
CDARS—An Investment Safeguard Strategy

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The current uncertain economic environment and recent series of bank and investment firm failures have caused depositors to pay closer attention to where their funds are held. Real estate firms, in particular, are focusing on the safety of funds deposited in escrow, lockbox and other accounts, which frequently hold amounts far in excess of the present \$250,000 FDIC insurance cap (which will return to the prior limit of \$100,000 on December 31, 2009). CDARS accounts provide a simple, efficient way to obtain up to \$50 million in FDIC protection on deposits.

CDARS—the Certificate of Deposit Account Registry Service—is a bank deposit placement service offered by Promontory Interfinancial Network that allows participating banks to place customer funds in uncertificated certificates of deposit in multiple other participating banks. The amount of the certificate of deposit issued by each bank, including both principal and interest earned, does not exceed the FDIC limit.

To start the process, the customer contacts a “relationship institution” (the bank into which the initial funds are deposited), and the parties enter into a CDARS Deposit Placement Agreement (“DPA”) pursuant to which the relationship institution, as agent, places the customer’s funds, through CDARS, with other “participating institutions.” The relationship institution also enters into a custody agreement with The Bank of New York Mellon, pursuant to which The Bank of New York Mellon, as the sub-custodian of the deposited funds, maintains a custody account in which the funds are held prior to investment in the certificates of deposit and again following redemption.

Each deposit-taking institution holds the funds in the name of “The Bank of New York Mellon, acting for itself and others, each acting for themselves and others.” This account description allows the FDIC deposit insurance to “pass-through” to the beneficial owner of the certificate of deposit. The Bank of New York Mellon’s records reflect that each certificate of deposit is held by the relationship institution “acting for itself and others,” and the relationship institution’s records reflect the customer’s holdings. No physical certificates evidencing the certificates of deposit are issued, which may be a concern for depositors who must take physical possession of a certificate. Also, care must be taken by a lender seeking to perfect a security interest in the customer’s interest in such certificates of deposit. The customer, though not the direct holder

of the certificates of deposit, is the beneficial owner, entitled to be paid the deposit and, if necessary, to claim FDIC insurance.

While the deposit and record-keeping structure within CDARS has some complexity, CDARS allows the customer to receive from its relationship institution a single monthly statement for all CDs acquired through CDARS. Thus, the customer holds FDIC insured deposits, but avoids the inconvenience of having to open accounts at multiple banks and to manage the separate CD terms, interest calculations, monthly statements, 1099 statements and banking relationships. CDARS consolidates these functions, while giving the customer the flexibility to determine the term of deposit and rate of interest acceptable for each CDARS placement under the DPA (although interest rates earned on CDARS placements may be lower than on more aggressive, "jumbo" certificates of deposit). The customer is also able to designate particular participating institutions for exclusion from the list of banks eligible to hold its funds. This right is typically exercised to ensure that a bank where the customer already has funds on deposit does not receive additional funds that would exceed, in the aggregate with existing deposits, the FDIC limit. No fees are charged to the customer for the placement of funds through CDARS.

The advantages of CDARS placements are several. They provide the customer with increased safety for deposits that would otherwise exceed the FDIC limit by breaking them into smaller amounts placed in multiple participating banks. CDARS also allows the customer to maintain a single banking relationship and significant control over the disposition of its funds. The CDARS program is offered in all 50 states and the District of Columbia, typically through regional and local banks.

Note: CDARS is a registered service mark of Promontory Interfinancial Network, LLC. The Bank of New York Mellon is a client of Pillsbury, and one of the Bank's affiliates is an investor in Promontory Interfinancial Network, LLC.

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