Banking on Communities:

Frequently Asked Questions About the Use of CDARS

The Initiative

How can CDARS® further the goals of the Banking on Communities initiative?
The Banking on Communities initiative is an effort by the Community Development Bankers Association (CDBA) to help its member banks raise funds that can be used to lend to quality projects in underserved communities and to provide hands-on support for those projects.

The CDBA is a national trade association of the community development banking industry and was established to help its members better meet the credit needs of their communities. Because of their size (small), age (young), and location (underserved communities), CDBA members often find their funding options limited and have fewer resources to devote to attracting deposits.

The Certificate of Deposit Account Registry Service®, also known as CDARS® enables CDBA banks to attract large deposits by offering access to $50 million or more in FDIC insurance to each depositor. CDBA banks may then lend these funds into their communities.

CDBA

What is the difference between CDBA and CDFI institutions?
Community Development Financial Institutions (CDFI) are financial institutions specially designated by the Department of Treasury to recognize that they primarily serve economically distressed communities or populations. Greater than 600 CDFI institutions exist in the U.S., but just over 60 of them are banks.

All CDBA banks are CDFIs.

Certificate of Deposit Account Registry Service®, CDARS®
Nearly 3,000 banks

Community Development Financial Institutions (CDFIs)
650 organizations, about 60 of them are banks

Community Development Bankers Association (CDBA)
About 25 banks

CDBA

CDARS

CDARS

What is CDARS?

CDARS, designed by Promontory Interfinancial Network, LLC, Arlington, Virginia (the "Network"), enables depositors to invest funds in multiple certificates of deposit ("CDs") through one bank, with eligibility for full FDIC insurance coverage. The service assists FDIC-insured institutions in placing their depositors' funds with other FDIC-insured depository institutions that also are members of the Network ("Participating Institutions"). Using CDARS, a Participating Institution places the funds of its depositors in CDs issued by other Participating Institutions in principal amounts (taking into account any interest to accrue over the term of a CD) that do not exceed the standard FDIC insurance maximum. Thus, Participating Institutions can offer depositors with funds that exceed the FDIC limit the ability to easily place those funds at other Participating Institutions in CDs that will be eligible for full FDIC insurance. In addition, for any funds that a Participating Institution submits for placement through CDARS, the Network will place an equal amount of funds as deposits with the Participating Institution. These transactions are referred to as "CDARS Reciprocal Transactions."[1]

If my deposit is spread among different institutions, how does my deposit benefit the local community?

CDFI and CDBA banks that offer CDARS are part of a special network. When you place your money with a CDFI bank in your community, the bank places your funds into certificates of deposit issued by other network banks. The CDFI bank then receives deposits dollar for dollar from other members of the CDARS network. As a result, the CDFI bank receives the same amount from the other network banks that it distributed. So the bank can make use of the full amount of your funds right in the local community. It is as if the money never leaves the CDFI bank.

What types of other banks issue CDs to me?

With CDARS, your funds are split among other banks that issue CDs to you. These banks are members of the network of banks that offers CDARS and are all FDIC-insured. They are not all CDFI banks. Nevertheless, all of your money still goes to work in the local community. Because banks swap deposits dollar for dollar, the full amount of your deposit is available for local lending.

1] For depositors seeking CRA credit, please inform the recipient CDFI bank that you wish to conduct a "CDARS Reciprocal[SM] transaction" and not a "CDARS One-Way transaction" to help ensure that your deposit will meet CRA requirements.

Mechanics of a CDARS Deposit

Can you walk me through the detailed transaction flow of a sample $1 million CDARS deposit into a CDBA bank?

