

FEDERAL RESERVE BANK OF DALLAS

DALLAS, TEXAS 75222

Circular No. 80-170 (A)
September 9, 1980

REVISED REGULATION D

TO THE CHIEF EXECUTIVE OFFICER
OF ALL CREDIT UNIONS IN THE
ELEVENTH FEDERAL RESERVE DISTRICT:

As you may already be aware, with the passage of the Monetary Control Act of 1980 (Public Law 96-221), all depository institutions--including credit unions--offering transaction accounts or nonpersonal time deposits will become subject to the Federal Reserve's Regulation D, Reserve Requirements. I am glad to inform you that, in the interest of reducing regulatory burden, the Federal Reserve Board in its revised Regulation D has deferred until May 1981 all reserve deposit and reporting requirements for institutions with total deposits of less than \$1 million.

This decision was based, among other things, on the large number of small institutions being brought under Federal reserve requirements for the first time by the Monetary Control Act. We estimate that more than 11,000 institutions (mostly credit unions) will be affected by the Board's deferral decision. Since these institutions collectively control less than 1 percent of all the deposits in the United States, the immediate imposition of Federal reserve requirements on them does not seem necessary for monetary control.

In addition to the deferral for very small institutions, the Board has adopted a procedure of quarterly rather than weekly reporting and reserve maintenance for institutions with total deposits of \$1 million or more but less than \$5 million. This procedure will begin in January 1981. Detailed information on reporting and reserve maintenance will be provided to these institutions later this year.

Institutions with total deposits of \$5 million or more will report and maintain reserves on a weekly basis. Reporting will begin for deposits as of October 30, 1980, and reserve maintenance on November 13, 1980. Detailed information on both reporting and reserve maintenance will be provided to these institutions within the next several weeks.

For purposes of the deferral or for quarterly rather than weekly reporting, the size of your institution is to be determined on the basis of total deposits as of December 31, 1979. For institutions that have commenced operations since December 31, 1979, the latest available data should be used. To determine the amount of your credit union's total deposits, all regular share accounts, share draft accounts, share certificates and certificates of indebtedness shall be aggregated, regardless of maturity and whether personal or nonpersonal.

Banks and others are encouraged to use the following incoming WATS numbers in contacting this Bank: 1-800-442-7140 (intrastate) and 1-800-527-9200 (interstate). For calls placed locally, please use 651 plus the extension referred to above.

Enclosed is the press release containing the highlights of the new reserve requirement structure, as well as more information on the deferral for small institutions and the preamble to Regulation D as submitted for publication in the Federal Register. Also enclosed are the press release and Federal Register document detailing the pass-through guidelines and a brochure regarding the Monetary Control Act of 1980. A copy of Regulation D is not enclosed. However, if your institution has \$1 million or over in deposits, or if you otherwise wish to have a copy of the regulation, please return the enclosed card.

For additional information, contact Richard D. Ingram, Assistant Vice President, Ext. 6333.

We look forward to a pleasant association with your institution.

Sincerely yours,

Ernest T. Baughman

President

Enclosures

FEDERAL RESERVE press release



For immediate release

August 15, 1980

The Federal Reserve Board today announced that it has revised its Regulation D -- reserve requirements of depository institutions -- to carry out provisions of the Monetary Control Act of 1980.

The first period for reporting deposits under the new regulation begins October 30, 1980 for all institutions whose requirements have not been deferred. The amount of initial reserves required beginning November 13 under the Act's new reserve ratios will be calculated from these reports.

The Board amended Regulation D to conform to the Act after consideration of comment on proposed new reserve requirement rules published in June.

The Monetary Control Act, which became law March 31, is designed to improve the effectiveness of monetary policy by applying new uniform reserve requirements, set by the Federal Reserve, to member and nonmember commercial banks, savings banks, savings and loan associations and credit unions that offer transaction accounts or nonpersonal time deposits.

By the terms of the Act, the reserve requirement on the first \$25 million of an institution's transactions accounts will be 3 percent. The initial requirement on remaining transactions accounts will be 12 percent. The reserve requirement on nonpersonal time deposits with original maturities of less than four years will be 3 percent. Nonpersonal time deposits with original maturities of four years or more will be zero percent. Eurocurrency liabilities will have reserve requirements of 3 percent. The new requirements are, by law, to be

phased in gradually in order to provide an orderly transition. The new regulation includes phase-in schedules, with requirements varying according to the status of the institution, and other factors.

Reporting requirements, and further details, are set forth in the Board's official notice of these actions, which is available upon request from the Federal Reserve Board and from the Federal Reserve Banks. The Federal Reserve Banks will send the notice to all affected depository institutions.

The major provisions of the new regulation are summarized below, beginning with key definitions.

Definition of transaction account

The Act defines transaction accounts to include demand deposits, NOW^{1/} accounts, ATS^{2/} accounts, share draft accounts and accounts permitting telephone or similar transfers for payments to third parties and some other payments. Regulation D as revised permits up to three telephone or preauthorized transfers a month (to another account of the depositor in the same institution or to a third party) before such accounts are regarded as transaction accounts. Accounts that permit more than three such transfers monthly are subject to reserve requirements even if not actively used. Accounts that permit the customer to make third party payments by means of automatic tellers or remote service units are also included among transaction accounts.

Transfers authorized in connection with loans made by the institution holding the deposit do not make the account subject to reserve requirements.

^{1/} Negotiable Order of Withdrawal.

^{2/} Automatic Transfer Service (for transfers of funds from savings to demand accounts).

All cash items (check or check-like items) in process of collection or due from other depository institutions may be deducted in computing transaction account reserve requirements.

Time deposits

Nonpersonal time deposits are subject to reserve requirements under the Act, but personal time deposits are not subject to reserve requirements.

The Act defines nonpersonal time deposits as a transferable time deposit or account, or a time deposit or account in which any beneficial interest is held by a depositor that is not a natural person. Regulation D defines a natural person as an individual or sole proprietor. A personal time deposit is one that is not transferable and in which the entire beneficial interest is held by a natural person. The regulation includes Individual Retirement Accounts (IRAs) and Keogh Accounts among personal time deposits, as well as time deposits held by trustees when the entire beneficial interest is held for a natural person.

The regulation specifies that time deposits do not become transferable by reason of being pledged for a loan, or due to transfer following death, bankruptcy, judicial attachment or the like.

As a transitional measure, the Board said it would regard all time deposits (over or under \$100,000) issued to individuals prior to October 1, 1980 as personal time deposits, even if they are transferable.

On or after that date, to be a personal time deposit, the instrument must be issued to and held by a natural person and bear a legend (which may be hand stamped or printed on the instrument) indicating that it is not transferable. The Board expects issuing institutions to follow normal practices

and to take steps designed to ensure that deposits are not issued to nonpersonal entities through individuals in order to escape reserve requirements.

