What happens if the bank fails? essay

Business, Industries

Due to worldwide financial crisis many people now are thinking of ways on how to survive to these economic challenges. Many people are worried about their money, finding ways to find safe means for their financial security.

People are saving and investing their money in a bank, but what if many banks nowadays are closing as an effect of economic crisis. The current global financial crisis which started in the early 2007 is due to the failure in the United States real state and development loans. This situation affected different markets and economies since failures brought weakness to market structures and regulations (Searles 1). The most important thing to focus right now is to deal with financial challenges confronting our country's economy in accordance with appropriate guidelines. Financial institutions mostly in highly developed countries failed which resulted to buyouts and the government of these nations needed to provide rescue packages to support the financial industry of their own country. The Federal Deposit Insurance Corporation (FDIC) listed almost 117 banks with assets over $78 billion before 2008. In order to The US treasury and FDIC Bank regulators are responsible for encouraging banks to take particular procedures to ensure security and protection of the entire banking system. In this time of crisis they are the ones trying to improve and regulate credit-risk management and measures on how to improve banking transactions.

Many small banks or even big ones were having a hard time coping up, if this chain of problems continues to occur closing the bank would be the worst consequence. The Federal Deposit Insurance Corporation is the federal agency that takes over small banks; however the FDIC ensures safety to every depositor's money because the FDIC is giving deposit insurance.

According to the book entitled New York Countdown Coach, the FDIC created not only to provide insurance to every deposit but as well as to regulate the United State banking system. According to the report prepared by the Federal Deposit Insurance Corporation regarding their Resolution Process which will take for 90 to 100 days, the FDIC claimed that they always perform a resolution process; this includes a specific plan for closing a particular bank or financial institution. However there are cases wherein resolution process cannot be completed and as a result plenty of liquidity problems will occur. There was this so-called Bridge Bank, designed for operation maintenance of a bank until stable and accurate solution for the problems completed. FDIC is processing first the failing bank letter to notify the institution, developing an information package which includes the amounts and assets of that particular institution.

The FDIC will conduct an asset valuation and the agency determines the suitable resolution arrangement, and conducting an on-site analysis for preparation before closing the failed institution. In preparation for closing, the FDIC measures the quantity and amount of uninsured dollar deposits at the bank. They also investigate any potential fraud through analyzing documents submitted and recovered by the failed bank. The FDIC will market the failed bank as soon as possible in order to attract and encourage buyers of the failed banks asset. There are signs to identify if the bank is in trouble first the stock value decline; secondly there is a high executive turnover, and also unexplained changes occurred in the management (Dennis III 1).

There are different ways the FDIC takes over a particular bank, the agency can close and pay all depositors, or manage and run the bank, or the most popular way to find a buyer or liquidating the bank's assets. Moreover the FDIC can provide financial support to failing banks. The FDIC receivership process is implemented to value and assess a failed bank and put it again to the market to sell failed bank's asset. FDIC gives importance to pay insured depositors even the uninsured depositors. During 1991, the United States congress passed the so-called Federal Deposit Insurance Corporation Improvement Act (FDICIA) in order to prevent banks to fail.

This act was proposed to penalize banks if they will engage in high-risk activities and this act was intended to reduce regulatory costs of troubled banks (Madura 513). The FDIC is arranging and planning a merge with other stable bank, the FDIC also has the authority to sell some bank assets to another bank, and if selling of bank assets is not possible the FDIC will sell government securities instead. The FDIC will choose and absorb those failed bank's asset not the good one for the purpose of preventing new problems that may occur if they will sell failed assets to acquiring banks (Sprague 224). The liquidation of assets starts at the main office then followed by regional and sub-regional offices where these offices are classified by category and supervised by a particular specialist selected by FDIC. However if the business asset is continuously operating, FDIC will allow it to operate to maintain its value until the business recovers from trouble (Sprague 225). The FDIC is preparing a list of potential bidders, buyers or acquirers among financial institutions and even from private sectors who are worthy and afford of acquiring additional assets.

The Board of Directors of FDIC is responsible for determining and implementing the low cost transaction and the Board of Directors also announces the winning bidder of the failed bank’s asset. The FDIC also balances the accounts of the failed bank and prepares specific documents directly after closing to properly transfer assets to the buyer and most importantly the agency determines the amount of assets for the payment transaction. Those who will win the bid is required to conduct due diligence at the failed bank. Due diligence is the inspection of records, accounts and books of the failed bank in order to assess the value of assets.

The board of directors of the failed bank are responsible for authorizing FDIC to accomplish due diligence before the inspection. The government securities are issued by the United Sates government, these securities is the most creditworthy since the United States government fully supported this kind of credit. The money of all depositors are insured by FDIC, therefore if the bank fails, depositors will going to receive specific amount insured by the FDIC. The FDIC insures deposits into two separate funds, first is from the BIF (Bank Insurance Fund) where FDIC insures all insured or uninsured state and national banks that are members of FRB. On the other hand is from the SAIF, where the FDIC insures the entire federal savings and thrift banks, and including loan association institutions (Carmichael & Whittington & Graham 9). The amount insured is up to $100, 000 (principal and interest already), however retirement accounts and money market accounts such as IRA, Roth IRA and SEP IRA are insured up to $250, 000.

For joint accounts, the amount insured is up to $200, 000 and $100, 000 insurance for those having beneficiary trust (with one beneficiary) (Searles 1). According to the consumer news released by the FDIC (2008), if your money in the bank exceeds $100, 000 then you can recover some additional money aside from the insured $100, 000 but there is no assurance that you will get everything, it depends on how much the FDIC recovers through selling bank's assets to lenders. However individuals who deposited on uninsured bank, means their deposits are not covered by FDIC insurance. But usually uninsured depositors can receive some money or percentage of their deposits at the failed bank but still FDIC will based it on how much they will recover from liquidation of the failed bank's asset (Weinstock & Breckinridge 2). In today's financial crisis, the Federal Deposit Insurance Corporation provided new rules for banks and financial institutions for monitoring in order to protect the interests of American depositors.

There are some changes on FDIC rules regarding deposit insurance and failed banks; one of those is the plans of FDIC to create automated sweep transactions at all banks. The FDIC will not give insurance to swept funds that are transferred from insured accounts to non-insured accounts. The FDIC will continue implementing this new deposit rule until July 1, 2009. Another new program was recently imposed and created by FDIC; the agency announced the temporary liquidity guarantee program which addresses the need for effort to strengthen confidence in depositors, lenders and other investors and foster liquidity in banks and thrifts.

This guarantee program was formed last October 14 of 2008 and the FDIC applied it to all United States domestic banks for 30 days. During the imposition of the guarantee program, many banks seem to be committed to pay assessment in order to provide unlimited protection and financial security for their depositors (Weinstock & Breckinridge 1). According to report prepared by Janney Montgomery Scott LLC (2008): Investors that understand the details behind FDIC coverage have an advantage in ensuring they're adequately compensated for the risks they're taking.

In this kind of challenging financial environment where people are worried and at the same time trying to find some ways to save and protect their money we should become informative of rules and regulations of different institutions. It seems that one of the most important focuses of people right now is securing a better future than having the ability to be creative at will, to solve problems, and develop new ways in order for us to survive in these challenges. Even though measures, decisions made and approved can worsen or lessen the effects of economic condition, still the most important of all is to exert greater efforts to deal with this economic crisis that affecting the lives of every single American.