FEDERAL RESERVE BANK OF DALLAS

DALLAS, TEXAS 75222

Circular No. 68-137
June 13, 1968

To All Member Banks
in the Eleventh Federal Reserve District:

There is enclosed a statement issued by the Board of Governors of the Federal Reserve System on June 5, 1968, for the purpose of clarifying certain provisions of Regulation Q.

Additional copies are available upon request.

Yours very truly,

P. E. Coldwell
President

Enclosure (1)

FEDERAL RESERVE

press release

For immediate release. June 5, 1968.

The Board of Governors of the Federal Reserve System, in an interpretation of its Regulation Q, said today that a member bank may pay interest on a multiple maturity time deposit at the maximum allowable rate--presently 5 per cent--only if the deposit is payable at intervals of at least 90 days.

The interpretation was issued for clarification purposes following receipt of inquiries on the conditions under which banks may pay the maximum 5 per cent rate on time deposits having more than one maturity date.

The text of the interpretation is attached.

5% Multiple Maturity Time Deposits

From time to time the Board of Governors receives inquiries relating to the payment of interest of 5 per cent per annum on "multiple maturity time deposits" as defined in § 217.1(g) of Regulation Q. In view of the variety of deposit contracts that have come into use in recent years, the Board considers it advisable to clarify, for banks and their depositors, certain limitations on the authority of a member bank to pay 5 per cent interest on funds deposited with it. The underlying principle is that a member bank may pay interest on a multiple maturity time deposit at the rate of 5 per cent only if the deposit is payable at intervals of at least 90 days.

90-day certificate of deposit. One major category of multiple maturity time deposits is certificates of deposit that (1) mature on a series of specified dates or (2) are automatically renewed at maturity without any action by the depositor. Certificates that mature at specified dates that are 90 days apart and certificates that mature 90 days after the date of issuance and are automatically renewable for successive 90-day periods until the depositor withdraws his funds constitute multiple maturity time deposits in certificate form with the shortest intervals between payment dates that are permissible if interest thereon is to be paid at a rate of 5 per cent.

90-day notice account. Another major category of multiple maturity time deposits is deposits that are payable only after written notice of withdrawal. Such deposits may be in the form of a passbook or otherwise. Funds may be added to the account either at specified times or whenever the depositor wishes, depending on the terms of the contract.

A member bank may pay interest at the rate of 5 per cent on funds in such an account, on two conditions. The first is that funds must not be withdrawable within 90 days of the date they are deposited. The second is that funds must not be withdrawable less than 90 days after the date of written notice of intention to withdraw. In other words, a member bank may pay 5 per cent only on deposits that are payable solely at intervals of at least 90 days.

If a depositor gives 90-days' notice of intention to withdraw and then decides that he will not need the funds at the specified date, he may cancel his notice, either explicitly, or impliedly by a new 90-day notice. He may not, however, retain his right to withdraw at the expiration of the first notice while giving a simultaneous or subsequent notice, unless the latter expires at a date at least 90 days after the expiration of the first.

90-day notice account coupled with provision for automatic renewal. Recently, a few banks have offered a 5 per cent multiple maturity time deposit contract that authorizes withdrawal by the depositor on more than one basis. For example, the contract may provide that funds received on or before January 1 may be withdrawn March 31 and, with respect to funds not withdrawn on that date, the deposit will be automatically renewed until June 30, and so forth. The contract also provides that funds may be withdrawn on 90 days' notice in writing. In such event, to be consistent with the principle that the depositor may not have access to a 5 per cent multiple maturity deposit at intervals of less than 90 days, such a contract should inform the depositor that, when notice is given with respect to all or a portion of the funds on deposit, such notice automatically cancels any other provision for withdrawal that is inconsistent with said principle.

Consequently, if the depositor gives notice on March 1 of his intention to withdraw $1000 from his account on June 1, the contract should make clear that this automatically cancels his right to withdraw such amount on March 31, since such amount would otherwise be payable at intervals of less than 90 days. Also, his right under the specified maturity (or automatic-renewal maturity) provision to withdraw such amount on June 30 should be suspended, for the same reason. The latter right might be reinstated by the depositor revoking before April 1 his notice of intention to withdraw, since that would be at least 90 days before the specified June 30 maturity. However, the right to withdraw on March 31 could not be reinstated. If it could, the depositor would be in a position to acquire access to the amount involved at intervals of less than 90 days.

As in a "straight" 90-day notice account, the depositor may supersede his notice of intention to withdraw by a subsequent 90-day notice. Again, such notice would have the effect of canceling any other right to withdraw that is inconsistent with the 90-day interval principle.

Withdrawal "grace period". There is one exception to the rule that a member bank may not pay 5 per cent interest on multiple maturity deposits that are payable at intervals of less than 90 days. A bank may permit a depositor to withdraw his funds within ten days after a specified maturity, even if there is a provision for automatic renewal for 90 days if not withdrawn at said maturity. If he does so, no interest may be paid for the period from the maturity date to the date of withdrawal, for during that time the deposit is a "demand deposit", on which payment of interest is prohibited by law. If he does not so withdraw, the deposit remains a time deposit, with a term running from the maturity date until a subsequent specified date or for a specified number of days.[1/]

"Emergency" withdrawal. In accordance with section 217.4(d) of Regulation Q, a bank may pay a time deposit before maturity where that is "necessary to prevent great hardship to the depositor", but in that case the depositor forfeits accrued and unpaid (uncredited) interest. Occasions for such withdrawals are exceptional. Unless the depositor is confronted with an actual emergency, a bank may not permit withdrawal of

1/ A single maturity time deposit also may be renewed by action of the depositor within 10 days after maturity. In such event, as in the case of the multiple maturity time deposit, a member bank may pay interest on the deposit between the maturity date and renewal thereof at the applicable maximum rate.

funds before maturity of the deposit or termination of the specified period of notice. If the depositor simply has a need for funds, the bank may extend credit to him on the security of his time deposit, but the rate of interest on such loan must be at least 2 per cent per annum in excess of the rate of interest paid on the time deposit.

Advertising time deposits. Some recent advertisements by member banks might be interpreted as offering withdrawal privileges from a 5 per cent multiple maturity time deposit at intervals of less than 90 days.

In December 1966, the Board was joined by the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the Federal Home Loan Bank Board in a statement of principles directed against misleading advertising practices in the solicitation of deposits. The third principle states that "If an advertised rate is payable only on investments or deposits that meet fixed time or amount requirements, such requirements should be stated." An advertisement by a member bank that permits the reader to infer that the bank will pay interest at the rate of 5 per cent on funds that may be withdrawn at intervals of less than 90 days is inconsistent with that principle and is regarded by the Board as misleading.

The Board heretofore has refrained, in the definition of "time deposit" in Regulation Q, from prescribing permissible designations for such deposits, and has not objected to banks offering time deposit contracts that are called "savings certificates" or "savings bonds".

However, use of such designations without explanation might have a misleading tendency, because of the public's impression that "savings" in a bank will be paid at any time. Consequently, the greater the possibility that the name given to an account may mislead, the more imperative is the bank's obligation to direct the depositor's attention to the withdrawal restrictions that govern the particular account offered.

Board of Governors of the
Federal Reserve System

June 5, 1968.