Step 1: A depositor seeking FDIC insurance on a deposit in excess of the standard FDIC insurance maximum can request that a CDFI that participates in CDARS place the depositor's funds—say $1,000,000—using the CDARS service at an interest rate agreed to between the CDFI and the depositor. The amount of the placement, interest payment terms and CD term are agreed to by the CDFI and the depositor. The CDFI will submit an order through the CDARS secure website requesting allocation of the funds for deposit in other Participating Institutions (in this case, at least eleven Participating Institutions, so that the full amount of principal and interest will be eligible for FDIC insurance), each of which will receive a deposit in an amount under the standard FDIC insurance maximum. When the depositor requests that the CDFI place the depositor's funds using CDARS, the CDFI will make available to the depositor a list of the Participating Institutions at which the depositor's funds are proposed to be placed. The depositor then has an opportunity to review the list and to notify the CDFI of any Participating Institutions where it does not wish its funds to be placed.

Step 2: On the settlement date (the day after the CDFI makes the list of proposed placements available to the depositor), in accordance with instructions transmitted by the Network, The Bank of New York ("BNY") issues CDs to the depositor on behalf of the (issuing) Participating Institutions. In particular, BNY issues the CDs as agent for the Participating Institutions in the name of BNY as sub-custodian. The CDFI, in turn, acts as the depositor's custodian with respect to these CDs. FDIC regulations provide that FDIC insurance coverage will "pass through" to the original depositor as the beneficial owner of the CDs. An FDIC interpretive letter, dated July 29, 2003, confirmed that deposits placed using the CDARS service would be eligible for insurance on a "pass-through" basis under the FDIC's rules on insurance coverage of agency or custodial accounts. Thus, the full amount of the depositor's original deposit of $1,000,000 will be eligible for FDIC insurance coverage.

Step 3: At the same time that the CDARS service allocates the depositor's funds among Participating Institutions, the CDFI is allocated the same amount of funds through the Network from other Participating Institutions in the Network. Thus, the same amount of funds invested by the depositor through the CDFI in effect returns to the CDFI in the form of reciprocal deposits from other Participating Institutions.

Step 4: No physical certificates are issued to the depositor placing funds through the CDFI, but the depositor receives through the CDFI confirmation of the issuance of the CDs and periodic account statements that reflect the depositor's beneficial ownership of the CDs.

Legal Background

Are the regulators aware of CDARS?

Yes, CDARS and its application to community reinvestment through CDBA members was referenced in an OCC regional newsletter in January of 2005.

Furthermore, the regulators have verbally advised CDBA that a deposit by a banking institution through a CDFI using CDARS can be considered a “qualified investment” for purposes of the “investment test” used to determine CRA performance.

In which part of the CRA test would a deposit through CDARS into a CDFI apply?

The deposit of funds by a banking institution through a CDFI using the CDARS service is consistent with the definition of “qualified investment” under the CRA regulations. A “qualified investment” is broadly defined as “a lawful investment, deposit, membership share, or grant that has as its primary purpose community development.”[1] “Community development,” in turn, is defined to include, among other things, “activities that revitalize or stabilize low- or moderate-income geographies.”[2] Interpreting these definitions, the agencies have determined that investments or deposits in a CDFI are “qualified investments.”[3]

Under the CRA regulations, federal banking regulators assess the CRA performance of a bank using several tests and standards, one of which is the investment test. Applying the investment test, regulators evaluate “a bank’s record of helping to meet the credit needs of its assessment area(s) through qualified investments that benefit its assessment area(s) or a broader statewide or regional area that includes the bank’s assessment area(s).”[4] As referenced above, the regulators orally have advised CDBA that a deposit by a banking institution through a CDFI using CDARS can be considered a “qualified investment” for purposes of the “investment test” used to determine CRA performance.

How can I determine if a CDFI bank falls within my multi-state region?

CDFIs are located throughout the country. Check with your bank examiner to find out if the bank is included in your multi-state region.

[1] 12 CFR __.12(s).
[2] 12 CFR __.12(h)(4).
[3] See 66 Fed. Reg. 36629 (July 12, 2001) (“Examples of qualified investments include, but are not limited to, investments, grants, deposits or shares in or to . . . [CDFIs]”); FFIEC letter dated June 26, 1995 (“Qualified investments include, but are not limited to, investments in CDFIs that primarily lend in low- and moderate-income areas or to low- and moderate-income individuals to promote community development . . ..”).
[4] 12 CFR __.23(a).