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FEDERAL DEPOSIT INSURANCE CORPORATION

# Consumer News



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News and Information On Consumer Issues from the Federal Deposit Insurance Corporation

WINTER 1994/95

VOLUME 2, ISSUE 2

# MONEY



Illustration by T.W. Ballard



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come from?**

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# Where Did All That Money Come From?

## A brief history of "scratch" and "spondulix"

It's the root of all evil. It burns a hole in your pocket. It can't buy happiness. But it makes the world go around. And we can't live without it—not very well, anyway. Since the Chinese invented it about two thousand years ago, it's taken such varied forms as stones, beads, nails and even playing cards.

So what's the origin of this stuff — this moolah, cabbage, scratch, these spondulix, fins and sawbucks and an endless number of other nicknames — that falls through your fingers like water and disappears so fast that you can't remember what you did with it? Yet we can all recall how we earned it — and we all complain about how it's not worth what it used to be. It's almost ritual to complain about money: "It's not pretty like the currency of other countries." "The government takes most of it anyway." How often have we heard laments like these? Yet, if you travel outside of the U.S. and have to exchange your currency, don't you feel a pang of regret when you give up those familiar bills and receive others with pictures of people you probably never heard of on them? Let's face it: we have a love-hate relationship with our money!

Before you let it slip away as it does with such amazing rapidity, why not take a quick look at it. Bills are works of art — the Great Seal of the United States and other elements of the designs each has a story of its own to tell. You wouldn't believe what our money has gone through to



Photo: 20th Century-Fox/Photofest

*Fortune-seeker Edgar Hopper (Dick Van Dyke) buried himself in cash and promptly worked himself to death in the 1964 comedy "What a Way to Go."*

get to what it is today. Money doesn't just change hands, it also changes to adjust to social, political and other influences. Those changes have been purposefully subtle and have evolved over long enough periods of time so that our citizenry has no reason to doubt its currency's validity. Even with some changes coming along to improve its security (see story on Page 7), there is no reason today to worry about the worth of our money. It's rock-solid. Residents of some other countries haven't been so lucky.

### The early days

Confidence in our currency would have been hard to come by when the country got started, because we didn't have any currency. England didn't bother to issue any money for her colonies in the U.S., but pioneer ingenuity took over. Supplies of all sorts were scarce in the 1600s when

the first folks arrived. Nails were such a rare commodity that they became currency, which is, after all, simply a means of trading one thing of value for another. Native Americans and French traders used wampum, or beads, as a means of exchange. Other countries had similar experiences. In Canada's colonial times, a currency based on playing cards was set up when nothing else was available. And the wealth of Yap Islanders in the Pacific even today is represented by various-sized stones, carved in a donut shape, placed outside their homes.

Well, our colonists realized pretty quickly that nails and other rare items couldn't continue to serve as money-substitutes, so they decided to use the Spanish and French coins that were circulating at the time. Then the colonies began issuing bills and by 1750 or so, each of the 13 original states had its own paper currency. You can imagine how confusing that must have been! Bills generally were small rectangles that came in strange (to us) denominations, such as seven dollars. Nevertheless, that system survived through the Revolutionary War, until Continental Currency was issued in 1776, shortly after the signing of the Declaration of Independence. But there just wasn't enough of it, and it depreciated until it was no longer accepted by merchants and others. So it was no longer issued after 1781 with the result that the U.S. government didn't issue any paper money for 80 years, leaving the task to private institutions.

After Continental Currency became worthless, it fell to Alexander Hamilton, the first Secretary of the Treasury, to establish a national currency system. This he did, most notably drawing up the plans for the U.S. Mint, which was authorized by Congress in 1792. The Mint's first facility, in Philadelphia (then the nation's capital), issued the first circulating coins — copper cents — in 1793. The Philadelphia Mint was the nation's only minting facility for 45 years. Over that time and to this day, many varieties of our coinage have been minted — lots of some and few of others, providing a fertile ground for collectors in one of the most popular hobbies in the country.

Meanwhile, the states continued to issue their own paper money. During the Civil War the country's finances were a total mess as the Union and the Confederacy each issued their own money to pay for soldiers' salaries

and goods needed to fight the war. The first issues of U.S. paper money, called "greenbacks," appeared in 1861. They were called greenbacks because, like today, the backs of the bills were printed in green ink. The new money helped meet expenses temporarily, but after it was obvious that a huge shortage still existed, Congress passed the National Banking Act of 1863. This law created national banks, which could issue currency backed by U.S. bonds. Congress soon amended the law to ban the states from issuing



The original Philadelphia Mint, built in 1792, was the first and only place where U. S. coins were made for 45 years.

(Photo U.S. Mint)

currency and that was that — the federal government assumed complete responsibility for issuing U.S. currency, and bills and coins issued by the states became destined for collectors.

## Modern times

Today, the U.S. Bureau of Engraving and Printing (BEP), which is part of the U.S. Treasury Department, prints all of our paper currency, most postage stamps, U.S. securities and other items. The tour of BEP's "money factory" in Washington, DC, is one of the most popular in the nation's

capital. It's hard to believe that this extensive operation, with a subsidiary in Fort Worth, TX, began business in 1862 with only six people working in a basement room of the Treasury Department (pictured on the back of the \$10 bill, by the way).

Today there are Mints in Philadelphia, Denver, San Francisco and West Point, NY, as well as the depository in Fort Knox, KY, that contains U.S. gold reserves. Originally part of the State Department, the U.S. Mint became an independent agency in 1799 and part of the Treasury Department in 1873; it remains there today.

Over a million people in the U.S. collect coins and/or paper currency. And it's an excellent hobby for

children. Many books, magazines and newsletters about this popular pastime are available at libraries and bookstores or by subscription. So read more about numismatics; you can start with free pamphlets and other information offered by the U.S. Mint and the Bureau of Engraving and Printing. (See Page 10 for where to write.)

