FEDERAL DEPOSIT INSURANCE CORPORATION, Washington, DC 20429

OFFICE OF THE CHAIRMAN

August 24, 2012

Honorable Bob Corker
United States Senate
Washington, D.C. 20510

Dear Senator Corker:

Thank you for your letter requesting the Federal Deposit Insurance Corporation's perspective on a potential extension of the unlimited noninterest-bearing transaction account guarantee provisions of the Dodd-Frank Act. Your letter asks specific questions relating to the potential effects of an extension on the Deposit Insurance Fund and the banking industry.

Enclosed are responses to the specific questions that you raised in your letter.

I hope this information is helpful to you. If you have other questions, please feel free to contact me at (202) 898-3888 or Eric J. Spitler, Director, Office of Legislative Affairs, at (202) 898-7140.

Sincerely,

Martin J. Gruenberg

Martin J. Gruenberg
Acting Chairman

Enclosure

Response to Questions from the Honorable Bob Corker by the Federal Deposit Insurance Corporation

Q.1: Throughout its history, the potential for the moral hazard arising from FDIC insurance has been mitigated by the limit on the insurance level. What is your view of the moral hazard that might be generated by an extension of the TAG program with unlimited insurance?

A.1: The FDIC established the original TAG program to maintain financial stability and banking system liquidity during the 2008 financial crisis. For similar reasons, Congress extended the program in 2010 through the end of this year. A long-term or permanent extension of the TAG program would raise clear moral hazard issues. However, the moral hazard issues raised by a short-term extension are less clear.

Q.2: The FDIC is generally required to charge premiums based on a risk-based insurance model and to design the premium structure to maintain adequate reserves. If TAG were to be extended, what changes, if any, would you recommend to the program relating to the payment of premiums to build reserves and to provide risk-based premiums at actuarially sound rates?

Q.2: Because the Dodd-Frank Act temporarily changed the definition of insured deposits to include the entire balance of noninterest-bearing transaction accounts, the FDIC currently does not charge a separate assessment for TAG deposits. Deposit Insurance Fund (DIF) risk-based assessments pay for losses incurred to protect all insured deposits, including those covered by temporary insurance.

The Dodd-Frank Act requires that the DIF reserve ratio (the DIF balance as a percent of estimated insured deposits) reach 1.35 percent by September 30, 2020. Since any short-term extension will have expired by then, TAG deposits will not affect the reserve ratio on this date.

The FDIC assessment rates have been set with this statutory goal and deadline in mind. We estimate that losses under the current Dodd-Frank TAG and the FDIC's original TAG were about 3 percent higher than losses would have been without the TAG coverage. Losses from TAG thus far have not been large enough to affect materially the DIF's ability to reach this goal and have not required any increase in assessment rates. While it is difficult to project the additional losses resulting from an extension of the program, the experience of the two TAG programs would suggest that the cost of a short-term TAG extension would not require an increase in assessment rates to reach 1.35 percent by September 30, 2020.

Q.3: Two of the primary arguments for extending TAG are to provide funds to community banks to increase lending and liquidity. However, recent analysis indicates that bank loan-to-deposit ratios are very low by historic standards and that the industry has plenty of liquidity. Would you please provide the latest information the FDIC has on industry loan-to-deposit ratios and measures of liquidity, and tell me if in light of these ratios the TAG extension remains necessary?

A.3: Recent bank liquidity measures are above historical averages. For example, as of March 2012 the ratio of short-term assets to short-term liabilities for commercial banks was 94.6 percent. In comparison, the ratio of short-term assets to short-term liabilities for commercial banks was 58.6 percent at the end of 2007 and 70.3 percent at the end of 2002. Recent industry average loan-to-deposit ratios also are lower than historical averages. As of March 2012 the industry average loan-to-deposit ratio was 70.4 percent. In comparison, the average loan-to-deposit ratio was 89.2 percent at the end of 2002 and 92.7 percent at the end of 2007.

While industry average loan-to-deposit ratios are lower than historic averages, community banks have been lending a greater percentage of their deposits than the industry overall in recent quarters. Historically, the average loan-to-deposit ratio for banks with less than $1 billion in assets has been lower than the industry average (e.g., in 2002, the ratio for banks with less than $1 billion in assets was 78.2 percent compared to a ratio for the industry of 89.2 percent). Since the fourth quarter of 2008, however, the average loan-to-deposit ratio for banks with less than $1 billion in assets has been higher than the industry average. As of March 2012, for example, the average loan-to-deposit ratio for banks with less than $1 billion in assets was 71.9 percent and the industry average was 70.4 percent.

For a variety of reasons, the banking industry is in a stronger liquidity position now than it has been in recent years, but significant changes in the economic environment could rapidly affect industry liquidity and loan-to-deposit ratios. Given the uncertainty in the near-term economic outlook, it is difficult at this time to anticipate the consequences of the expiration of temporary coverage at the end of this year for industry liquidity.

Q.4: Members of Congress and others have expressed concern about the increasing percentage of industry assets held by the largest banks. Community banks have expressed the concern that a TAG extension is needed to help them compete with the largest banks. At the same time, it appears proportionally more of the TAG deposits may be held by the largest banks, and these deposits may account for a significant percentage of the growth in those banks. Could you please provide your latest information on the location of TAG deposits by size of banks?

A.4: The table below shows the share of amounts over $250,000 in noninterest-bearing transaction accounts (TAG deposits) by size of the insured institution where the accounts are held.

Insured Commercial Banks and Savings Institutions
Distribution of Noninterest-Bearing Transaction Deposits
by Asset Size

As of March 31, 2012

Asset Size	Number of Institutions	Total Assets ($ B)	Domestic Noninterest-Bearing Transaction Accounts Larger Than $250,000		
			Total ($ B)	Amount Above $250,000 Coverage Limit ($ B)	Share
Less than $1 Billion	6,644	1,421.1	70.3	45.2	3.4%
$1 - $10 Billion	557	1,419.8	101.1	74.1	5.6%
$10 - $50 Billion	71	1,387.8	119.9	98.7	7.5%
$50 - $100 Billion	17	1,281.0	121.1	105.6	8.0%
Over $100 Billion	19	8,416.1	1,095.2	995.1	75.5%
Total	7,308	13,925.9	1,507.5	1,318.7	100.0%