FDIC Wants Banks to Prepay Fees

The Federal Deposit Insurance Corporation proposed on September 29 that banks prepay $45 billion in insurance premiums to help the FDIC avoid running out of money to cover bank failures.

The proposal allows a 30-day period for public commentary before it would go into effect. It would require banks to prepay their premiums for 2010-2012. This would be the first time the FDIC has required fees to be prepaid.

The prepayment requirement would help avoid either assessing a special fee on banks or borrowing from the Treasury Department. Neither of these two options is highly regarded because the fee would hurt banks and perhaps put some in danger of going under, while borrowing from the Treasury would amount to a taxpayer bailout with negative political repercussions.

Without the infusion of cash, the outlook for the FDIC is grim. The government-run insurance fund will be technically in the red as of September 30, as the failure of 120 banks in the last two years has taken its toll. The funds expenses to cover the cost of the failures is expected to grow to $100 billion over the next four years.

“What we are proposing to do is to tap the ample liquidity of the banking industry to improve our own liquidity position without borrowing from the Treasury,” FDIC Chairman Sheila Bair explained during a board meeting in Washington. Under the proposal approved by the board, banks would need to pay their premiums for the fourth quarter of 2009 and all of 2010-2012 by December 30 of this year.

“It’s certainly a better solution than taking a large chunk of money out of banks’ income and capital,” said James Chessen, chief economist at the American Bankers Association. According to Chessen, requiring prepayment gives “the FDIC the cash that they need, it will be paid for by the industry and it will not have the severe impact that other options would have had on banking.”

But some analysts see this as a temporary fix at best; it only delays the inevitable need for special fees or increasing annual premiums. “You pull this forward once, but if the gap is large, you’ll have to charge (an extra fee) anyway,” noted Jaret Seiberg, an analyst with Concept Capital’s Washington Research Group.

Because the plan is essentially an “early collection” of premiums for the coming years, no further premiums would be owed in the near future, and no further money would come into the FDIC without special fees or borrowing. Seiberg declared the move a “one-time accounting gimmick.”

Even on the popular old television show *MacGyver*, the gimmicks used to avert disaster were only temporary fixes. The FDIC’s prepayment ploy may serve for the time being to keep the accounts of bank depositors insured, but the best long-term solution would be to get the federal government out of the business of bailing out both banks and bank depositors.