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## Maximizing Federal Deposit Insurance Corporation's Insurance of Deposits

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# Feature

*For this issue's Feature, the Reporter presents comments by David W. Lobbell and John A. Darrow\* of Burke, Wilson & McIlvaine which will assist consumers in determining whether their deposits are insured by the Federal Deposit Insurance Corporation under current law.*

## Maximizing Federal Deposit Insurance Corporation's Insurance of Deposits

In light of the recent failure of the Bank of New England, the nature and scope of insurance of deposits by the Federal Deposit Insurance Corporation ("F.D.I.C.") has become a prevalent concern. While the F.D.I.C. has initially stated that all deposits in the Bank of New England will be insured to their full amounts, this certainly will not always be the case in future bank failures.

This article reviews FDIC insurance coverage of deposits under current law for individual accounts, joint accounts, trust accounts and accounts of business entities. 55 Fed. Reg. 20122 (1990)(to be codified at 12 C.F.R. § 330). In addition, current documentation requirements are reviewed. Finally, the article describes the recent Treasury Department bank reform proposals and explains their impact upon the amount of deposit insurance which an individual may receive. Upon reviewing this article, an individual may wish to consult their financial institution in order to maximize the insurance coverage for his or her family, household, or business entity.

### Current Insurance Coverage of Deposits

Under present law, each depositor in an insured institution<sup>1</sup> is protected by federal deposit insurance on the aggregate of all deposits in that institution, held by the depositor in the same right and capacity, up to a maximum limit. The present maximum is

\$100,000. For example, assume individual A held the following accounts in the following capacities and amounts at a single insured institution: (1) A, an individual — \$75,000; (2) A, an individual — \$50,000; (3) A and B, joint tenants — \$50,000.

First, as to the accounts held in an individual capacity, the aggregate of the deposits is \$125,000. This amount exceeds the \$100,000 maximum and therefore this arrangement results in \$25,000 in uninsured funds. Second, as to the accounts held in the capacity as a joint tenant, the deposit totals \$50,000, which falls within the maximum. Thus, the joint account is fully insured.<sup>2</sup>

### Individual Accounts

Funds owned by an individual and invested in one or more accounts in his or her own name are insured up to \$100,000 in the aggregate. This is true whether the accounts are maintained in the name of the individual owning the funds, in the name of his agent or nominee, or in the name of a guardian, conservator or custodian holding the funds for one's benefits. If, however, more than one person has the right to withdraw funds from a single ownership account, it will be considered a joint account unless there is a Power of Attorney or unless the account records clearly indicate that the second individual serving as an "authorized signee" on the account is not an owner of the funds.

### Joint Accounts

Funds held in an account in the names of two or more natural persons, each possessing equal withdrawal rights, are insured up to \$100,000.<sup>3</sup> This insurance is separate from the insurance afforded individual accounts held by any of the joint account holders. "Joint accounts" include joint tenancies with rights of survivorship, tenancies by the entirety, tenancies in common, or accounts by husband and wife as community property.

An account held in two or more names which fails to qualify as a joint account is treated as being owned by each owner, according to actual ownership interests, as an individual account.

Joint accounts are subject to double restrictions on insurance coverage. First, joint accounts held by the same combination of individuals are added together and insured only up to \$100,000. Second, and in addition to the first restriction, an individual co-owner's interests in all joint accounts, whether owned by the same or different combinations of persons, are added together and insured only up to \$100,000.

For example, assume individual A held the following joint accounts: (1) A and B — \$100,000; (2) A and B — \$100,000; (3) A, B and C — \$75,000. First, because accounts (1) and (2) are owned by the same combination of individuals, step one requires that the two accounts be added together and insured up to \$100,000. This step leaves \$100,000 uninsured. In contrast, account (3) is fully insured since it is held by a different combination of individuals and its balance is less than \$100,000. Under step two, the interests of A are added together. For insurance purposes, A has a one-half interest in the insured balances of accounts (1) and (2) (\$25,000 interest in each) and a one-third interest in the insured balance of account (3) (\$25,000 interest). A's \$75,000 total interest is within the \$100,000 limitation, resulting in no further uninsured deposits.

### Testamentary Accounts

Funds owned by an individual

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and invested in a testamentary account, for the benefit of the owner's spouse, child, or grandchild, are insured up to \$100,000 in the aggregate as to each such named beneficiary, separately from any other accounts of the owner or beneficiary. A testamentary account evidences an intent that upon the owner's death the funds shall belong to a named beneficiary. Examples of a testamentary account include a revocable trust account, a tentative or Totten trust account, and a payable on death account.

