

What Happens to your Money when a Bank Fails (in the US)

Very few people used to think about whether or not their money was safe in the bank - it was always assumed that it was. Until some of the recent bank failures made people wonder, is my money really safe in the bank? How do I know?

In the United States, the Federal Deposit Insurance Corporation (FDIC) is an independent federal agency created in 1933 to promote public confidence and stability in the nation's banking system. Throughout its history, the FDIC has provided bank customers with prompt access to their insured deposits whenever an FDIC-insured bank or savings association has failed.

In this article you will learn about bank failures, how deposit insurance works, what its limits are, and how to keep your money safe.

What is the FDIC and how does it work?

The FDIC protects depositors' funds in the unlikely event of the financial failure of their bank or savings institution. FDIC deposit insurance covers the balance of each depositor's account, dollar-for-dollar, up to the insurance limit, including principal and any accrued interest through the date of the insured bank's closing. In the event of a bank failure, the FDIC acts in two capacities. First, as the insurer of the bank's deposits, the FDIC pays insurance to the depositors up to the insurance limit. Second, the FDIC, as the 'Receiver' of the failed bank, assumes the task of selling/collecting the assets of the failed bank and settling its debts, including claims for deposits in excess of the insured limit.

What is a bank failure and how does it happen? A bank failure is the closing of a bank by a federal or state banking regulatory agency. Generally, a bank is closed when it is unable to meet its obligations to depositors and others. This article deals with the failure of 'insured banks.' The term 'insured bank' means a bank insured by FDIC, including banks chartered by the federal government as well as most banks chartered by the state governments. An insured bank must display an official FDIC sign (see the logo above) at each teller window.

What money is insured by FDIC?

Who does the FDIC insure? Any person or entity can have FDIC insurance on a deposit. A depositor does not have to be a citizen, or even a resident of the United States. FDIC insurance only protects depositors, although some depositors may also be creditors or shareholders of an insured bank. FDIC insurance covers deposits received at an insured bank. Types of deposit products include checking, NOW, and savings accounts, money market deposit accounts (MMDA), and time deposits such as certificates of deposit (CDs).

The basic insurance amount is \$100,000 **per depositor, per insured bank**. This includes principal and accrued interest up to a total of \$100,000. The \$100,000 amount applies to all depositors of an insured bank except for owners of certain retirement accounts, which are insured up to \$250,000 per owner, per insured bank. Deposits in separate branches of an insured bank are not separately insured. Deposits in one insured bank are insured separately from deposits in another insured bank.

Deposits maintained in different categories of legal ownership at the same bank can be separately insured. Therefore, it is possible to have deposits of more than \$100,000 at one insured bank and still be fully insured. For example, a husband and wife could have up to \$200,000 in one or more joint accounts at the same insured bank and the deposits would be fully insured. The husband's ownership share is insured up to \$100,000 and the wife's ownership share is insured up to \$100,000. In addition, they could each have qualifying retirement account insured up to \$250,000 per depositor.

The FDIC **does not insure** money invested in stocks, bonds, mutual funds, life insurance policies, annuities, or municipal securities, even if these investments were bought from an insured bank. The FDIC also **does not insure** U.S. Treasury bills, bonds, or notes. These are backed by the full faith and credit of the United States government.

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The following types of retirement plan deposits qualify for coverage as 'certain retirement accounts' that are covered up to \$250,000 per owner per insured bank:

- All types of IRAs, including:
 - Traditional IRAs
 - Roth IRAs
 - Simplified Employee Pension (SEP) IRAs
 - Savings Incentive Match Plans for Employees (SIMPLE) IRAs
- All Section 457 deferred compensation plan accounts, such as eligible deferred compensation plans provided by state and local governments regardless of whether they are self-directed
- Self-directed defined contribution plan accounts, such as self-directed 401(k) plans, self-directed SIMPLE held in the form of 401(k) plans, self-directed defined contribution money purchase plans, and self-directed defined contribution profit-sharing plans
- Self-directed Keogh plan accounts (or H.R. 10 plan accounts) designed for self-employed individuals

All retirement accounts listed above owned by the same person in the same FDIC-insured bank are added together and the total is insured up to \$250,000.

The FDIC defines the term 'self-directed' to mean that plan participants have the right to direct how the money is invested, including the ability to direct that the deposits be placed at an FDIC-insured bank. If a participant of a retirement plan has the right to choose a particular depository institution's deposit accounts as an investment, the FDIC would consider the account to be self-directed. Also, if a plan has as its default investment option deposit accounts at a particular FDIC-insured institution, the FDIC would deem the plan to be self-directed for deposit insurance purposes because, by inaction, the participant has directed the placement of such deposits.

However, if a plan's only investment vehicle is the deposit accounts of a particular bank, so that participants have no choice of investments, the plan would not be deemed self-directed for deposit insurance purposes. Finally, if a plan consists only of a single employer/employee, and the employer establishes the plan with a single-investment option of plan assets, the plan would be considered self-directed for deposit insurance purposes.

Naming beneficiaries on a retirement account does not increase deposit insurance coverage.

Coverdell Education Savings Accounts (formerly known as an Education IRAs), Health Savings Accounts, and Medical Savings Accounts are not included in this ownership category ('certain retirement accounts') and are not eligible for the increased coverage limit. Also, accounts established under section 403(b) of the Internal Revenue Code (annuity contracts for certain employees of public schools, tax-exempt organizations and ministers) are not eligible for the \$250,000 coverage limit. For information on these types of accounts, contact the FDIC using the links at the end of this article.

Defined-benefit plans (benefits predetermined by an employee's compensation, years of service, and age) **are not** eligible for the \$250,000 coverage limit.

What exactly happens if my bank fails?

In the unlikely event that your bank fails, the FDIC notifies each depositor in writing using the depositor's address on record with the bank. This notification is mailed immediately after the bank closes. When the failed bank is acquired by another bank; the assuming bank also notifies the depositors. This notification usually is mailed with the first bank statement after the assumption. Every effort also is made to inform the public through the news media, town meetings, and notices posted at the bank.

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How long does the FDIC take to pay insurance on deposits after an insured bank fails? Federal law requires the FDIC to make payment as soon as possible. Historically, the FDIC pays insurance within a few days after a bank closing either by establishing an account at another insured bank or by providing a check. Deposits purchased through a broker may take longer to be paid because the FDIC may need to obtain the broker's records to determine insurance coverage.

Customers with uninsured deposits receive the insured portion of their account as described above. They will wait longer to receive payment for some or all of their **uninsured** deposits. The amount of uninsured deposits they may receive, if any, is based on the sale of the failed bank's assets. Depending on the quality and value of these assets, it may take several years to sell the assets. As assets are sold, uninsured depositors receive periodic payment on their uninsured deposit claim.

The FDIC does not insure safe deposit boxes or their contents. In the event of a bank failure, the FDIC in most cases arranges for an acquiring bank to take over the failed bank's offices, including locations with safe deposit boxes. If no acquirer is found, boxholders would be sent instructions for removing the contents of their boxes.

Where to learn more:

<http://www.fdic.gov/deposit/deposits/insured/index.html> Guide describes the FDIC's rules for insurance coverage of bank and savings association deposits and answers frequently asked questions about the FDIC's insurance rules.

<http://www4.fdic.gov/EDIE/> Calculate insurance coverage using the FDIC's online Electronic Deposit Insurance Estimator

Call toll-free at:

1-877-ASK-FDIC (1-877-275-3342)
from 8am until 8pm (Eastern Time)
Monday through Friday

Hearing Impaired Line:

1-800-925-4618

Source: Federal Deposit Insurance Corporation