So You Think Your Bank is Solvent

By: John Pico, BA, JD

You may think your bank is secure, but suppose there is a financial crisis and you need your money immediately, along with hundreds or thousands of other depositors.

On March 18, 2023, the NY Post reported that **nearly 200 banks are at risk** for same fate as SVB: study and that "*Even insured depositors — those with $250,000 or less in the bank — could have problems getting their cash if these institutions face the sort of run that SVB saw a week ago.*"

It is a 99.9% certainty that your bank won't have the money and/or you will not be able to get your money quickly.

The fact is that banks do not keep your deposit in their safe. They loan it out to other people and, if all of the depositors wanted their money, your bank could not produce it.

The United States banks, and most world banks, work on a **fractional reserve banking system.**

Under the Federal Reserve Act of 1917, banks, depending upon size, were required to retain only 13%, 10%, and 7% of its deposits. Over the years, the amount of reserves required to be kept fluctuated between eight and eighteen percent.

Then, the Board reduced reserve requirement ratios to zero percent effective March 26, 2020. This action eliminated reserve requirements for all depository institutions. (*See: Federal Reserve Maintenance Manual, November 2019, pages 15 & 16.*)

Effective January 3, 2023, the Board was amending Regulation D, Reserve Requirements of Depository Institution to raise the reserve requirement exemption amount and the amount of the low reserve tranche, but noted that "The annual indexation of the reserve requirement exemption amount and low reserve tranche, though required by statute, will not affect depository institutions' reserve requirements, which will remain zero[1]."

Today, American financial institutions only retain enough cash on hand to cover a fraction of their deposits. That is why bank runs, as demonstrated by the Silicon Valley Bank run, can cause a bank to go under.

While it is true that the FDIC insures bank deposits up to $250,000, you could still easily find yourself separated from your cash. See: where a **Wells Fargo computer glitch** caused money in customers' "*accounts to disappear, leaving behind negative balances and overdraft notifications*."

There are also more draconian reasons you could lose access to funds. See for example, where the Canadian government **seized the bank account of a single mother** because the politicians in power did not like the fact that she donated $50 to truckers protesting against the Covid vaccine.

When you deposit money in a bank, you lose control of your money and rely on (1) the bank's good faith; and (2) the government's good faith that you can get your money bank when you want it.

You also rely on the fact that there won't be any power outages, or other crises intervening to delay your demand for funds.

The moment you give someone else something of yours to hold, you are relying solely on trust that you will get it back.

It doesn't matter what the person says, signs or pledges, if you can't hold it, you don't own it.

There are thousands of examples supporting that statement. All of Bernie Madolff's clients thought Bernie was holding "their" money. All of Sam Brinkman-Freid's customers thought he was holding "their" money. And, finally all of Silicon Valley Bank's (SVB) customers thought it was holding "their" money.

If it is not in your hand, you don't really own the object; you are merely the beneficiary of a promise. That is why is good to keep a portion of your assets in your personal possession, in cash and cash commodities (e.g., gold, silver, platinum) and to keep them secured in a safe deposit box, or some other insured location.

[1] Section 19(b)(2) of the Act (12 U.S.C. 461(b)(2)) authorizes different ranges of reserve requirement ratios depending on the amount of transaction account balances at a depository institution. Section 19(b)(11)(A) of the Act (12 U.S.C. 461(b)(11)(A)) provides that a zero percent reserve requirement ratio shall apply at each depository institution to total reservable liabilities that do not exceed a certain amount, known as the reserve requirement exemption amount. Section 19(b)(11)(B) provides that, before December 31 of each year.

Mr. Pico is a retired attorney and managing partner of Advising Automobile Dealers LLC, with 50-years experience in mergers/acquisitions, dealership valuations and bankruptcy workouts. His expertise has been recognized by both state and federal courts.