about 63 percent of all deposits owned by small and medium-sized businesses (row 6, column 6) Most of these holdings are uninsured at the current deposit insurance limit of \$100,000 Only \$29.7 billion of the total deposits in this group are insured (row 8, column 6), the remaining \$52.3 billion are uninsured (row 10, column 6)

Although a large proportion of small and medium-sized business deposits are in the \$100,000 or more group, these deposits account for only 2.2 percent of total deposits at commercial banks and thrift institutions (row 7, column 6).⁵ Indeed, all deposit account balances of small and medium-size businesses, regardless of size, account for 3.5 percent of total deposits. (row 7, column 7)⁶

Characteristics of Account Owners. Data in rows 11 through 19 of table 1 present some demographic characteristics of small and medium-size firms holding different sized deposit accounts. Firm size -- whether measured by sales, total assets, or number of full-time equivalent employees -- distinguishes owners of low balance accounts from owners of large balance accounts. For example, mean sales for firms owning deposit accounts under \$25,000 is \$657,000 (row 14, column 2). In contrast, firms with deposit account balances of \$100,000 or more have mean sales of \$8.4 million dollars (row 14, column 6) Organization form also varies by account size Owners of deposit accounts with balances under \$25,000 are divided almost evenly between

⁵ Total deposits of commercial banks and thrift institutions, obtained from the Call Report, was \$3,725 billion in December 1987

⁶ Statistics from the flow of funds accounts suggest that all non-farm, nonfinancial businesses held no more than 10.4 percent of total deposits at commercial banks and thrift institutions at the end of 1987

sole proprietorships and corporations (rows 17 and 19, respectively). In the \$100,000 or more group, however, only 5.4 percent of the firms are sole proprietorships, while 86.8 percent are corporations.

Share of Deposits Covered Under Alternative Deposit Insurance Ceilings

Table 2 presents the estimated share of small and medium-sized business deposits that would be covered under various hypothetical deposit insurance ceilings. For example, the last column of table 2 estimates the insured deposit distribution with the current \$100,000 deposit insurance level. The estimates in the column indicate that all small and medium-sized businesses have insured deposit balances equalling \$77.9 billion and that \$52.3 billion of small and medium-sized business deposits are uninsured.⁷ Thus only 59.8 percent of total small and medium-sized business deposits are insured at the current ceiling. At a \$50,000 ceiling, the estimated percentage of small and medium-sized business deposits covered would fall to 45.2 percent. As shown in the last row of table 2, a reduction in the insurance level to \$50,000 would about double the number of firms with uninsured balances from 246,000 to 474,000 small and medium-sized businesses.

⁷ The \$77.9 billion is the same value shown in column 7, row 8 of table 1.

Table 1
 Selected Characteristics of Deposit Account Ownership by Small and Medium-sized Businesses
 By Size of Account at Insured Depository Institution
 1988 National Survey of Small Business Finances

Item	Size of Account at Insured Institution						All Sm Bus
	No account	\$1-25K	\$25K-50K	\$50K-75K	\$75K-100K	>\$100K	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
1 Num of sm & med bus(thou) ¹	149	2771	317	184	76	246	3510
2 % of all sm & med bus	4.2	78.9	9.0	5.2	2.2	7.1	100.0
<i>Account characteristics</i>							
3 % of acc'ts held (thou)	0.0	3255	331	191	83	297	4157
4 Mean account size (\$thou)	0.0	5.96	32.87	56.73	84.20	277.58	31.30
5 Amount of deposits held(\$bil)	0.0	19.4	10.9	10.9	7.0	82.0	130.2
6 % of all sm & med bus deposits	0.0	14.9	8.4	8.4	5.4	63.0	100.0
7 % of all deposits	0.0	0.5	0.3	0.3	0.2	2.2	3.5
8 Amount of insured deposits(\$bil)	0.0	19.4	10.9	10.9	7.0	29.7	77.9
9 % of all insured sm & med bus deposits	0.0	24.9	14.0	14.0	9.0	38.1	100.0
10 Amount of uninsured deposits(\$bil)	0.0	0.0	0.0	0.0	0.0	52.3	52.3
<i>Firm characteristics</i>							
11 Median 1987 sales(\$ thou)	10	200	771	1127	1320	3200	237
12 Median 1987 assets(\$thou)	12	75	250	450	525	1300	100
13 Median employees ²	1	3.5	7.5	14.5	13.5	23.5	4
14 Average 1987 sales(\$thou)	77	657	2170	3442	3479	8449	1262
15 Average 1987 assets(\$thou)	273	479	1100	1280	1860	3007	521
16 Average employees ²	3.2	8.3	19.9	27.9	27.8	46.3	11.2
17 % Proprietorships	64.8	43.9	18.9	14.0	14.7	5.4	39.9
18 % Partnerships	14.2	8.5	5.9	4.8	5.5	7.9	8.3
19 % Corporations	20.9	47.6	75.3	81.2	79.9	86.6	51.8

1 Sum is greater than total because businesses may own multiple accounts.

2 Full-time equivalent employees defined as the sum of full time employees plus one half part time employees

Table 2
Estimated Percent of Small and Medium-sized Business Deposits
Covered by Deposit Insurance at
Various Hypothetical Deposit Insurance Ceilings
1988 National Survey of Small Business Finances

	Hypothetical deposit insurance ceiling			
	\$25K	\$50K	\$75K	\$100
Insured Deposits (\$bil)	41 9	58 8	69 7	77 9
Uninsured Deposits (\$bil)	88 3	71 4	60 5	52 3
Percent of Small Business Deposits Covered	32 2	45 2	53 5	59 8
Number of Small Businesses with Uninsured Accounts (thou)	753	474	308	246