As a further transitional measure, the new rules permit institutions to estimate -- using standard sampling methods -- the breakdown between personal and nonpersonal fixed maturity time deposits issued prior to October 30 (the beginning of the first reporting period for deposits). Institutions must, however, identify all existing savings deposits and time deposit open accounts as personal or nonpersonal. All time deposits (open or fixed maturity) and savings accounts issued on or after October 30, 1980 must be classified as personal or nonpersonal.

A new type of time deposit

New Regulation D establishes, effective October 30, 1980 a new type of time deposit with a minimum maturity of 14 days, to help improve the ability of domestic depository institutions to compete with banking offices located abroad and with short-term domestic issues. The minimum maturity for time deposits has been 30 days.

Small institutions

The Board deferred reserve and reporting requirements for nonmember depository institutions other than branches and agencies of foreign banks and Edge corporations of less than \$1 million in total deposits until May 1981, in order to relieve potential operating problems. This applies to over 11,400 institutions, mostly credit unions. The Board will determine at a later date whether to extend this deferral.

To ease the reporting burden of small institutions and Reserve Bank administration, the Board adopted a procedure for quarterly reporting of deposits and reserve maintenance for institutions between \$1 million and \$5 million in total deposits. This procedure will begin January 1, 1981. It does not apply to branches and agencies of foreign banks or to Edge corporations.

Reserve requirements on domestic borrowings

Subordinated notes with maturities of seven years or more, federal funds, repurchase agreements against U.S. Treasury and Federal agency securities and certain other domestic borrowings are not regarded as deposits subject to reserve requirements.

Revised Regulation D specifies that the 3 percent reserve requirement applies only to nonpersonal time deposits that have original maturities of less than four years. Nonpersonal time deposits with maturities of four years or more are subject to reserve requirements, but they will have an initial zero reserve ratio.

Eurocurrency reserves

Gross borrowings by institutions in the United States from unaffiliated foreign depository institutions and net borrowing from an institution's own foreign offices are subject to a 3 percent reserve ratio. This ratio applies also to the proceeds of sales of domestic or foreign assets to an institution's own foreign offices and to loans to U.S. residents made by foreign offices of U.S. depository institutions. Such reserve requirements will be computed on the seven-day reserve maintenance period in effect for all other deposits.

The Eurocurrency reserve requirements are designed to eliminate any artificial incentives favoring the raising of funds offshore as compared with raising funds in the domestic market. The basic reserve requirement on Eurocurrency deposits is currently zero.

Other deposits subject to reserve requirements

Regulation D requires that the following also be treated as deposits subject to reserve requirements:

- Commercial paper, including that issued by savings and loan associations.
- Credit union certificates of indebtedness.
- Ineligible acceptances (marketable time drafts on a bank's customer).
- Due bills that remain uncollateralized by similar securities within three days. (A due bill is a promise by a depository institution to deliver at a future date a security bought by the institution's customer.)
- Mortgaged-backed bonds with an original maturity of less than four years.

Reserve requirement calculations for branches and agencies of foreign banks, and Edge corporations

Only one \$25 million tranche at the 3 percent reserve ratio on transaction accounts will be permitted for each foreign bank or Edge or Agreement corporation regardless of the number of their U.S. offices. The U.S. branches and agencies of foreign banks and offices of the same Edge or Agreement corporation will report on a statewide basis.

Eligible reserve assets

All vault cash (except silver and gold coins) and balances held directly or on a pass-through basis at Reserve Banks (above clearing balance requirements) can be used to satisfy reserve requirements.

Phasing in reserve requirements

Nonmember depository institutions

These institutions -- other than those affected by the Board's actions with respect to small institutions, and branches and agencies of foreign banks -- will post, on November 13, 1980, one-eighth of the reserve requirements applicable to them. Subsequently, they will post an additional one-eighth of the reserve requirements applicable to them during the first reserve maintenance week following each September 1, until, in the eighth year, they are posting their full required reserves.

Member banks

Member banks will phase down their required reserves over a period of approximately 3 1/2 years from September 1, 1980, with the first reserve reduction beginning in November 1980.

The reserves that member banks will be required to post while phasing down to the lower new structure of required reserves under the Monetary Control Act will be the amount required under the new structure, plus a percentage of the difference between the lower new requirements and the higher requirements in effect on August 31, 1980. The table below shows the percentages of this difference to be used in each phase-down period. The phase down will begin during the reserve maintenance period starting November 13, 1980.

<u>Reserve maintenance periods occurring between</u>	<u>Percentage of the difference to be applied</u>
November 13, 1980-September 2, 1981	75
September 3, 1981-March 3, 1982	62.5
March 4-September 1, 1982	50
September 2, 1982-March 2, 1983	37.5
March 3-August 31, 1983	25
September 1, 1983-February 29, 1984	12.5
March 1, 1984 forward	0

To simplify this process, and to reduce the reporting burden of member banks, a member's required reserves on time deposits used in calculating requirements under the old structure will be the average ratio in effect on the bank's time deposits of all maturities during the 14-day period from July 24 to August 6, 1980.

New banks, new members
and agencies and branches of foreign banks

Such U.S. institutions will have a 24-month transitional period during which to phase-in to the reserve requirements under the Act. This applies also to new Edge corporations. These institutions will begin by posting one-eighth of their required reserves, and will add an eighth each quarter. The 24-month phase-in applies also to a new branch or agency of a foreign bank when the office is the foreign bank's first in the United States.

NOW accounts

By the terms of the Act, there is no phase-in period for reserve requirements on NOW accounts of nonmembers outside states where NOW accounts are currently permitted (New York, New Jersey and New England). Similarly, no phase-in is provided for NOW accounts of member banks outside these current NOW account states.

Coverage of the Act

Regulation D specifies that in addition to member banks, nonmember banks, U.S. branches and agencies of foreign banks and Edge and Agreement corporations, savings and loan associations, savings banks and credit unions, the reserve requirement provisions of the Act apply also to industrial

banks, but not to New York Investment Companies and "banker's banks" (banks doing business only with other banks). The latter two types of institutions, however, may continue to sell federal funds.

Contemporaneous reserve accounting

The Board is disposed toward returning to contemporaneous reserve accounting, possibly by September 1, 1981, if further investigation indicates that such a system is operationally practical. The Board proposed such a possible change in June. At present, reserves are posted on the basis of deposits held two weeks earlier.