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### FDIC Consumer News

is published quarterly by the Federal Deposit Insurance Corporation

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## Why is Our Money Green? . . . and other trivia

### The color of money

No one is certain why U.S. paper money is green, but the generally accepted explanation goes like this: In 1929, the size of our currency was reduced to what it is today, and certain features of the bills, like portraits, emblems and monuments,

were standardized. At that time, green ink was plentiful and was known to stand up to a lot of handling. And, says the Bureau of Engraving and Printing, the color was thought to represent stability and strength.

Green ink also seemed to best meet certain requirements of the printing process used then for manufacturing the bills. And, as various changes were made to bills since then, the green tint was simply retained as the basic color.

### Is there really gold in Fort Knox?

Auric Goldfinger knew what he was after when he tried to raid the U.S. Mint's installation at Fort Knox, KY. Just how many gold bars are there isn't public knowledge, but each one, about the size of a building brick, weighs about 27.5 pounds. Each brick, or bar, is worth about \$17,000. As for paying a social call to visit what's backing up our bucks, forget it. Maybe James Bond could fly in and save the day, but that only happens in the movies. In real life, no visitors are allowed at Fort Knox.



Photo: United Artists/PhotoTest

Above: The Fort Knox of Hollywood, where in the 1964 thriller "Goldfinger" visitor James Bond (Sean Connery) was "allowed" in to stop an atomic bomb from detonating with exactly 0-0-7 seconds to go.



Photo U.S. Mint

Left: The real Fort Knox of Kentucky, where no visitors are allowed inside the mighty walls and gates that house U. S. gold reserves.

### Is there "gold" in Grandma's trunk?

If you find old bills in your attic, or anywhere else, and you think they may be valuable, you can send them to the U.S. Treasury Department (Washington, DC 20220), which will redeem them at face value if they are genuine U.S. currency. But the Treasury will NOT place a value on your find. You need to contact a currency dealer to do that — they're listed in the yellow pages of your phone book under "Coin Dealers."

And if you happen to find a \$1,000 note on the Bank of the United States bearing the serial number 8864, containing six portraits and made out to A. Fairman, PLEASE do NOT send it to the Treasury Department. Although there once was a Bank of the United States (1816-1841), the bill is not genuine and is therefore worthless. Seems the fake

notes were issued in 1967 as part of a promotional campaign by a record company. And the company sent out a lot of them. The Treasury Department received so many inquiries about this particular note that it printed an explanation to respond to the huge volume of mail. The heaps of letters did not amuse the folks at the Treasury who had to answer the mail or numismatists who were presented with these replicas by people who thought they were valuable and wanted to sell them. And, who had some really creative explanations for their origin, including "I found it in grandma's trunk" or "Grandpa left it to me in his will" and other fantasies reported by a trade magazine of the time. A replica of the fake note was even used by a check-printing company some years later as artwork on boxes of checks sent to customers.

## Salmon P. Chase, where are you?

In case you've missed seeing this Secretary of the Treasury (1861-1864) on your currency (his portrait appears on the \$10,000 bill), it's because bills in denominations of \$500 and over were taken out of circulation in 1969 as a deterrent to criminal activities. So don't look for James Madison (\$5,000), Grover Cleveland (\$1,000) or William McKinley (\$500), either.

Who's on what bill is only one of the many facts about our money contained in the informative pamphlets available from the Bureau of Engraving and Printing and the U.S. Mint. (See Page 10 for where to write.)

## Speaking of numbers . .

- A stock of currency one mile high would contain over 14 1/2 million notes.
- If you had 10 billion \$1 bills and spent one every second of every day, it would require 317 years for you to go broke.
- You can fold a bill about 4,000 times — back and forth each time — before it will tear.

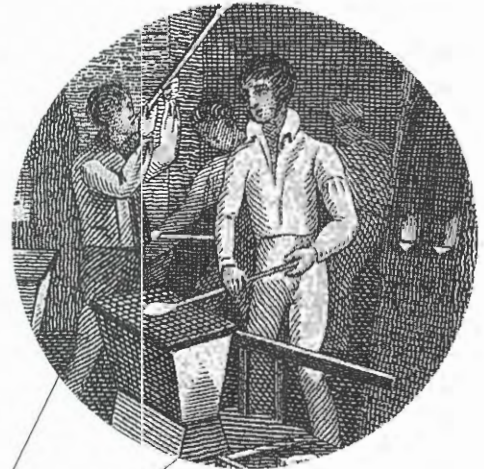
## Final thoughts

Interested in learning more about the Great Seal of the United States? Why it contains pyramids and other Middle Eastern symbols? Want to know the origin of the dollar sign? Why our bills say "Federal Reserve Note"? What that tiny "D" on some pennies means? More information about these and other fascinating aspects of our currency are as far away as the sources listed on Page 10 or your local library.

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## Elvis sighted? Not on OUR money!

Seems a dealer in North Carolina noticed that a figure pictured on an obsolete bank note looked amazingly like "The King." It must be the white suit and the sideburns. Whether or not you believe "Elvis Lives," the bank note is a collector's item. To see the real Elvis on currency, you need look only as far as the Marshall Islands, where the Marshall Islands have just issued new \$5, \$10 and \$50 coins bearing his likeness. The coins are legal tender there but not in the United States.



(Credit: Claud Murphy, Jr.)

## Does Your Money Have the Right Stuff?

### A few tips on spotting the real thing

How can you tell if the money you have in your wallet or you receive from merchants is the real thing and not counterfeit? While it may not always be easy, here are some ways you can spot the genuine article.

