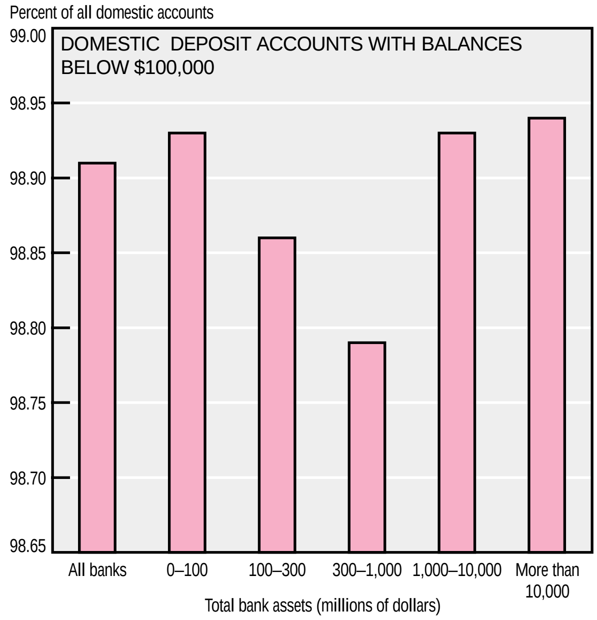
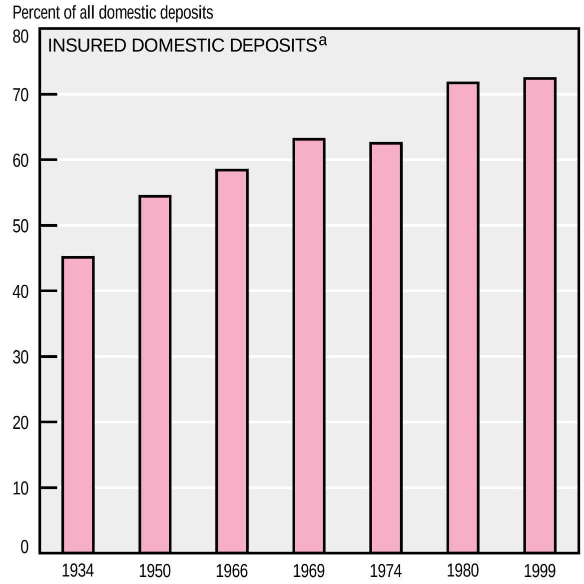
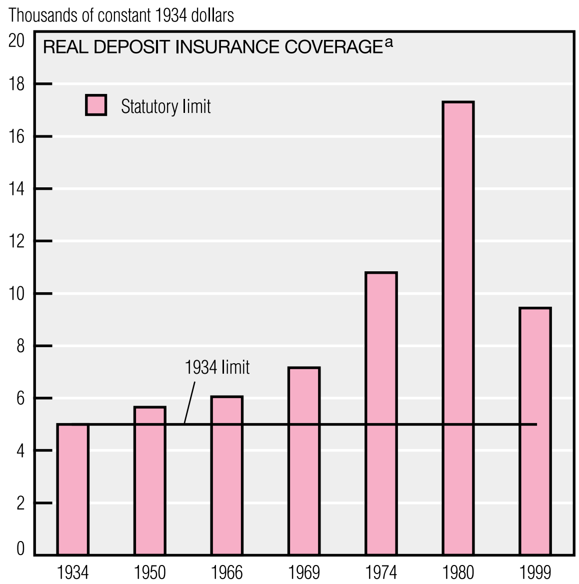
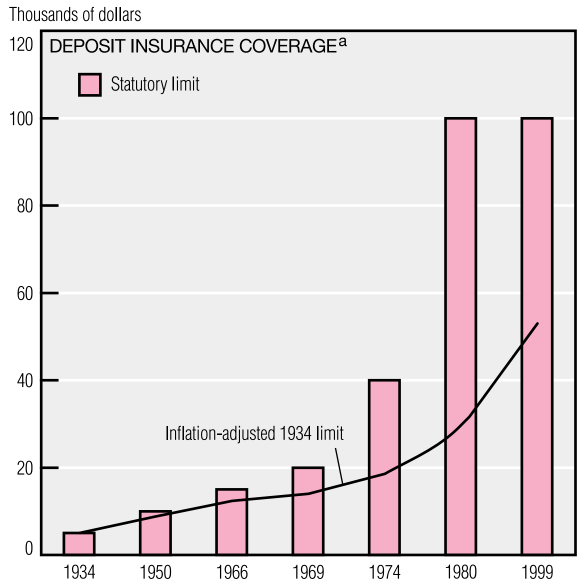
Deposit Insurance









a. The years shown are those in which the statutory limit was changed.
SOURCES: U.S. Department of Commerce, Bureau of Economic Analysis; and Federal Financial Institutions Examination Council, *Reports of Condition and Income.*

The Financial Modernization Act of 1999 created the most sweeping banking reforms since the Great Depression. But even as regulators, financial institutions, and policymakers have worked to implement this act, its critics have called for additional reforms. In particular, the Federal Deposit Insurance Corporation has initiated a study to reexamine and restructure federal deposit insurance; this would include doubling the deposit insurance limit. While raising the limit might benefit insured banks and thrifts, it appears to offer most depositors little or no benefit. After all, balances fall within the current $100,000 limit for more than 98% of insured banks' domestic deposit accounts (regardless of a bank's size).