Business-day reserve computation period

The Board has determined not to adopt a business-day computation period at this time. Nevertheless, the Board expects that depository institutions will not engage in reserve avoidance practices under which reserve requirements are lowered by transactions that increase artificially cash items and due-from deductions. Such practices include so-called "weekend Eurocurrency exchange" transactions and borrowing arrangements involving receipt of uncollected funds and repayment in collected (or federal) funds. To ensure compliance, the Federal Reserve will monitor individual institutions and will consider the need for implementation of additional measures, including adoption of a business-day (in place of the current seven-day) reserve computation week.

Due-from/due-to's

In view of comment received regarding the additional operational difficulties institutions would encounter, the Board has determined not to adopt

at this time a proposal made in June to eliminate the reserve requirement against due-to accounts nor to require changes in the use of due-from balances. The Board indicated that it would continue to study this matter.

Educational Activities

Representatives of the Federal Reserve Banks will carry out an intensive educational program on the requirements of the Act and Regulation D in meetings with groups of representatives of depositories, expected to reach all institutions affected by the new reserve requirements, before the new requirements go into effect.

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TITLE 12--BANKS AND BANKING

CHAPTER II--FEDERAL RESERVE SYSTEM

SUBCHAPTER A--BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

[Regulation D]

(Docket No. R-0306)

Part 204--RESERVE REQUIREMENTS OF DEPOSITORY INSTITUTIONS

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Final rule.

SUMMARY: The Monetary Control Act of 1980 (Title I of P. L. 96-221) imposes Federal reserve requirements on depository institutions that maintain transaction accounts or nonpersonal time deposits. The Act authorizes the Federal Reserve to require reports from depository institutions as necessary or desirable to monitor and control monetary and credit aggregates, provides access to the Federal Reserve discount window for depository institutions with transaction accounts or nonpersonal time deposits, and requires the Federal Reserve to price its services and provide access to system services to all depository institutions. The Board has adopted a revised Regulation D--Reserve Requirements of Depository Institutions (12 CFR Part 204) to implement the reserve requirement provisions of the Monetary Control Act. The revised reserve requirement regulation will also apply to Edge Act and Agreement Corporations and United States branches and agencies of foreign banks.

DATE: November 13, 1980. On that date, depository institutions, U. S. branches and agencies of foreign banks, and Edge and Agreement Corporations will be required to commence maintaining required reserves under revised Regulation D based upon deposits held during the seven-day reserve computation period beginning October 30, 1980.

FOR FURTHER INFORMATION CONTACT: Gilbert T. Schwartz, Assistant General Counsel (202/452-3625), Paul S. Pilecki, Attorney (202/452-3281), or Thomas D. Simpson, Senior Economist (202/452-3361), Board of Governors of the Federal Reserve System, Washington, D. C. 20551.

SUPPLEMENTARY INFORMATION: The Monetary Control Act of 1980 ("Act") (Title I of Pub. L. 96-221; 94 Stat. 132) imposes Federal reserve requirements on depository institutions that maintain transaction accounts or nonpersonal time deposits. Depository institutions subject to reserve requirements include any Federally-insured commercial or savings bank, or any such

bank that is eligible to become insured by the Federal Deposit Insurance Corporation; any mutual or stock savings bank; any savings and loan association that is a member of a Federal Home Loan Bank, insured by, or eligible to apply for insurance with, the Federal Savings and Loan Insurance Corporation; and any credit union that is insured by, or eligible to apply for insurance with, the National Credit Union Administration Board. The reserve requirements of the Act will apply to United States branches and agencies of foreign banks with total worldwide consolidated bank assets in excess of \$1 billion, and to Edge and Agreement Corporations. In this regard, the Act provides that nothing in the reserve requirement provisions of the Act limits the authority of the Board under section 7 of the International Banking Act of 1978 ("IBA") (12 U.S.C. § 3105). On March 19, 1980, the Board adopted amendments to Regulation D to impose reserve requirements on such branches and agencies (45 Fed. Reg. 19216); however, as discussed below, the revised regulation modifies certain aspects of that action in view of the enactment of the Monetary Control Act. In addition, since U.S. branches of foreign banks are eligible to apply for Federal deposit insurance, Regulation D also will apply to foreign banks with total worldwide consolidated bank assets of \$1 billion or less in the same manner as applicable to other nonmember depository institutions.

In light of the enactment of the Monetary Control Act, on June 4, 1980, the Board requested public comment (45 Fed. Reg. 38388) on a revised Regulation D to implement the provisions of the Act. The period for public comment expired on July 15, 1980. After consideration of the more than 750 comments received from the public (primarily from depository institutions and financial institution trade groups), the Board has adopted a revised Regulation D substantially in the form proposed. However, certain modifications were made, as discussed below, relating primarily to the definition of a transaction account and in the area of nonpersonal time deposits. In addition, certain technical changes were made in order to clarify regulation.

DIGEST OF BOARD ACTIONS

The following is a general description of certain aspects of the Board's actions with respect to the imposition of reserve requirements that are broadly applicable to all depository institutions. A detailed discussion of the reserve requirements and various technical issues follows this digest.

General Requirement. A depository institution is required to maintain reserves against its transaction accounts and nonpersonal time deposits. An institution's reserve requirements are computed on the basis of the institution's average daily net deposit balances during a seven-day period beginning each Thursday (the "computation period").

Required reserve balances must be maintained at a Federal Reserve Bank during a corresponding seven-day period (the "maintenance period") which begins on the second Thursday following the end of the computation period. However, in determining the reserve balance to be held with the Federal Reserve during the maintenance period, the average daily United States currency and coin held during the computation period is deducted from the institution's reserve requirements. The first reserve maintenance period under revised Regulation D will begin November 13, 1980 based on deposits held during the reserve computation period beginning October 30, 1980.

Transaction Accounts. A "transaction account" is defined to include demand deposits, negotiable order of withdrawal (NOW) accounts, savings accounts subject to automatic transfers (ATS), share draft accounts, accounts that permit payments to third parties through use of a check, draft, negotiable instrument, debit card or other similar items, accounts under the terms of which a depositor is permitted to make more than three preauthorized or telephone transfers per month (whether to another account of the depositor or to a third party), and accounts that permit a depositor to make payments to third parties through automated teller machines or remote service units. An account is not regarded as a transaction account merely because it permits repayments or transfers in connection with loans made by the institution itself (as originator or servicer). Whether an account is a transaction account by virtue of the number of telephone or preauthorized transfers (excluding loan repayments) permitted is to be determined based upon the terms of the account contract or by practice of the depository institution and not on the basis of the actual number of transfers made in a particular calendar month. Institutions are expected to establish adequate monitoring procedures or systems to insure that the number of transfers made in a calendar month does not exceed the permissible amount in order for such accounts not to be regarded as transaction accounts.

