Increases in the number of bank failures during the 1980’s put a strain on the deposit insurance fund that caused a great deal of concern about the role of regulators in the banking industry and the ability of the deposit insurance system to withstand credit crises. The FDIC raised deposit insurance premiums during this period to keep the Bank Insurance Fund (BIF) solvent and also adopted a risk-based fee structure in 1994. The purpose of this dissertation is to analyze the effects of these premium changes on bank total asset risk.

Theoretical evidence suggests that banks attempting to maximize the value of deposit insurance will increase asset risk when deposit insurance premiums increase. The empirical evidence does not consistently report this relationship.

The contribution of this research is as follows: First, this research tests the effect of changes in deposit insurance premiums on bank asset risk. Other studies have used options methodology and failure rate methodology. Studies employing a linear regression technique have used other variables, such as the percentage of deposits insured, to determine the effect of deposit insurance on bank risk. Second, this research employs a simultaneous equations methodology to reflect the simultaneity of bank input, output, and pricing decisions. Simultaneous equations methodology has been used in the banking literature to analyze the bank structure-performance issue, but has not been used specifically to determine effects of deposit insurance on bank performance.