#### 1. Notice the feel.

U.S. currency paper is strong but still pliable because it's made of 75 percent cotton and 25 percent linen. The designs are produced from engraved plates that give new notes an embossed or raised feel.

#### 2. Hold the bill to the light.

On the left side of many newer bills, starting with the \$50 and \$100 notes in 1990 down through newly printed \$5 notes today, you'll see a printed strip between the Federal Reserve seal and the outer border showing "USA" and the note's value.

#### 3. Get out your magnifier.

Higher denomination bills have a fine line around the portrait. But when magnified, you'll see it's not a line at all, but "The United States of America" printed repeatedly.

#### 4. Check out the details.

The fine lines around the border of the bill should be clear and unbroken. The lacy, web-like design inside the border also consists of unbroken white lines. Throughout the bill, tiny red and blue fibers are embedded in the paper.

#### 5. Notice the portrait.

The faces of Washington, Lincoln and the other American statesmen on the currency should appear lifelike. The eyes will almost sparkle and the portrait will stand out distinctly from the fine, screenlike background.



[Photo: 20th Century-Fox/Photofest]

Loveable Skipper Miller (Edmund Gwenn) uses an old printing press to make \$1 bills in the 1950 comedy "Mister 880." Today's real-world counterfeiters use sophisticated photocopyers and are no laughing matter.

While this short primer won't turn you into an expert on spotting counterfeit money, it just may make you a little more aware of how you can check on some of the security measures the government takes to protect our currency.

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## Current



## U. S. Currency to Get a Face-lift

### But don't worry... Changes won't affect the value of your money

The U.S. Treasury Department is working on a redesign of our currency — the first major overhaul of paper money in 65 years — to stay ahead of counterfeiters. But don't worry. It won't happen overnight and it won't change the value of our money. Your old bills will still be good.

The first of the new notes will be that favorite of counterfeiters, the \$100 bill. It will debut in 1996, and the other denominations will follow in descending value, every six months to a year or so.

The overhaul is needed because counterfeiters are now using highly sophisticated photocopying equipment. To thwart the criminals, the Treasury is considering making the portraits larger and more

detailed, so they become distorted if photocopied. Also a watermark — an image that is only visible when the note is held up to the light — of the person pictured on that note may be added. Other changes may include embedding in the paper bits of shiny paper that won't reproduce and creating a background that will become distorted if photocopied.

Whatever the final design changes, the "new" bills will still have the traditional look of U.S. money.

"The new currency will maintain its current size and colors, with portraits of the same historical figures on the faces and the same buildings or monuments on the backs," Mary Ellen Withrow, Treasurer of the United States, told Congress last summer.

Another feature that may be included is called color-shifting ink. This means that when the bill is viewed directly the ink appears to be the traditional

green, but when the bill is turned at an angle, it changes to gold.

Also included will be hidden features that can be identified only by machines at banks and businesses, making it easier for the banking system to detect counterfeits.

The Treasury Department also will be undertaking a massive worldwide campaign to explain the new security measures to the public. This educational program will be international because U.S. currency has become a world standard. The Federal Reserve Board says that of the \$357 billion in U.S. currency in circulation, about \$200 billion is overseas. Most of the counterfeit notes are there, too.

With improvements in photocopying machines and other means of reproduction, experts say the public should expect currency to continue to change with ever-advancing technology.

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### Proposed

Larger  
off-center  
portrait

Inks change  
color depending  
on the angle  
viewed



Matching  
portrait  
only visible  
when held  
to light

Shiny bits  
of tissue  
built into  
paper

# Cash or Trash?

## Weary greenbacks and coins don't just fade away, they get recycled

You know money doesn't grow on trees, but did you know it could be expanding (or contracting) on top of your roof...as shingles? That's because a lot of the bills that were in your wallet just a few months ago by now have probably been declared unfit by the government and given a new life — recycled into roofing shingles and other products.

Most of us probably don't appreciate what the government goes through to take money out of circulation efficiently and safely. Nor do we quite understand what to do with the worn-out bills and coins in our possession. That's why **FDIC Consumer News** has put together a guide to how the government handles our tired bills and coins — including the ones so dirty or mangled even the biggest spender in your family probably wouldn't use them.

Much of what follows in question-and-answer format may surprise you...and maybe even help you put some crisp and clean *new* money in your pocket.

### **How long does paper money stay in circulation before it's no longer usable?**

It depends on the denomination. As you'd suspect, smaller bills are handled more frequently by the public and get torn and worn a lot faster than the rest.

The \$1 bill has the shortest average life span — just 18 months. Next

comes the \$5 bill, at two years. For the \$10 and \$20 bills, the average life is three years and four years, respectively. The \$50 and \$100 bills don't get that much of a



*Jim Reese, senior vice president of the Federal Reserve Bank of Richmond, takes comfort in some of the 7,000 tons of paper money shredded and recycled each year.*

workout, so they're in circulation about nine years. Even though the \$2 bill is a small denomination, the public hasn't quite accepted it and therefore it hardly ever gets replaced because of wear and tear.

### **Are we talking about a lot of money needing to be replaced?**

Yes, even by federal government standards. Each day, the U.S. Treasury Department's Bureau of Printing and Engraving cranks out 35 million crisp new bills with a face value of \$465 million, and 95 percent of those are to replace bills that are worn or damaged. Nearly half of all the bills printed by the Treasury Department are \$1 bills.

### **So how do faded or damaged bills go from our**

### **wallets to the government recycling bins?**

Consumers turn in some of this "bad" money, but the overwhelming majority is spotted and removed from circulation by the 12 regional Federal Reserve Banks and their branches. Each day, the Fed examines millions of dollars deposited with them by banking institutions as part of the routine coming and going of money through the financial system.