While the level of real deposit insurance coverage at the end of 1999 was only about half that in 1980, it remains high by historical standards. Deflated to 1934 prices, it is nearly double the level guaranteed when the FDIC began operations. In today's prices, the 1934 deposit insurance limit is around $53,000. Moreover, despite the decline in real deposit insurance coverage since 1980, the insured portion of total domestic deposits has increased slightly, from 71.7% to 72.4%.

Community banks have argued that increasing the deposit insurance limit would level the playing field between small depository institutions and large banking organizations that may be perceived as "too big to let fail," a status that they say would effectively give large banks 100% insurance on all deposits. Hence, community banks maintain that a sizeable increase in the insurance limit is needed to make the current system more fair. The interests of depositors and taxpayers do not figure in this debate; however,

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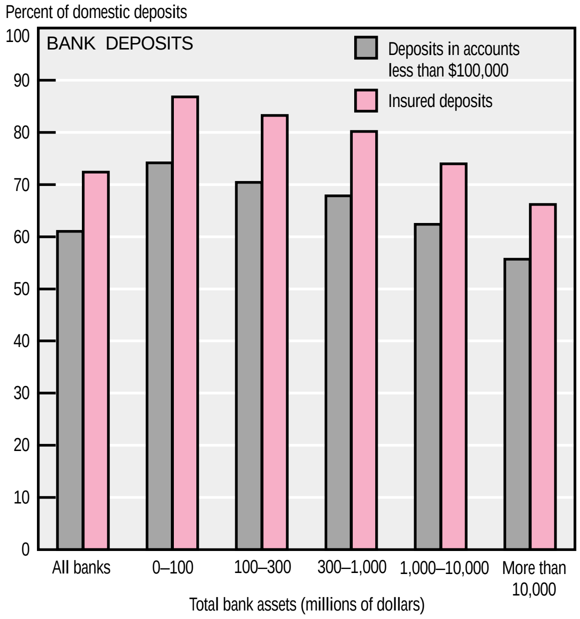
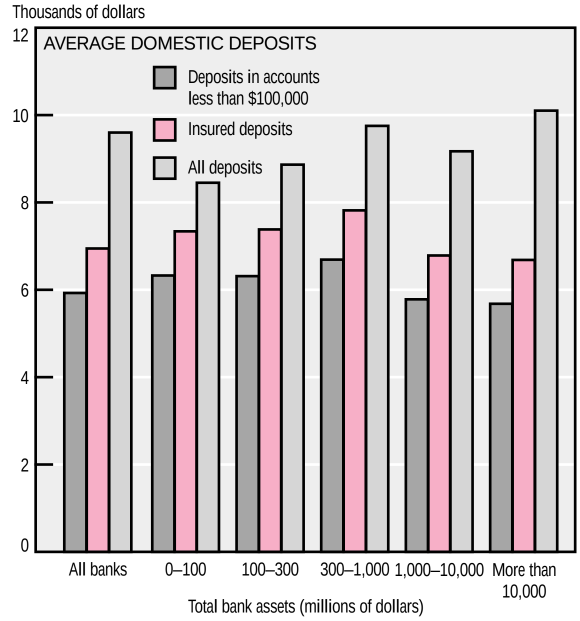
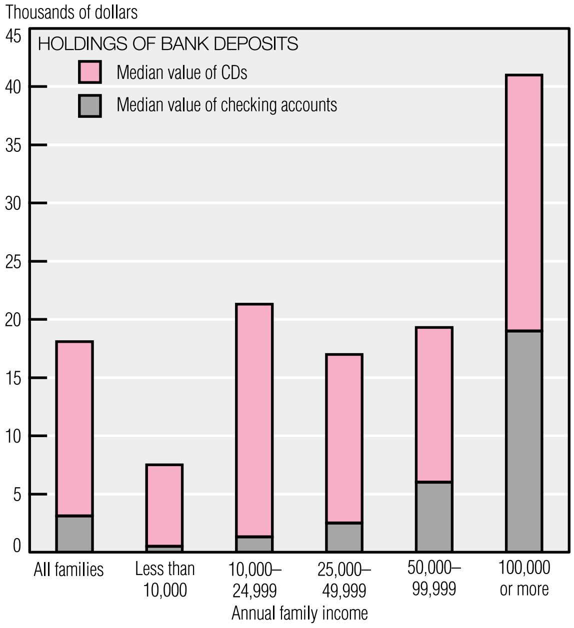
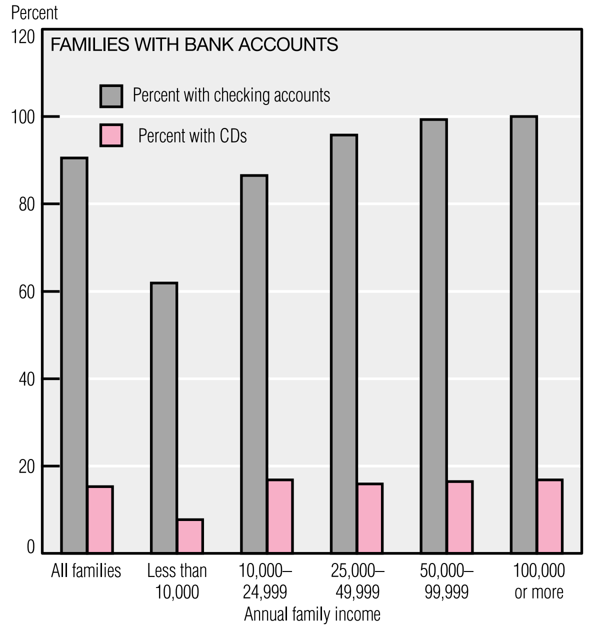
Deposit Insurance (cont.)









