Financially Speaking

FDIC Insurance Helps To Keep Bank Deposits Safe

Those of you who have read my columns over the years know that I am what you would call a Christmas nut. I love everything about the season – the decorations, the get-togethers, the festive music and yes, even the corny movies.

One of the all time best known Christmas movies, “It’s a Wonderful Life” starring James Stewart deserves a watch every year just for the inspiring and timeless message about life that it shares. But it also tells a story about the history of the American financial system and does so in a way that the hero, George Bailey, makes easy to understand.

In a pivotal scene in the movie George is driving by his family’s Savings and Loan building and sees a mob of people lined up trying to get in. He learns that they are depositors who have gotten scared and want to withdraw their money. George tries to calm them by explaining that their deposits were used to do things like loan their neighbor the money to build a house and the money isn’t just sitting in a vault in the back. Many still want to take their deposits out so George ends up giving them his own wedding money, allowing the business to stay open.

While this makes for a great movie scene, it is also drawn from real events in history.

During the Great Depression many banks experienced what became known as a “run on the bank” in which many depositors tried to withdraw their money at the same time. Just like George tried to explain in the movie, banks don’t keep deposits sitting in a vault. They invest that money and use it for things like giving out loans. While banks keep reserves available to cover regular withdrawals, they were not prepared for a large percentage of deposits to be withdrawn all at once, such as what happened in the early 1930’s. As a result, there was a wave of bank failures across the country and many people lost their money because of it.

To try and bring stability to the financial system, the federal government passed the Banking Act of 1933, otherwise known as the Glass-Steagall Act. Glass-Steagall made sweeping changes to how banks can operate and gave tighter regulation of national banks to the Federal Reserve System. Many of the rules ushered in by Glass-Steagall are still in force today.

Arguably one of the most important provisions of Glass-Steagall was the creation of the Federal Deposit Insurance Corporation (FDIC). The FDIC is an independent agency backed by the full faith and credit of the U.S. government that provides protection for depositors in case a bank becomes insolvent, is liquidated, or experiences other financial difficulties.

I think most people today know that the FDIC exists, but many may not understand the rules determining how bank deposits are protected.

The most commonly quoted coverage amount is to say that deposits are protected up to $250,000 per depositor, per insured bank. That is true but not the full story. Depending on how your account is owned, you may qualify for a larger amount of total coverage at a given institution because the FDIC has established coverage for a number of ownership categories.

For example, certain retirement accounts, such as traditional and Roth IRAs, qualify for a separate, additional $250,000 of coverage. That means that if an individual has $50,000 in checking, $100,000 in savings and another $200,000 in a bank deposit IRA that it could all be covered by FDIC insurance. The $150,000 in checking and savings is under the $250,000 personal limit and the $200,000 in the IRA is under the $250,000 retirement account limit.

However, if that same person had $50,000 in checking, $250,000 in savings and $100,000 in a bank deposit IRA it would not all be covered by FDIC insurance. The $300,000 in checking and savings would exceed the personal $250,000 limit by $50,000 so would only be protected up to the limit. The $100,000 in the IRA would be under the $250,000 retirement account limit so would be fully protected.

There can also be additional amounts of FDIC protection available for the same person at the same bank if they own accounts in other ownership categories. This can include things like accounts that are owned jointly with others, are titled in the name of a trust or have a Payable on Death beneficiary set up on them.

You can see how understanding how much in bank deposits at a single bank are protected by FDIC insurance can become complicated. Because the FDIC realizes that it can be confusing, they have a calculator called the Electronic Deposit Insurance Estimator, available on their website to help you. That calculator can be found here:

edie.fdic.gov

FDIC insurance was created to help people feel confident that their bank deposits are safe. For nearly a century it has provided protection for depositors and worked well to help keep our financial system stable. If you understand how the rules apply to you, you too can know that your bank deposits are secure.

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