The Fed runs each note through a high-speed sorting machine that checks for holes, tears, tape or other problems. (The machine also rejects suspected counterfeit bills, which are visually inspected and then forwarded to the U.S. Secret Service to investigate.) Although some of the bills flagged as worn or torn are sent back into circulation, most are directed to a special shredder and then on to a machine that compresses this green confetti into "bricks" or "bales." Each year, the Fed shreds about seven billion notes, adding up to about 7,000 tons of money.

### **That's a lot of confetti. What does the Federal Reserve do with the money next?**

Unfortunately, the Fed can't just recycle this shredded money into new currency because the quality of the paper wouldn't be up to the high standards needed to separate the real thing from counterfeit bills. Until recently, the Fed's regional offices had been disposing of this currency

[Photo: Federal Reserve Bank of Richmond]



in landfills. Some also went to law enforcement agencies to help train police dogs that sniff out drugs and drug money. But more and more, the Federal Reserve Banks have been giving large quantities to private companies that will haul the paper away at no charge and recycle it. This arrangement is easier and cheaper for the Fed than continuing to pay for the material to be removed, and it's a great way to cut the environmental costs of using landfills.

We already mentioned that one company is using shredded currency in its roofing shingles. Others are putting it in such products as fuel pellets for electric power generators and fiberboard panels for stage sets and trade show displays. Many more industrial uses are under development, reportedly including products such as protective barriers along highways. Manufacturers aren't just being good citizens helping the Federal Reserve dispose of a lot of paper. Among other things, they say the cloth-like mixture of cotton and linen in the bills could make their products stronger and more flexible than other materials. Of course, some entrepreneurs also are buying the shredded currency and turning it into artwork, green-tinted stationery, statues, souvenirs and other novelty items including, as you'd probably expect, bags of shredded currency for sale.

### **Can private firms or individuals do anything they want with the shredded currency?**

No. The Federal Reserve Banks and the private companies they contract with must follow strict guidelines and

procedures set by the U.S. Treasury Department's Office of Currency Standards intended in part to protect our health and our environment. For example, because of the various chemicals in the ink, private companies cannot use shredded currency in any product that could contain food or drink, in fire logs or other products where the chemicals could be ingested by humans, animals or plants.

If you want more information about obtaining and recycling shredded currency, contact a nearby Federal Reserve office listed in the U.S. Government section of the telephone book. If you can't find it listed there, ask for help from the Federal Reserve System office listed on Page 15 of this newsletter.

### **Can average citizens turn in damaged bills? Where, how, and how much can you expect to get back for them?**

It depends on the condition of the bills. The government classifies damaged bills into two categories — mutilated or not mutilated — and each is treated differently.

### **What's mutilated currency, and how is it handled?**

A mutilated bill has no more than half the original note remaining and/or requires special examination by the government just to determine its value. The most common causes of mutilation include fire, flood, chemicals, explosions, animal or insect damage, and deterioration from being buried. People can still get full face value if the Treasury Department is able to authenticate the bills and is convinced that the missing portions have been totally

destroyed. (The latter requirement is to prevent two-for-one sales. That is, the Treasury doesn't want you to be paid \$100 for a mutilated \$100 bill and then have someone else demand \$100 for the rest of that same note.)

The Treasury performs 30,000 of these examinations and sends out checks totaling about \$30 million each year. There is no fee for this service, other than your shipping or mailing costs.

If you want to submit mutilated bills for examination and redemption, write or call the Treasury's Bureau of Printing and Engraving to request information about its service and the safest ways to send in your currency (address and phone number are listed in the box on the next page). And don't take mutilated bills to your bank or the Federal Reserve because they don't have the staff or the equipment to examine or process them.

### **What about bills that are dirty or worn but aren't mutilated? Can't we just take them to our bank?**

Yes. Even though banks, savings institutions and credit unions are under no legal obligation to exchange these bills, they generally will do so as a courtesy. In all likelihood you can expect to get your face value back on the spot, assuming there are no other problems, like your faded bill turns out to be counterfeit. Likewise, your grocery store or gas station or any other merchant is under no legal requirement to accept or exchange a scruffy-looking bill, but many do so

(Continued on next page)

anyway. Another option, if it's convenient, is to take these bills to a nearby Federal Reserve office, which is where your financial institution will send them eventually.

### **What about coins that become damaged?**

Coins are much more durable than paper money — they last about 30 years under normal usage. But they, too, become worn or damaged. When that happens, the coin most likely will be caught by the Federal Reserve's sorting machines. But individual consumers sometimes have reasons for wanting to turn coins in. As with the paper variety, coins are classified as mutilated or not mutilated, and each comes under different rules for redemption.

### **What's a mutilated coin, and where can we exchange it?**

A coin is mutilated if it's bent, chipped, corroded or melted together and not machine-countable. According to the U.S. Mint, there are three ways that coins typically get mutilated: they're left in a fire; they're under water in fountains for prolonged periods; or they're recovered from autos at the junkyard. And yes, coins get mutilated a lot more than you'd probably think. In 1993, the public sent the Mint about 500,000 pounds of mutilated coins, for which checks totaling \$5 million were mailed back.

To cash in mutilated coins, you must send them to the Mint's Coin Redemption Branch in Philadelphia, PA. There is no charge for this service. Your only costs are to cover the shipping. But before sending in any mutilated coins, contact the Mint to get more details and instructions

(see address and phone number at right). For example, the Mint pays more if you separate your coins by category (cents, nickels and so on) than if you mix them all together. You also can't just send in a few coins; the Mint requires at least one pound per category of coin or two pounds of mixed coins. And don't try to exchange mutilated coins through banks or the Fed; they're just not equipped to handle them.