The reserve ratio on transaction accounts will be 3 per cent on amounts of \$25 million or less and 12 per cent on amounts in excess of \$25 million. In computing the amount of its transaction accounts, a depository institution is permitted to deduct all cash items in process of collection and balances due on demand from other depository institutions.

Nonpersonal Time Deposits. The Act defines "nonpersonal time deposit" as a (1) time deposit or account that is transferable or (2) a time deposit or account representing funds deposited to the credit of, or in which any beneficial interest is held by, a depositor that is not a natural person. Under the regulation, a time deposit includes certificates of deposit, certificate accounts, credit union share certificates, notice accounts, and regular accounts, savings deposits and share accounts that are not regarded as transaction accounts. Time deposits issued to and held by natural persons are not subject to reserve requirements if they are

not transferable. Time deposits that are issued in transferable form on or after October 1, 1980 will be regarded as nonpersonal time deposits because of the transferability feature. The definition of nonpersonal time deposit excludes a time deposit issued to and held by a natural person on or after October 1, 1980, if it includes on the deposit instrument or other document evidencing the account a specific statement that it is not transferable, or is transferable only on the books of, or with the permission of, the depository institution. To meet this requirement, a depository institution may use the following terminology or any other statement of equivalent legal effect: "Not transferable;" "Nontransferable;" "Not transferable, as defined in 12 CFR Part 204;" or "Not transferable except on the books of the depository institution." However, the words "Not negotiable" and "Nonnegotiable" will not meet this requirement. Depository institutions may stamp the required terminology on existing stocks of deposit documents.

A transferable time deposit issued before October 1, 1980, to a natural person will not be regarded as a nonpersonal time deposit. Prior to that date, depository institutions shall refrain from issuing transferable time deposits to natural persons that might otherwise be issued in the name of a corporation or other organization for the purpose of avoiding reserve requirements.

Since the provision of the Act defining transferable time deposits as nonpersonal time deposits was intended to prevent the evasion of reserve requirements through the transfer of time deposits from individuals to organizations or governmental units, the Board will not regard as "transfers" a number of transactions that normally would not be undertaken as reserve avoidance devices. A time deposit will not be regarded as "transferable" because it can be pledged as collateral for a loan, or because title or beneficial interest in the deposit can be passed in circumstances involving death, bankruptcy, divorce, marriage, judicial attachment, incompetency, or by operation of law. In addition, the reissuance of a time deposit by a depository institution in the name of another will not be regarded as a transfer.

Nontransferable time deposits representing funds held pursuant to Individual Retirement Accounts (IRA) and Keogh (H. R. 10) Plans will be regarded as personal time deposits. Escrow accounts, such as funds held for tax or insurance payments, will be regarded as personal time deposits if the depositor is a natural person and the other conditions of a time deposit are met, even though the funds are held by the depository institution or other organization as escrow agent. In addition, the Board will regard nontransferable time deposits held by fiduciaries as personal time deposits exempt from reserve requirements where the entire beneficial interest in the funds is held by natural persons. A natural person is an individual or a sole proprietorship. A partnership,

corporation (including one solely owned by an individual), governmental unit, or other association or organization (including a not-for-profit organization) is not a natural person.

Depository institutions will be permitted to estimate (using standard sampling methods) the breakdown between personal and nonpersonal categories of fixed maturity time deposits issued prior to October 30, 1980, the beginning of the first deposit reporting period under the revised regulation. All existing savings deposits, time deposit open accounts and notice accounts, as well as fixed maturity time deposits issued on or after October 30, 1980, are required to be classified as either personal or nonpersonal. Savings deposits, time deposit open accounts and notice accounts may not be estimated since these accounts do not have a stated maturity and if estimation were permitted for such accounts, they would always be reported on the basis of estimates rather than actual amounts.

Nonpersonal time deposits with original maturities of 14 days or more but less than four years will be subject to a reserve requirement ratio of 3 per cent. Nonpersonal time deposits in the form of borrowings from non-U.S. offices of unrelated depository institutions with original maturities of less than four years also will be subject to a reserve requirement of 3 per cent. All nonpersonal time deposits with original maturities of four years or more will be subject to a zero per cent reserve requirement.

Eligible Reserve Assets. The reserves of a depository institution may be held in the form of vault cash or a balance maintained at the Federal Reserve Bank, either directly or indirectly on a pass-through basis. A depository institution that is a member of the Federal Reserve System must hold its required reserve balances directly with its Federal Reserve Bank. A nonmember depository institution may hold its required reserve balance directly with its Federal Reserve Bank or, alternatively, it may pass its required reserve balance to the Federal Reserve through a correspondent. Such a correspondent may be a depository institution that holds a required reserve balance directly with the Federal Reserve, a Federal Home Loan Bank, or the National Credit Union Administration Central Liquidity Facility. A depository institution is permitted to use all of its vault cash, that is, United States currency and coin, as eligible reserve assets. However, silver and gold coin and other currency and coin whose numismatic or bullion value is substantially in excess of face value will not be regarded as vault cash.

On June 26, 1980, the Board announced (45 Fed. Reg. 44962) proposed procedures for nonmember depository institutions to follow if they maintain required reserves under a pass-through arrangement. The Board's final pass-through procedures will be announced shortly.

Phase-in of Reserve Requirements. (1) Member banks will be phased down to the new structure of reserve requirements over a three and one-half year period from the effective date of the Act, September 1, 1980. During this period, reserves required to be maintained will equal

required reserves under the reserve structure in effect on August 31, 1980 ("old structure") less a portion of the difference between reserves calculated under the structure of the Act ("new structure") and the old structure. In order to relieve the reporting burden during the phase-in period, a member bank's required reserves will be computed under the old structure using its average reserve ratio on time deposits during the 14-day period from July 24 - August 6, 1980. This average ratio will be used throughout the phase-in period to compute required reserves on time deposits under the old structure.

Member banks will begin to phase down to the new reserve requirement structure during the reserve maintenance period beginning November 13, 1980. At that time, required reserves will be reduced by 1/4 of the difference between reserves under the old structure and the new structure. The phase-down adjustment will increase by 1/8 of the difference between reserves computed under the old and new structures beginning in September 1981, and at each six-month interval thereafter until the new reserve structure is phased in fully.

(2) Nonmember depository institutions will be required to hold an amount equal to 1/8 of reserve requirements calculated under the Act beginning with the reserve maintenance period beginning November 13, 1980. During the seven-day maintenance period beginning on that date, a nonmember depository institution will maintain reserves based on its deposits and vault cash outstanding during the seven-day computation period beginning October 30, 1980. Thereafter, the amount of required reserves will increase by an additional 1/8 of the reserve requirements under the Act on the first maintenance period beginning after September 1, of each succeeding year until the new reserve structure is implemented fully.

