QwickViews for investors

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# CD Investments—What to expect if the bank fails.

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The federal regulatory agencies anticipate a rise in the number of problem institutions over the next few quarters. If your institution has a CD investment in a failed bank, do you know what happens next?

As we speak with QwickRate members on a day-to-day basis, we find that many of our subscribers do not have a clear picture of how the FDIC resolves the situation, and how an investor's deposits may be impacted. Understanding the basics of the bank resolution process that normally occurs when a bank fails will help to alleviate some of the uncertainty and anxiety often experienced in this situation. This article discusses those issues and indicates when you may access your funds.

There are two types of resolution options most commonly used by the FDIC when a bank fails: 1) Purchase or Assumption Option: facilitating the transfer of the institution's insured deposits to an assuming institution; or 2) Depositor Payout Option: paying insured depositors directly. The FDIC determines an accurate valuation of the failing institution by assessing its assets and liabilities in an effort to determine an orderly and least-cost resolution.

The amount of time that it takes investors to get their deposits back, and the amount of interest they could lose, will depend on the type of resolution process chosen by the FDIC. Plus, another factor also impacts investors: whether you placed the CD investment directly or through a third party such as a deposit broker or corporate placement program. Transactions executed through a third-party may potentially alter or delay the return of your deposit.

## Access to Your Funds when Deposits are Purchased or Assumed

The preferred way to resolve a failed institution, and the most common one, involves finding a healthy bank to quickly buy the rights to assume the insured deposits and other business of the failed bank. Depositors automatically become customers of the assuming bank, and offices of the failed bank reopen under the name of the acquiring institution—usually by the next business day. If the FDIC cannot find another institution to buy the failed bank's insured deposits, they may choose to transfer the insured deposits to a newly created bank that would be operated by the FDIC (as in the case of IndyMac). This new bank, referred to as a "bridge bank" or "conservatorship", enables depositors to access their insured funds by the next business day and to maintain other banking services until the FDIC can find a buyer for the new bank.

In the case of a purchase and assumption, the acquiring institution will either assume all of the bank's deposits or will have the opportunity to only assume a select component of the failed bank's depositor base. Those deposits which

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are assumed by the acquiring institution will automatically be transferred to the assuming bank and depositors will have access to their insured and uninsured funds by the next business day.

However, at this point, the depositor does not have an actual agreement or deposit contract with the acquiring institution. Therefore you should be mindful of the following points:

- The acquiring depository institution can, with written notice, lower the interest rate that it will pay on the deposits it has acquired. Acquired depositors must choose whether to accept the new rate, in effect entering into a deposit agreement with the acquiring institution, or to withdraw their funds.
- If the depositor chooses to withdraw their funds, they may do so without incurring an early withdrawal penalty.
- If the depositor chooses to accept the new interest rate and deposit agreement offered by the acquiring institution, it will continue on as a customer of the assuming bank.
- If the depositor already has a CD with the assuming institution, both CDs will continue to be insured until the maturity date of the first CD.

More often than not, the primary goal of the acquiring institution is to gain market share in a particular area; consequently, the institution will only be interested in obtaining assets and liabilities that are considered to have franchise value and that provide an opportunity for growth in the failed bank's key markets. In this situation, the acquiring bank may decide to purchase only the "insured" deposits, and may further limit the insured deposits to those which were placed directly with the failed institution. Often an acquiring institution infers that a deposit facilitated by a third party offers no opportunity for a lasting relationship with the depositor. Large denomination deposits, those exceeding the insurance limit, may also be excluded by the acquiring institution and left for resolution by the FDIC. As a result, if your deposit was placed through a broker or is in excess of the deposit insurance limits, there is a probability that, in the case of a purchase and assumption, it will not be assumed by the acquiring institution and will be subject to the FDIC depositor payout and resolution process.

## Access to Direct Deposits In A Depositor Payout Resolution

When a failed bank is resolved through a straight depositor payout—meaning no agreement has been reached with an acquiring institution to assume all or part of the failed bank's deposits—the FDIC will issue checks directly to depositors in amounts up to the federal insurance limit. Deposits in excess of the deposit insurance limit will be subject to the resolution process of the FDIC. In the case of deposits which are clearly identifiable on the deposit record of the failed financial institution and are valued below the deposit insurance limits, the stated goal of the FDIC is to pay out deposits one business day from the date of closing. Closings generally occur on Friday with payout on the following Monday. Interest is accrued through the date of closing. As a result, those depositors who have placed their CDs direct and whose identities are

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clearly determinable on the deposit records of the bank, will generally face two to three days of lost interest in the event of a bank failure and deposit payout.

## Access to Brokered Deposits in a Depositor Payout

No matter how the FDIC resolves a failed bank, some types of deposits present special challenges. For some deposits, the FDIC may require more time to obtain the documentation needed to finalize the insurance payments. Examples include accounts linked to a formal written trust agreement, deposits placed by an administrator of an employee benefit plan, and bank certificates of deposit (CDs) sold by deposit brokers. In the latter, the bank's records often note only the name of the broker, not the individuals or institutions who made deposits, and the FDIC may need additional time to gather supplemental documentation from the broker and make an accurate insurance determination. It is the responsibility of the broker or third party placement agent to present this supplemental information to the FDIC, in the proper format as specified in the FDIC's Deposit Broker Processing Guide. The FDIC processes information submitted by brokers/as agents on a first-in, first-out basis. The sooner the broker provides the proper information to the FDIC, the sooner the depositor can be identified and paid. Interest is accrued on the deposit through the date of closing of the failed institution. Depositors who have placed their CDs through a deposit broker may incur additional lost interest based on the time frame associated with the broker's providing the supplemental information to the FDIC.

## Direct Depositor Identification

When a bank fails, the first step in the FDIC resolution process is to identify the bank's depositors and deposit accounts. The ability to clearly identify depositors leads to quicker access to your deposit dollars. Customers who have placed their deposits direct, and whose deposits are readily identifiable, will incur fewer delays and a minimal amount of lost interest. As a direct deposit listing service, QwickRate advances the direct investment process by providing investors the ability and opportunity to communicate directly with a nationwide pool of financial institutions, thereby promoting optimum returns for our subscribers.

In summary, if you have a CD investment in an institution that fails, don't panic. Your CD investments are protected by the FDIC in the unlikely event of the financial failure of a bank or savings institution. FDIC deposit insurance covers the balance of each depositor's account, dollar-for-dollar, up to the insurance limit, including principal and any accrued interest through the date of the insured bank's closing. When a bank fails, the FDIC notifies a depositor immediately in writing using the depositor's address on record with the bank. The FDIC also makes every effort to inform the public through the news media and internet notifications. Information regarding the type of transaction utilized to resolve the failed institution is made available within those notifications. For more information on the processes associated with the failure of a financial institution you may refer to the FDIC publication "When a Bank Fails - Facts for Depositors, Creditors, and Borrowers" located on the FDIC website at http://www.fdic.gov/consumers/banking/facts/index.html.

*We hope that you find this information to be valuable and encourage you to take full advantage of the additional services QwickRate offers to support your investing initiatives.*