### **And what about coins that are very worn but aren't mutilated?**

Coins that are worn or dirty but still can be recognized and be counted by machine can be redeemed in a few places. You can send them to a Federal Reserve Bank or branch. Or you can ask if your bank would accept and redeem them. No matter what, these coins will end up back at the U.S. Mint.

### **Does the Mint recycle these worn-out coins it receives?**

Yes. The Mint melts coins and sends this and other scrap metal to contractors; sometimes the scrap is even returned to the Mint in metal used to make new coins. The Mint also is increasing its use of private contractors in order to cut pollution from its own melting operations, save energy and reduce production costs.

### **OK. What can we do to prevent money from becoming worn or mutilated in the first place?**

Lots of things. For example, you can always deposit it into a federally insured institution. Or...you can spend it as fast as you can!

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## **A Wealth of Information**

These government-related offices have free or low-cost materials about money.

### **Bureau of Engraving and Printing**

Office of Communications  
14th & C Streets, SW, Room 533M  
Washington, DC 20228  
Phone 202-874-3019

Brochures and information about paper money include: "Your Money Matters" (measures to deter counterfeiting); "Preparation and Redemption of Mutilated U.S. Paper Currency" (how to redeem ruined money); "The Money Factory" (a brief history of the Bureau); "A Treasury of Gift Ideas" (catalog for ordering uncut sheets of currency, engraved Presidential portraits, etc.); and public tour information.

### **U.S. Mint**

Customer Service Center  
10001 Aerospace Road  
Lanham, MD 20706  
Phone 202-283-COIN (2646)

Publications explain the history of the Mint and how coins are made and redeemed by the government. Gives information on coin offerings and tours. You can be placed on the Mint's "customer mailing list."

### **Federal Reserve Bank of New York**

Public Information Dept.  
33 Liberty Street  
New York, NY 10045  
Phone 212-720-6134

Its "Public Information Materials" catalog lists hundreds of booklets, films and other items dealing with money and banking. Among the offerings: "The Story of Money," a comic book for youths and adults. (Both publications are being updated and will be available approximately April 1, 1995.)

### **Consumer Information Center**

Catalog  
Pueblo, CO 81009  
Phone 719-948-4000

Provides free and low-cost booklets published by more than 40 federal departments and agencies on many subjects, including how to deposit and invest your money. First call or write for the free catalog.



## Answers to your questions about deposit insurance and other consumer protections

### The \$100,000 question

*"To flatly state that deposits should not exceed FDIC insurance limitations is a major disservice to many fine financial institutions which have worked long and hard to attract depositors with significant balances. Clearly people need to be informed, but the ultimate decision should be a business decision on the depositor's part."*

- Santa Fe, NM

*"Most financial institutions work very hard at establishing relationships with their depositors and would like to take care of their needs instead of encouraging these clients to seek 'relationships' elsewhere. Some uninsured money can become insured by restructuring the accounts within the existing institution."*

- Minneapolis, MN

We seem to have struck a nerve in suggesting in previous issues that depositors who have accounts exceeding the \$100,000 insurance limit might want to consider moving their uninsured funds to another institution. That is certainly an option for people who are concerned about full deposit insurance coverage. However, there may be other choices for them, such as opening different types of accounts and restructuring existing accounts, that

still provide full coverage under the rules. So those of you who want full coverage should check at your institution to see if your particular situation can be adjusted so that all of your funds can remain where they are with full coverage. If there are no other alternatives for you, and you believe you need full coverage, then we still suggest that you consider moving any excess funds to another institution.

But what if you've customarily kept balances over \$100,000 and full insurance coverage is not that important to you? After all, deposit insurance only applies if a bank or thrift fails, and the number of failures has slowed to a trickle in the past year or so. And perhaps you've been doing business with the same financial institution for years and you don't even think about deposit insurance coverage? Of course you — and any other customer of a financial institution — should do whatever feels comfortable.

Whether or not your accounts are set up so that they're fully covered, in the event of a failure, is strictly your own business decision. Trouble is, many people don't pay enough attention to their finances or the institutions where they do business. It's these folks we're talking to when we say make sure your funds are fully protected, not those who monitor their financial situation — and their financial institution (see "How Healthy Is Your Bank?" in the Spring 1994 issue) and have made

an informed decision based on their own research and experience.

People who don't pay attention to their accounts or deposit insurance coverage invariably were the ones, during the period when a lot of bank failures occurred, who said after they lost at least part of their uninsured funds, "I didn't know"; "No one told me"; "I thought I was covered" and similar complaints. So, if you're not worried about having uninsured funds, fine. But all of us should simply be aware of the possibility that some funds could be lost if a financial institution fails.

Also, remember that if your personal situation changes, your deposit insurance coverage may change, too. For example, if one of the owners of a joint account dies, the survivor could become the sole owner of funds that, when added to the survivor's other single ownership accounts, might then exceed the insurance limit. Under any circumstances, depositors concerned about insurance coverage should review their account balances and the insurance rules from time to time. Insurance questions? Contact the FDIC at the offices listed on Page 15.

•••

Got a question? Send it to **FDIC Consumer News**, Office of Corporate Communications, 550 17th Street, NW, Washington, DC 20429. We'll answer as many as possible.

# Your Home is Safer on a Mountain (of Paper)

## How all those mortgage forms protect you

If you've ever applied for a mortgage loan, you've probably wondered: Why are my banker and lawyer asking me to look at and sign so many pieces of paper? Why do they need so much proof about things like the exact location of the house? (Don't *they* know where the house is?) Did it take this much effort for the Dutch to buy Manhattan?