(3) United States branches and agencies of foreign banks will phase in to the new reserve requirements on a quarterly basis over a two-year period beginning November 13, 1980.

(4) Reserve requirements on NOW accounts outside New England, New York and New Jersey, authorized pursuant to Federal law on December 31, 1980, will not be subject to the phase-in provisions.

Quarterly Reporting and Reserve Maintenance. To ease the reporting burden and Reserve Bank administration, the Board has adopted a procedure of quarterly reporting and reserve maintenance for institutions that have less than \$5 million in total deposits. This procedure will begin in January 1981. This procedure will not apply to Edge or Agreement Corporations or to U.S. branches and agencies of foreign banks.

Deferred Effective Date for Smaller Institutions. To further relieve potential operational problems during the initial period of reserve maintenance by depository institutions, the Board has deferred

until May 1981 reserve requirements and reporting for institutions with total deposits of less than \$1 million. At that time, the Board will make a determination as to whether to continue to defer reserve requirements on such institutions.

Contemporaneous Reserve Accounting. The Board is disposed toward returning to contemporaneous reserve accounting, possibly by September 1981, if a further investigation indicates that such a system is operationally practical.

DETAILED DISCUSSION

Transaction Accounts

Definition. The Board proposed to define transaction accounts to include all demand deposits, negotiable order of withdrawal (NOW) accounts, savings accounts subject to automatic transfer (ATS), share draft accounts, accounts subject to preauthorized or telephone transfer or withdrawal and all accounts that permit the account holder to make third-party payments using automated teller machines (ATMs) or remote service units (RSUs). The Board invited comment on the desirability and feasibility of exempting from reserve requirements those accounts subject to preauthorized or telephone transfers that are limited to a minimal number of transfers per month for special purposes, such as loan repayments and occasional transfers or withdrawals by telephone from a savings account to a checking account.

Comments from the public indicated that the proposed definition of a transaction account was too broad, that accounts that were not normally used for transaction purposes would be covered and that the proposal could adversely affect the level of services offered by depository institutions. Consequently, the Board has narrowed the definition of the term "transaction account" so as not to interfere with occasional withdrawal or payment arrangements. Under the regulation, "transaction account" includes demand deposits, NOW accounts, ATS accounts, share draft accounts, accounts that permit payments to third parties through use of checks, drafts, negotiable instruments, debit cards or other similar items, accounts that permit a depositor to make payments to third parties through ATMs or RSUs, and accounts that permit a depositor to make more than three telephone or preauthorized transfers per calendar month. Under this approach, those accounts that are actively used for transaction purposes will be subject to transaction account reserve requirements.

With regard to accounts subject to telephone or preauthorized transfer, the determination of whether such an account is a transaction account must be made on the basis of the number of transfers authorized

in a calendar month under the terms of the account agreement rather than on the basis of the number of transfers actually made in a particular month. A preauthorized transfer includes any arrangement by the depository institution to pay a third party from the account of a depositor upon written or oral instruction (including an order received through an automated clearing house (ACH)), or any arrangement by a depository institution to pay a third party from the account of the depositor at a predetermined time or on a fixed schedule. For example, if under the terms of a savings account agreement (written or oral) or if permitted by custom or practice of the institution a depositor is allowed to make more than three telephone transfers during a calendar month, including transfers to third parties for purposes of making payments or transfers to another account, then such an account would be a transaction account. This account would be a transaction account at all times even if a depositor never made more than three transfers during a particular calendar month.

In order for an account that permits telephone or preauthorized transfers to be exempt from transaction account reserve requirements, the account must provide that no more than three such transfers per calendar month are permitted and the account must not otherwise meet the definition of a transaction account. A depository institution is required to establish a system or other procedure to insure that no more than three such transfers are made during any calendar month from such accounts. A savings account will not be regarded as a transaction account merely because it permits the depositor to make loan repayments and pay associated expenses, such as insurance and escrow requirements, to the institution itself (as servicer or originator). (Arrangements providing for credit extended to cover checks drawn on a zero balance or low balance account are regarded as ATS accounts.) In addition, an account would not be regarded as a transaction account because withdrawals to be paid directly to the depositor could be effected by telephone or preauthorized order. All other telephone and preauthorized transfers, including those made to third parties or to another deposit account of the same depositor, would count toward the three permissible transfers per month.

Summary of Transaction Account Classifications

Always Regarded as Transaction Accounts

1. Demand deposits
2. NOW accounts
3. Share draft accounts
4. ATS accounts
5. Accounts that permit third party payments through ATMs or RSUs

6. Accounts that permit third party payments through use of checks, drafts, negotiable instruments, debit cards or other similar items.

Accounts Regarded as Transaction Accounts If More Than Three of the Following Transactions Per Calendar Month Are Permitted to Be Made by Telephone or Preauthorized Order or Instruction

1. Payments or transfers to third parties
2. Transfers to another account of the depositor at the same institution
3. Transfers to an account at another depository institution

Not Regarded as Transaction Accounts (Unless Specified Above)

1. Accounts that permit telephone or preauthorized transfers or transfers by ATMs or RSUs to repay loans made or serviced by the same depository institution
2. Accounts that permit telephone or preauthorized withdrawals where the proceeds are to be mailed to or picked up by the depositor
3. Accounts that permit transfers to other accounts of the depositor at the same institution through ATMs or RSUs
4. Accounts that permit three or less telephone or preauthorized payments or transfers to third parties or to other accounts

Bona Fide Cash Management Arrangements. In determining the amount of outstanding transaction accounts to which the reserve ratio will apply, a depository institution shall not treat overdrafts in a demand deposit account as negative demand deposits. Since overdrafts are properly reflected on an institution's books as assets, they shall not be netted against positive balances in other transaction accounts; for purposes of reporting deposits, accounts in overdraft status shall be regarded as having a zero balance. However, under present interpretations, in cases where a customer has multiple demand deposit accounts with a member bank, overdrafts in one account pursuant to a bona fide cash management arrangement are permitted to be netted against demand balances in other accounts for reserve requirement purposes. Under revised Regulation D, depository institutions will be permitted to continue this practice.

Computation of Net Transaction Accounts. In computing demand deposit reserve requirements, member banks currently are permitted to deduct from their gross demand deposits cash items in the process of collection ("CIPCs") and demand balances due from other banks. The purpose of this deduction is to prevent situations in which more than one institution holds required reserves against the same deposit liability to the nonbank public.