SOURCES: Federal Financial Institutions Examination Council, *Reports of Condition and Income*; and "Recent Changes in U.S. Family Finances: Results from the 1998 Survey of Consumer Finances," in *Federal Reserve Bulletin*, vol. 86 (January 2000), pp.1–29.

any proposal to reform the deposit insurance system must be fair to them as well as to banks of all sizes. Around 60% of domestic deposits are in accounts with balances below the $100,000 insurance ceiling, and more than 70% of all domestic deposits are insured. In the two categories of banks with the smallest assets, more than 80% of deposits are insured. The average deposit balance in banks of all sizes is well below the $100,000 insurance limit. This is true for the average deposit in accounts under $100,000, the average insured deposit, and the average domestic deposit.

The adequacy of the current deposit insurance ceiling might also be judged by considering family income in relation to bank deposits. Not surprisingly, survey evidence shows that families whose incomes exceed $100,000 hold the largest bank accounts. Yet even for these families, the current level of deposit insurance is more than double the combined median value of bank certificates of deposit and checking accounts, and nearly five times that of any other income group.

Finally, it is interesting to note the relationship between income and the share of families with bank accounts. While 98% of families with annual incomes over $50,000 have checking accounts, only 40% of those with incomes under $10,000 do. This makes it difficult to rationalize raising the insurance limit on the grounds of providing safe vehicles for small savers.

The FDIC's Bank Insurance Fund (BIF) and Savings Association Insurance Fund (SAIF) continued stable in 2000:IQ. BIF and SAIF reserves are 1.35% and 1.44% of insured deposits, well above the 1.25% target set by Congress in the Financial Institution Reform, Recovery, and

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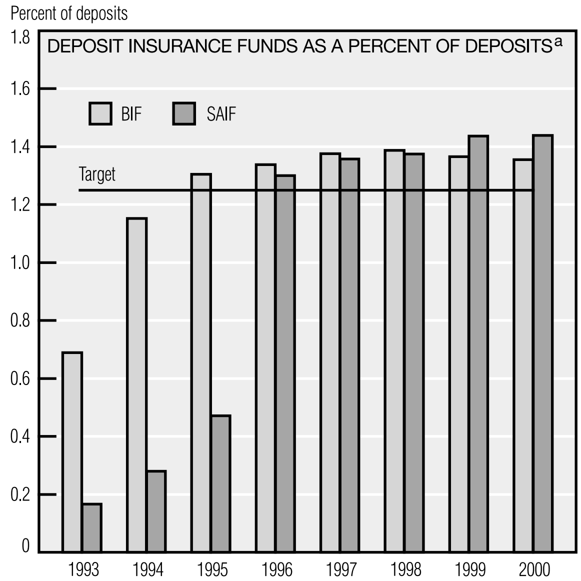