You're right. There *are* a lot of documents you'll be asked to review and approve in order to get a mortgage. And sure, a lot of these documents are to protect the lender, who could be out big bucks if your loan goes bad, or there's a dispute over the dimensions or ownership of the property (that's why land surveys and title searches are done). *But a major amount of this paperwork is to protect you, the home buyer.* After all, buying a home could be the most expensive thing you'll do. That's why Congress and government agencies require certain procedures to help ensure that you are:

- Treated fairly by the lender and other professionals you'll be dealing with;
- Told how much you can expect to pay for your loan, insurance, property appraisals and other services, and of your ability to comparison-shop for the best deal;
- Clear about your obligations to make timely loan payments and fulfill

other responsibilities, and that you're aware of serious consequences if you don't; and

- Informed of your rights to complain or file a lawsuit if you believe you've been treated unfairly or illegally.

*FDIC Consumer News* has put together the following overview of the "disclosures" (government-talk for special notices and alerts you must be provided) and the other documents you'll most likely see if you apply for a loan from a bank, savings institution or credit union. Most of these documents are required by federal laws such as the Real Estate Settlement Procedures Act and the Truth-in-Lending Act, and certain state laws. This story focuses only on the typical loan for a home purchase arranged through a bank or other depository institution. It doesn't cover every type of home loan or lender. Additionally, many, but not all, of these same requirements also apply to home improvement loans, home equity loans and loans to refinance an existing mortgage.

### When You Apply for a Mortgage...

#### 1. You'll be asked to supply personal information

**about your race or national origin, your sex, marital status and age.** Why? The federal government compiles this information about loan applicants, plus details of whether loans were approved or denied. The results, which are publicly available under the Home Mortgage Disclosure Act, help regulators and the public form a judgment about whether the lender is complying with anti-discrimination laws.

You can't be denied a loan if you refuse to provide this kind of personal information. But if you don't answer these questions, your lender must attempt to do so. And the information you do provide cannot be used by the lender in making a decision about whether to approve or deny your loan.

**2. The lender must give you a booklet explaining the mortgage loan process and its costs.** The U.S. Department of Housing and Urban Development (HUD) publishes a

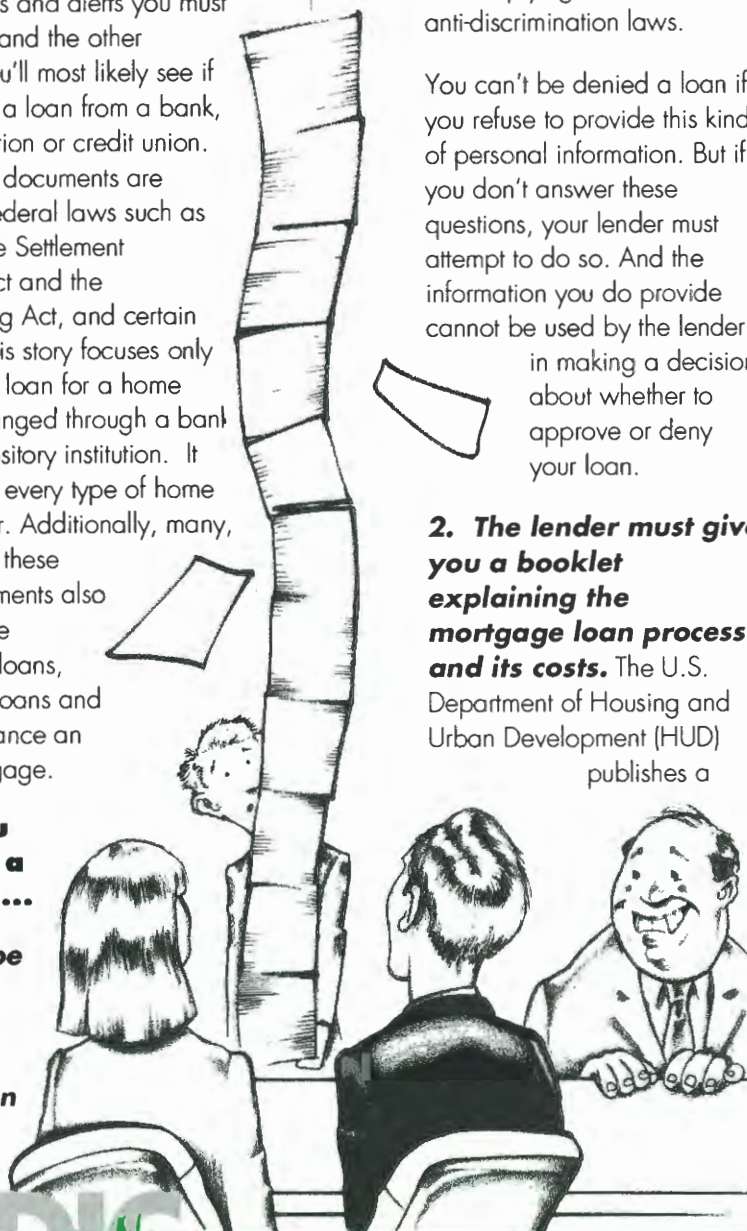


Illustration by T. W. Ballard

special booklet to help prepare you for the coming days and weeks of difficult and costly decisions. It includes: tips and questions to ask when you shop for a lender, a lawyer and other services; an explanation of services you may be asked to pay for, such as title insurance; your protections against discriminatory lending and other unfair practices; your obligations as a borrower to make timely payments and maintain insurance; and sample forms and worksheets that will help you review and compare the charges you're being quoted.

Your lender must give or mail this booklet to you within three business days of filing a written application for the loan, assuming your loan hasn't been denied by then.

**3. You'll get an early estimate of your settlement costs.** Within specified periods, your lender must give you a "good faith estimate" of how much you can expect to pay for various settlement fees and services. Examples include any one-time loan origination fees or "points" you'd pay the lender, loan processing fees and insurance.