The Board requested comment on the desirability of substituting an exemption from reserve requirements for balances "due to" depository institutions for a "due from" deduction. It was noted that such a treatment of "due from's" and "due to's" is more consistent with an institutional environment in which all depository institutions are subject directly to Federal reserve requirements and, in such an environment, there is no longer a need to control the deposits of nonmember institutions indirectly through reserve requirements on the deposits nonmembers hold with their member bank correspondents. Moreover, it was suggested that such a treatment of interbank transactions would reduce the risk that distortions in measures of the monetary aggregates could arise from the clearing of checks and improve monetary control by removing one source of disturbance to the multiplier connecting reserves to the money stock.

Comment from the public generally was adverse on this issue, indicating that such an approach would be operationally burdensome. In view of the comments received, the Board has determined not to adopt this procedure at this time, but will continue to study the matter. Consequently, a depository institution generally will be permitted to deduct all cash items in process of collection and all balances due on demand from U. S. offices of other institutions subject to Federal reserve requirements from the sum of all transaction accounts in computing reserve requirements. Although requests have been received by the Board to expand the definition of CIPC to include credit card sales slips, the Board has determined that credit card sales slips will continue not to be regarded as cash items in process of collection.

Reserve Requirement Ratio. The Act specifies that any reserve requirement imposed by the Board shall be solely for the purpose of implementing monetary policy and shall be applied uniformly to all transaction accounts at all depository institutions. A reserve ratio of 3 per cent on transaction accounts of \$25 million or less is established by the Act. This low reserve requirement tranche will be adjusted annually beginning in 1982 based on the change in the total of transaction accounts at all depository institutions during the previous year. With regard to transaction accounts in excess of \$25 million, the Board has established a reserve ratio of 12 per cent, the initial ratio established by law. This ratio may be varied within a range of from 8 to 14 per cent.

Nonpersonal Time Deposits

Definition. The Act defines "nonpersonal time deposit" as a (1) transferable time deposit or account, or (2) a time deposit or account representing funds deposited to the credit of or in which any beneficial interest is held by a depositor that is not a natural person. Nontransferable time deposits solely in the name of, or in which the entire beneficial interest is held by, a natural person are not be subject to reserve requirements. Under the revised Regulation D, the term "savings deposit" will continue to be included in the definition of "time deposit;" thus any savings deposit that is not otherwise regarded as a transaction account and that is held by a business or nonprofit organization or a domestic governmental unit would be regarded as a nonpersonal time deposit.

Time deposits that are issued in transferable form on or after October 1, 1980 will be regarded as nonpersonal time deposits because of the transferability feature. The provision of the Act that defines transferable time deposits as nonpersonal time deposits was intended to prevent the evasion of reserve requirements through the transfer of time deposits from individuals to organizations or governmental units. Accordingly, the Board has determined that a transferable time deposit issued before October 1, 1980, to a natural person in a denomination of less than \$100,000 would not be regarded as a nonpersonal time deposit.^{1/} In addition, a transferable time deposit of any denomination issued to a natural person before that date will be regarded as exempt from the reserve requirement on nonpersonal time deposits. The definition of nonpersonal time deposit excludes a time deposit issued to and held by a natural person on or after October 1, 1980, if it includes on its face a statement that it is not transferable or if it is transferable only on the books of, or with the permission of, the depository institution. To meet this requirement, a depository institution may use the following terminology or any other statement of equivalent legal effect: "Not transferable;" "Nontransferable;" "Not transferable, as defined in 12 CFR Part 204;" or "Not transferable except on the books of the depository institution." However, the words "Not negotiable" and "Nonnegotiable" will not meet this requirement since such terms would not prohibit the depositor from engaging in certain types of transactions that could

^{1/} The date was originally proposed as July 15, 1980. However, in response to numerous comments expressing concern over the ability of institutions to meet this deadline, the Board modified the date to September 1, 1980 (see 45 Fed. Reg. 47846). This date has been modified further to October 1, 1980.

lead to an evasion of reserve requirements. In this regard, the transferee of a nonnegotiable time deposit would not be a holder in due course and would not have the ability to cut off certain defenses of an obligor. Although such a transferee would be in a less desirable position vis-a-vis a transferee of a negotiable time deposit, an exchange for value can be made and reserve avoidance transactions would be possible. Consequently, in order to prevent this possibility, a time deposit issued to a natural person on or after October 1, 1980 must be nontransferable in order to be exempt from reserve requirements.

Depository institutions may stamp, type or otherwise affix the required legend to existing stocks of deposit documents. Any personal time deposit or account originally issued before October 1, 1980, would not require a legend to be exempt from reserve requirements, including time deposits that automatically renew after that date and accounts to which additional funds can be added. The required legend must appear on the document that evidences an account issued on or after October 1, 1980 whether in certificate, passbook, statement, or book-entry form.

Depository institutions should not issue time deposits in the name of a natural person prior to October 1 that normally would be issued in the name of a corporation or other organization. The Board expects that depository institutions will observe the grandfather date for transferable personal time deposits in good faith.

Transferability. A number of comments received from the public raised questions concerning the potential limitations that could be imposed by designating a time deposit "not transferable." As stated above, the provision of the Act including transferable time deposits as nonpersonal time deposits was intended to prevent the evasion of reserve requirements by transferring time deposits from natural persons to nonexempt entities. Accordingly, the Board will not regard a time deposit as "transferable" although it can be pledged as collateral for a loan from any lender, or even if title or beneficial interest in the deposit or account can be passed on in circumstances arising from death, bankruptcy, divorce, marriage, incompetency, attachment or otherwise by operation of law. In addition, the reissuance of a time deposit by an institution in the name of another or the addition or subtraction of names on the time deposit will not be regarded as a transfer. In this regard, a depository institution's involvement in the transaction would enable it to know if any beneficial interest in the time deposit is being acquired by other than a natural person, and, thus, the appropriate reserve requirement change could be made.

IRA and Keogh Plan Time Deposits and Escrow Funds. The Monetary Control Act provides that any time deposit held in the name of a depositor that is not a natural person is subject to reserve requirements on nonpersonal time deposits. Under this provision IRA and Keogh Plan time deposits, which can only be issued to individuals, would be treated as nonpersonal time deposits since they are held by the depository institution as trustee or custodian due to the technical requirements of the Internal Revenue Code. Since these deposits are indistinguishable from other personal time deposits and are regarded by the depositor as his own funds subject to his direct control, the Board will regard such funds as personal time deposits.

In addition, escrow accounts, such as funds held for tax or insurance payments, will be regarded as personal time deposits if the depositor is a natural person and the other conditions of a time deposit are met, notwithstanding that the funds are held by the depository institution or other organization as escrow agent. (If escrow funds are held in any other type of deposit account, they will be regarded as a transaction account.)