The testamentary intention must be manifested in the title of the account, using such commonly accepted terms as "in trust for," "payable on death to," or "as trustee for." If the beneficiary of such an account is other than a spouse, child, or grandchild of the owner, the funds in the account are, for insurance purposes, added to any other individual accounts of the owner and insured with such accounts up to \$100,000 in the aggregate.

The Resolution Trust Corporation has indicated that it will look to the relevant State law in determining whether or not an account qualifies as a testamentary account. Under Illinois law, a "payable on death account" is defined as an account in which individual signs an agreement (such as a signature card) with the institution that provides that on the death of a person designated as holder, the account shall be paid to or held by another person or persons. Ill. Ann. Stat., ch. 17, para. 2134 (Smith-Hurd 1990).

#### Irrevocable Trust Accounts

Generally, the trust interests of a beneficiary in accounts established under one or more irrevocable trust arrangements created by the same settlor are added together and insured up to \$100,000 in the aggregate. Such coverage is separate from the insurance coverage provided for other accounts held by the trustee, settlor or beneficiary. A "trust interest" is the interest of a beneficiary in an irrevocable express trust, whether created by written trust instrument or statute, but does not include any interest retained by the settlor.

As stated, the trust interest may

be created by statute. Under Illinois law, a trust account is defined as a signed agreement with an institution providing that the account shall be held in the name of a person or persons designated as trustee or trustees for one or more person designated as a beneficiary or beneficiaries. Ill. Ann. Stat., ch. 17, para. 2133 (Smith-Hurd 1990).

#### Accounts Held By A Corporation, Partnership Or Unincorporated Association

All funds invested in an account by a corporation, partnership or unincorporated association, engaged in any independent activity, are added together and insured to the \$100,000 maximum. An entity is deemed to be engaged in an "independent activity" if it is operated primarily for some purpose other than to increase insurance coverage. If the corporation, partnership or unincorporated association is not engaged in any independent activity, any account held by the entity is insured as if owned by the persons owning or comprising the entity. The imputed ownership interest of each such person is added to any individual account that the owner maintains in order to determine insurance coverage of such accounts.

#### Sole Proprietorship Accounts

Funds owned by a sole proprietorship and deposited in one or more accounts in the name of the business are treated as the individual accounts of the person who is the sole proprietor. The funds are added to any other individual accounts of that person and insured with such accounts up to \$100,000 in the aggregate.

#### Documentation Requirements

Generally, the account records of an institution must disclose any relationship upon which a claim for insurance coverage is based, such as a joint tenancy or a testamentary trust. Also, the details of the relationship must be ascertainable either from the records of the institution or from the records of the account holder maintained in good faith and in the regular course of business. If any insured deposit obligation of a bank is evidenced by a negotiable instrument such as certificate of deposit, cashier's

check or letter of credit, the owner of such will be recognized to the same extent as if her name and interest were disclosed on the records of the bank, provided the instrument was in fact negotiated with the owner prior to the date of the bank closing.

#### New Proposals Could Mean Less Coverage

The Treasury Department has recently submitted to Congress a comprehensive package of bank reform proposals.<sup>4</sup> Included in this package is a proposal to limit the deposit insurance for individual depositors to \$100,000 per institution for checking and savings accounts, and \$100,000 per institution for retirement accounts. Extended coverage presently available through the use of joint accounts and revocable trusts would be eliminated.

Under the proposals, there would be no limit on the number of institutions in which a person could have the new maximum amount on deposit. However, the FDIC will study the possibility of limiting insurance to \$100,000 a person regardless of how many accounts and banks were used. It is too early to tell whether these proposals, or modified versions thereof, will be approved by Congress. Nevertheless, these changes would certainly reduce the potential insurance coverage for consumers.

<sup>1</sup> An individual should initially determine whether the institution in which his or her deposits are held is an insured institution pursuant to the Federal Deposit Insurance Act.

<sup>2</sup> Because the deposits are held in different capacities, the joint account is not aggregated with the individual accounts. Rather, each type of account is insured separately up to \$100,000.

<sup>3</sup> Each co-owner must personally sign the signature card, except in the case of certificates of deposit, any deposit obligation evidenced by a negotiable instrument, or any account maintained by an agent, nominee, guardian, custodian or conservator on behalf of two or more persons.

<sup>4</sup> The report is entitled *Modernizing the Financial System: Recommendations for Safer, More Competitive Banks*. The report was introduced as legislation in the Senate and House of Representatives on March 20, 1991 as Senate Bill S.713 and House Bill H.R.1505, respectively.