At this stage, the dollar amounts are only estimates, not guarantees. *They're intended to help you comparison-shop or try to negotiate a better deal.* And if your lender insists that you use a particular company or person for one of these services, this relationship, along with the estimated cost and other details, must be disclosed to you.

**4. You'll get an early estimate of your future interest payments.** Under the Truth-in-Lending Act, your lender also

must set out the interest rate you've agreed to pay and how that would translate into mortgage payments each month and over the full life of the loan. If you're applying for an "adjustable rate mortgage" where the interest rate could change during the life of the loan, details of how rate increases could affect your payments also must be included.

Also important: a disclosure of the loan's "annual percentage rate" or APR. All lenders must use the same method of calculating the APR, so you can reasonably compare one lender's rates with another's. For example, an advertised rate of 8.5 percent may be closer to 8.7 percent once you figure in all the costs. If there's a significant error in what's disclosed to you when your loan is final, you may be eligible for reimbursements from your lender. Federal examiners check for this when they examine banking institutions, and you'd be notified if an error is found.

You also must be informed of how likely your lender is to sell your loan to another bank, along with your rights and responsibilities if the loan eventually is sold. This gives borrowers who are reluctant to deal with some unknown company in the future the chance to understand their rights and perhaps decide to apply elsewhere for a loan.

### **If Your Loan is Denied...**

**5. You must be told in writing why your loan was rejected.** By law, you have 30 days after completing your application to find out if you've been approved or denied. If your loan is rejected, the lender must explain why

in writing and give you the name and address of the appropriate federal agency to contact if you think you've been discriminated against. Remember, you can't be denied credit solely because of your race, sex, age, religion, national origin, marital status, handicaps or certain other factors. If you suspect a problem, it's best to try to resolve the matter with the lender first.

If a bad credit report is the reason you've been denied a loan, you must be told of that fact. By law, you're entitled to a free copy of that report if you request it from the credit bureau within 30 days. This gives you the opportunity to dispute the report and perhaps have your loan reconsidered.

### **If Your Loan is Approved...**

**6. You'll get a rundown of all services and fees to be paid at your loan settlement.** HUD developed the "uniform settlement statement" (sometimes called the HUD-1 form) for your attorney or other settlement agent to list how much you owe the lender, your lawyer, insurance companies and so on. By law, you have the right to see this document one business day before the settlement meeting. Your settlement agent may not have all the fees finalized by then, but you have the right to review the known charges so you have yet another chance to question a fee. The HUD-1 form also will include such information as to how much you will be asked to pay each month into an "escrow account" from which the lender will periodically withdraw funds to pay your property taxes and insurance.

(Continued on next page)

Of course, you'll be asked to approve the completed HUD-1 form at settlement. But it's usually better to question something *before* you sit across the table from the lawyers and the sellers who are just as anxious as you to wrap things up. Keep your final HUD-1 form (and a copy or two) in a safe place for at least as long as you own your home. Chances are you'll need the information for tax purposes if you sell the home or refinance your loan.

**7. You'll be told if you need flood insurance.** Many consumers don't realize that flood damage isn't protected against loss by their homeowners' insurance policies. That's why Congress in 1968 created the National Flood

Insurance Program and, in 1973, began requiring that certain loans for properties in flood-prone areas carry the insurance. Your lender must notify you at least 10 days prior to your settlement meeting if you need federal flood insurance.

Only about 2.7 million of the approximately 11 million properties in flood hazard areas now carry flood insurance. In the past, many home owners purchased coverage because it was required to get their loan approved but then didn't renew the policies. Congress closed this loophole in 1994 by amending the law to require, among other things, that *if you need to get the insurance but you refuse, your lender must purchase it for you.* The lender can

then add the cost of the insurance to your loan payments. If you have questions about flood insurance, contact your lender or the National Flood Insurance Program at 1-800-638-6620.

### **Final Thoughts**

Take the time to review the disclosures and don't hesitate to seek guidance from your lender, attorney, real estate broker or other professionals. Chances are that by the time you sign all the documents and write all the checks, you'll realize it was all worth it for the peace of mind that is now yours as you cross the threshold of your very own home.

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## **A Glossary of Mortgage Terms**

**Adjustable Rate Mortgage** - A mortgage whose rate, often based on a market rate or index, can be changed periodically within limits agreed to by the borrower and the lender.

**Amortization Schedule** - A list of payments over the life of a mortgage showing the breakdown of principal and interest.

**Appraisal** - A professional estimate of the fair market value of real estate, needed by the lender to determine how much can be loaned on the property.

**Escrow** - A sum commonly paid as part of a monthly mortgage payment and accumulated by the lender (or third party) to make payments when due on real estate taxes and hazard insurance.

**Lien** - An official claim (filed in public land records) against the

owner of a property for failure to pay legal obligations such as real estate taxes or condominium fees. A lien prevents any legal transfer of the property to another owner unless payments are made.

**Origination Fee** - A fee charged by the lender for providing information about a mortgage, sometimes waived if the inquiry results in a mortgage loan.

**PITI** - A term referring to the four general components of a mortgage payment: Principal, Interest, Taxes and Insurance. Remember when mortgage-shopping that most lenders' quotes are for principal and interest only. Real estate taxes and property insurance must be considered when calculating the total payment.

**Points** - A charge imposed by the lender for providing the loan; a point equals one percent of the loan. On a \$100,000 loan, for example,

one point would be \$1,000, and 2 1/2 points would be \$2,500.