Time Deposits Held by Trustees. A number of commentators raised the issue as to the appropriate treatment of time deposits held by trustees and other fiduciaries where the entire beneficial interest is held by natural persons. The Board believes that the imposition of reserve requirements on such funds is not necessary for the conduct of monetary policy. Therefore, any nontransferable time deposit held in the name of a trustee or other fiduciary, whether or not a natural person, will be regarded as a personal time deposit if the entire beneficial interest is held by natural persons. A nontransferable time deposit that is an asset of a pension fund would normally be regarded as a personal time deposit since the entire beneficial interest of such funds normally is held by natural persons.

Definition of Natural Person. Consistent with its longstanding positions currently embodied in Regulations D and Q as to what constitutes an individual for purposes of maintaining a NOW, ATS, or savings account, the Board will regard a "natural person" to consist of an individual and a sole proprietorship. "Natural person" will not include a partnership, corporation (including one solely owned by an individual), governmental unit, or other association or organization.

Estimation of Personal Time Deposits. A number of depository institutions inquired during the comment period whether they would be permitted to estimate the breakdown between the amount of outstanding personal and nonpersonal time deposits. The Board has determined to permit depository institutions to estimate (using standard sampling methods) funds held in fixed maturity time deposits issued before October 30, 1980, the beginning of the first computation period for reserve requirements under the revised regulation.

Amounts of personal and nonpersonal time deposits held in savings accounts, time deposit open accounts and notice accounts may not be estimated since such accounts do not have a stated maturity and reliance on estimates of such accounts, therefore, would continue indefinitely into the future. An institution will be required to classify as personal or nonpersonal all existing savings, time deposit open accounts and notice accounts as well as new fixed maturity time deposits issued on or after October 30, 1980.

Maturity of Time Deposits. The Board has adopted its proposal to shorten the minimum maturity of time deposits for purposes of Regulations D and Q from the present 30 days to 14 days. The Board believes that the shorter minimum maturity on time deposits will improve the competitive position of domestic depository institutions vis-a-vis open market instruments and foreign banking offices. Beginning October 30, 1980, member banks and U. S. branches and agencies of foreign banks that are subject to Regulation Q (12 CFR Part 217) may issue time deposits with original maturities between 14 and 29 days issued in denominations of \$100,000 or more and pay interest on such deposits at any rate since there are no Federal interest rate limitations on time deposits issued in such denominations. It is anticipated that the other Federal financial institution regulatory agencies will consider taking similar action with respect to the definition of the term time deposit and that the Depository Institutions Deregulation Committee will consider the establishment of an interest rate ceiling on time deposits under \$100,000 with maturities of 14 to 29 days.

Gross Borrowings From Non-U.S. Offices of Unrelated Institutions. The Board has determined that the term time deposit also will include, regardless of maturity, a promissory note, an acknowledgment of advance, or a similar obligation that is issued to any office located outside the United States of another depository institution or another foreign bank, or to institutions whose time deposits are exempt from interest rate limitations under § 217.3(g) of Regulation Q (12 CFR Part 217.3(g)).

Reserve Requirement Ratio. The Board has established a reserve ratio of 3 per cent on nonpersonal time deposits with original maturities of less than four years. Nonpersonal time deposits with original maturities of four years or more will be subject to a zero per cent reserve ratio.

Treatment of Promissory Notes, Due Bills and Other Miscellaneous Obligations of Depository Institutions

Regulation D currently defines as deposits a number of sources of funds that frequently are not classified as deposits for other purposes. The Board will continue to regard as deposits promissory notes (commercial paper), ineligible acceptances (finance bills), due bills, acknowledgments

of advance, repurchase agreements against assets other than obligations of, or fully-guaranteed as to principal and interest by, the United States government and its agencies, and funds supplied from nondepository affiliates. Generally, such obligations having original maturities of less than 14 days will be regarded as demand deposits and will be subject to the reserve requirement on transaction accounts; those having maturities of 14 days or more will be regarded as nonpersonal time deposits, if transferable or held by a depositor other than a natural person. Under this approach, certificates of indebtedness issued by credit unions and mortgage-backed bonds and commercial paper issued by all depository institutions including savings and loan associations will be defined as deposits. While such obligations with original maturities of four years or more will be regarded as time deposits, they will be subject to a zero per cent reserve requirement.

Subordinated Notes. Under Regulations D and Q (Interest on Deposits) subordinated capital debt of member banks is not regarded as a deposit subject to reserve requirements or interest rate limitations provided that certain conditions are met, including a minimum maturity of seven years or more. The Board proposed to retain these conditions for depository institutions. In this regard, the Federal Deposit Insurance Corporation has similar rules concerning issuance of subordinated notes exempt from interest rate limitations by insured nonmember commercial banks (see 12 CFR Part 329). For thrift institutions, the Board proposed a similar exemption from reserve requirements for subordinated capital debt. Such a debt obligation would be exempt from reserve requirements if it would have a minimum original maturity of seven years or more and was approved by the institution's primary Federal supervisor or was issued under the rules of the primary Federal supervisor. The Board has adopted these proposals as published.

Obligations of Nondepository Affiliates. The Board has adopted its proposal to revise the reserve treatment of funds advanced by affiliates to depository institutions. At present, deposits of member banks include the liability of an affiliate that it has issued to the extent that the proceeds are used for the purpose of supplying funds to the affiliated institution. However, these rules relating to determination of deposit status of such obligations are complex. In order to simplify the determination of the deposit status of affiliate obligations, the Board will apply the following rules. An obligation issued by the affiliate will not be regarded as a deposit of the affiliated depository institution if the obligation has a maturity of four years or more. In addition, an obligation issued by an affiliate will not be regarded as a deposit of the affiliated depository institution if the obligation would not have been a deposit had it been issued directly by the affiliated depository institution. For example, a borrowing by an affiliate from an unaffiliated depository institution will not be regarded as a deposit of the affiliated depository institution. However, if the proceeds from such obligations

are placed with the affiliated depository institution in the form of a deposit or other nonexempt borrowing, then such funds are reservable to the affiliated depository institution. An obligation of a nondepository affiliate will be regarded as a deposit if the obligation issued by the affiliate would have been a deposit had it been issued directly by the affiliated depository institution. For example, a borrowing by an affiliate from a nondepository business organization will be regarded as a deposit of the affiliated depository institution if the funds are supplied to the depository institution by the affiliate. If the affiliate's obligation is determined to be a deposit, then the appropriate reserve ratio to be applied will be determined by the shorter of the maturity of the affiliate's obligation or the maturity of the obligation issued to the affiliate by its affiliated depository institution. If the affiliate's obligation is determined to be a deposit and the proceeds are used to purchase assets, then the appropriate reserve ratio to be applied will be determined by the shorter of the affiliate's obligation or the remaining maturity of the assets purchased.