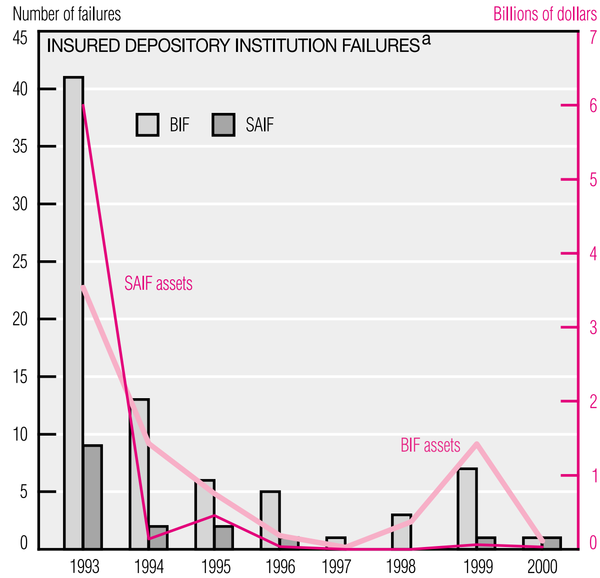

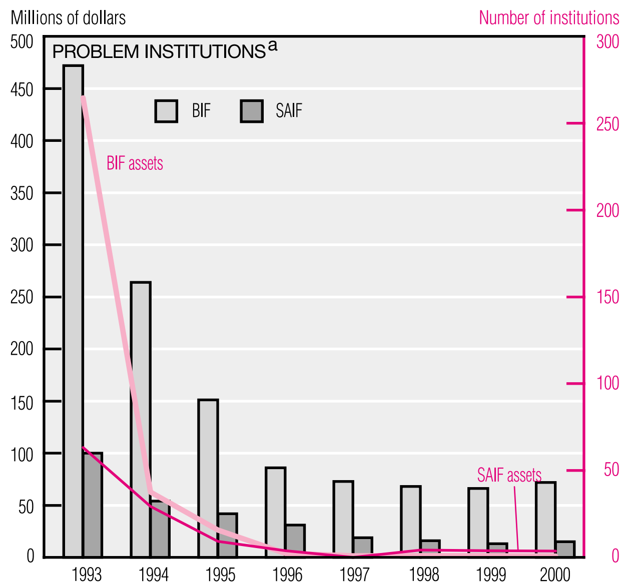

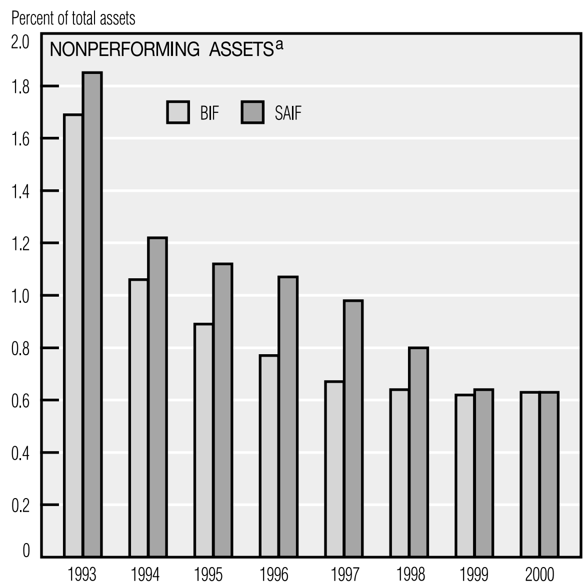

a. Data as of March 2000.
SOURCE: Federal Deposit Insurance Corporation, *Quarterly Banking Profile*.

Enforcement Act of 1989. Moreover, while BIF's reserves are down slightly from their peak of 1.39% of insured deposits, SAIF's ratio of reserves to insured deposits is at an all-time high.

The solid position of the two FDIC funds is evidenced by the stability of the banking and thrift industries. Failures of BIF members in 1999 reached their highest level since 1994 in terms of number (seven institutions) and total assets ($1.4 billion). The failure of one SAIF member in 2000:IQ matches the total number of SAIF-insured institution failures over the last three years. The dearth of thrift institution failures over the second half of the 1990s contrasts starkly with the solvency problems that plagued the industry throughout the 1980s. And although the number of bank failures has increased lately, the total still represents a tiny percent of FDIC-insured institutions in terms of number of firms and total assets.

Problem institutions (those with substandard examination ratings) rose from 66 to 72 for the BIF and 13 to 15 for the SAIF during 2000:IQ. However, while the increase in BIF problem institutions was matched by an increase in problem banks' assets, the increase in SAIF-insured problem institutions was accompanied by a decrease in their assets, indicating a decrease in the average size of problem thrifts. For both funds, the continued low number of problem institutions and the smallness of their assets suggests that losses to the insurance fund will remain low in the near future. This conjecture is supported by the low levels of nonperforming assets as a percent of total assets on the books of BIF and SAIF members.