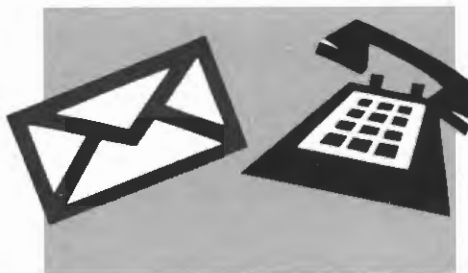
**Title** - Legal proof of ownership of real or personal property, such as a deed or title certificate. The name of the mortgage-holder or lender is shown on the document. When a mortgage is paid off, make sure you receive official notification and that the land records reflect the payoff.

**Title Search** - A review of public real estate records usually to ensure that no liens exist against the property for which a mortgage loan is being provided.

[Note: A more complete glossary as well as detailed information about fair lending can be found in the FDIC's publication "Side by Side - A Guide to Fair Lending." For a free copy write to: FDIC, Room 7118, 550 17th Street N.W., Washington, DC 20429.]

## For More Help

The FDIC offers protection to consumers by insuring deposits up to \$100,000. The FDIC, as well as other regulatory agencies, enforces rules that promote sound banking practices, and compliance with consumer protection and civil rights laws. These protections include: prohibitions against discriminatory lending practices; initiatives to prevent unfair or deceptive practices in deposit-taking or lending; and rules that encourage institutions to meet local credit needs.



**For questions about deposit insurance coverage:** Contact the FDIC's Division of Compliance and Consumer Affairs in Washington or the regional offices listed below.

**For questions about consumer or civil rights laws, or complaints involving a specific institution:**

First attempt to resolve the matter with the institution. If you still need assistance, write to the institution's primary regulator listed on this page. Although the FDIC insures nearly all banks and savings associations in the United States, the FDIC may not be the primary regulator of a particular institution.

### Office of the Comptroller of the Currency

Charters and supervises national banks. (Often the word "National" appears in the name of a national bank, or the initials "N.A." follow its name.)

Compliance Management Division,  
250 E St., SW, Washington, DC 20219  
Phone 202-874-4820

### Federal Reserve System

Supervises state-chartered banks that are members of the Federal Reserve System.

Division of Consumer and Community Affairs,  
20th Street and Constitution Avenue, NW,  
Washington, DC 20551  
Phone 202-452-3693

### Office of Thrift Supervision

Supervises federally and state-chartered savings associations as well as federally chartered savings banks. (The names of these institutions generally identify them as savings and loan associations, savings associations or savings banks. Federally chartered savings associations have the word "Federal" or the initials "FSB" or "FA" in their names.)

OTS Consumer Affairs Office,  
1700 G Street, NW,  
Washington, DC 20552  
Phone 800-842-6929 or  
202-906-6237

### Federal Deposit Insurance Corporation

Supervises state-chartered banks that are not members of the Federal Reserve System. Operates the Bank Insurance Fund and the Savings Association Insurance Fund.

Division of Compliance and Consumer Affairs  
550 17th Street, NW,  
Washington, DC 20429  
Phone 800-934-3342 or  
202-898-3773

**Atlanta Region** (Alabama, Florida, Georgia, North Carolina, South Carolina, Virginia, West Virginia):  
One Atlantic Center, Suite 1600,  
1201 West Peachtree Street, NE,  
Atlanta, GA 30309  
404-817-1300

**Boston Region** (Connecticut, Maine, Massachusetts, New Hampshire, Rhode Island, Vermont):  
200 Lowder Brook Drive,  
Westwood, MA 02090  
617-320-1600

**Chicago Region** (Illinois, Indiana, Michigan, Ohio, Wisconsin):  
500 West Monroe St., Suite 3600,  
Chicago, IL 60661  
312-382-7500

**Dallas Region** (Colorado, New Mexico, Oklahoma, Texas):  
1910 Pacific Avenue, Suite 1900,  
Dallas, TX 75201  
214-220-3342

**Kansas City Region** (Iowa, Kansas, Minnesota, Missouri, Nebraska, North Dakota, South Dakota):  
2345 Grand Avenue, Suite 1500,  
Kansas City, MO 64108  
816-234-8000

**Memphis Region** (Arkansas, Kentucky, Louisiana, Mississippi, Tennessee):  
5100 Poplar Avenue, Suite 1900,  
Memphis, TN 38137  
901-685-1603

**New York Region** (Delaware, District of Columbia, Maryland, New Jersey, New York, Pennsylvania, Puerto Rico, Virgin Islands):  
452 Fifth Avenue, 19th Floor,  
New York, NY 10018  
212-704-1200

**San Francisco Region** (Alaska, Arizona, California, Guam, Hawaii, Idaho, Montana, Nevada, Oregon, Utah, Washington, Wyoming):  
25 Ecker Street, Suite 2300,  
San Francisco, CA 94105  
415-546-0160

Some banking matters may involve state laws. For assistance on these matters, please contact the appropriate state financial institution regulatory agency or state Attorney General's office. These state offices usually are listed in your telephone book and other directories.

For information about credit unions, contact the National Credit Union Administration, Office of Public and Congressional Affairs, 1775 Duke Street, Alexandria, VA 22314-3428. Phone 703-518-6330.

## **"Your Insured Deposit" is Available in English, Spanish**

Here's a reminder that the FDIC's booklet, "Your Insured Deposit," is available free of charge from banks and savings associations as well as from the FDIC. The booklet, also published in Spanish, gives a broad description of the FDIC's insurance rules in a question and answer format. If you already

have a copy of this booklet, make sure it's the latest edition, marked 1993 on the last page. Previous editions should be destroyed. To obtain one or more copies of this booklet from the FDIC, write to our Division of Compliance and Consumer Affairs, 550 17th Street, NW, Washington, DC 20429.

### **Please Write!**

Is there an issue you'd like addressed or a question you'd like answered in *FDIC Consumer News*? Please send your thoughts and suggestions to:

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Washington, DC 20429-9990  
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