Due Bills. A due bill is a promise by the depository institution to deliver at some future date a security purchased by the institution's customer. Under existing provisions, due bills issued or undertaken by a member bank principally as a means of obtaining funds to be used in its banking business are regarded as deposits subject to reserves. However, due bills that are not issued principally as a means of obtaining funds to be used in the banking business are deposits only if they are not collateralized with a similar security within three days after issuance. The principal questions that arise in connection with these transactions involve whether a member bank is utilizing due bill transactions as a means of obtaining funds principally for use in its banking business and whether such obligations are collateralized with a "similar" security.

In order to minimize compliance and enforcement problems involving due bills, the Board proposed to revise Regulation D so that all due bills would be reservable deposits from the date of issuance without regard to the purpose of the due bill unless collateralized within three days from date of issuance by a security identical to the security purchased by the depository institution's customer.

Comments from the public indicated that the requirement that securities identical to those purchased be used as collateral would place dealer banks at a significant competitive disadvantage to nonbank dealers and could impair the market for U. S. government securities. In view of these comments, the Board has adopted the proposed simplifications concerning due bills in modified form, that is, eliminating the distinction between bona fide and other due bills, but requiring that the collateral provided be similar to, rather than identical to, the securities purchased. In this regard, a security will be regarded as "similar" if it is of

the same type and if its maturity is comparable to that of the obligation purchased by the customer. A due bill that remains uncollateralized after three business days is a deposit from that time forward. In addition, the Board is reviewing other aspects relating to due bills and may adopt additional operational safeguards on due bills at some future date.

Eurocurrency Reserve Requirement

Under the Act, the Board's authority to establish a reserve requirement necessary for the implementation of monetary policy on Eurocurrency transactions is extended to cover all domestic depository institutions. In addition to imposing basic reserve requirements on all depository institutions, the Board is authorized also to place reserve requirements on: net borrowings from related foreign offices, net borrowings from unaffiliated foreign depository institutions, loans to United States residents made by overseas offices of depository institutions located in the United States, and sales of assets by depository institutions in the United States to their overseas offices. With the exception of net borrowings from unaffiliated foreign depository institutions, these are essentially the same categories that are reservable under Regulation D currently. As explained below, using its basic reserve requirement authority as well as a portion of its Eurocurrency reserve requirement authority, the Board has determined to continue to subject to reserve requirements the same categories of transactions that currently are reservable as Eurocurrency transactions, except that the proceeds of sales to foreign branches of all assets--rather than only domestic assets--will be reservable. Loans to U.S. residents made by non-U.S. offices of foreign banks will not be reservable.

Under the Board's proposed regulations, borrowings from foreign offices of unaffiliated depository institutions would continue to be reservable on a gross rather than a net basis. U. S. agencies and branches of foreign banks and some large domestic banks objected to the proposal to reserve such liabilities on a gross basis. These institutions indicated their view that the Monetary Control Act authorizes the Board to impose reserve requirements on borrowings from unaffiliated institutions only on a net basis. The Board has determined to treat these borrowings on a gross basis as time deposits under the basic reserve requirement authority of the Board rather than under the Board's additional Eurocurrency reserve requirement authority. The Board intends to review the matter of gross versus net borrowings from unaffiliated depository institutions in the context of proposals to establish Domestic International Banking Facilities.

The Board has adopted a reserve ratio of 3 per cent on Eurocurrency transactions, the same ratio applied to nonpersonal time deposits. The Board believes that this action will eliminate any artificial incentive through the reserve requirement structure that favors raising funds

offshore as compared with the domestic market. As a technical matter, the revised Regulation D reflects a change in the four-week computation and maintenance period for Eurocurrency reserves to one week periods coinciding with normal reserve computation and maintenance periods, as proposed.

Eligible Reserve Assets

The reserves of a depository institution may be held in the form of vault cash or a balance maintained at the Federal Reserve Bank, either directly or indirectly on a pass-through basis. A depository institution that is a member of the Federal Reserve System must hold its required reserve balances directly with its Federal Reserve Bank. A nonmember depository institution may hold its required reserve balance directly with its Federal Reserve Bank or, alternatively, it may pass its required reserve balance to the Federal Reserve through a correspondent. Such a correspondent may be a depository institution that holds a required reserve balance directly with the Federal Reserve, a Federal Home Loan Bank, or the National Credit Union Administration Central Liquidity Facility.

The Board has the authority to specify the portion of vault cash that a depository institution may use to meet its reserve requirements. Under Regulation D, a depository institution will be permitted to use all of its vault cash as eligible reserve assets. Vault cash consists of United States currency and coin, and does not include securities or earning assets of any type. In addition, all silver and gold coin and other currency and coin whose numismatic or bullion value is substantially in excess of face value will not be regarded as vault cash.

Reserve Requirement Calculation by United States Branches and Agencies of Foreign Banks

The Board has determined to continue the system of statewide aggregation for reserve computation and maintenance for branches and agencies. This procedure was adopted by the Board on March 19, 1980, in regulations (45 Fed. Reg. 19216) implementing section 7 of the IBA (12 U.S.C. § 3105), which authorizes the Board to impose reserve requirements on United States branches and agencies of foreign banks with total worldwide consolidated assets in excess of \$1 billion. However, only one \$25 million low reserve requirement tranche on transaction accounts will be permitted for each foreign bank, since its U.S. branches and agencies compete primarily with domestic money center banks, which, by statute, have only one low reserve requirement tranche. Allowing a foreign bank only one low reserve tranche is consistent with the IBA's goal of promoting competitive equality between branches and agencies and domestic depository

institutions. The Board also will allow an Edge or Agreement Corporation only one low reserve tranche on transaction accounts regardless of the number of its branches.

Under the Board's rules, a foreign bank or an Edge or Agreement Corporation will be allowed to assign its low reserve requirement tranche to any of its offices. However, if possible, the low reserve tranche must be assigned to a single office or to a group of offices filing a single aggregated report of deposits. In the event that the low reserve tranche cannot be fully utilized by a single office or by a group of offices filing an aggregated report of deposits, the unused portion may be assigned to other offices. Reassignment of the low reserve requirement tranche will be permitted on an annual basis.

Phase-in of Reserve Requirements

Member Banks. Member banks will be phased down to the new structure of reserve requirements over a three and one-half year period from the effective date of the Act, September 1, 1980. During this period, reserves required to be maintained will equal required reserves under the reserve structure in effect on August 31, 1980 ("old structure"), less a portion of the difference between reserves calculated under the structure of the Act ("new structure") and the old structure.

In order to relieve the reporting burden during the phase-in period, the Board has adopted a simplified procedure for computing reserve requirements under the old structure during this period. The Board believes that this procedure will be beneficial to the Federal Reserve and to member banks and is consistent with Congressional intent concerning transitional adjustments. Under this approach, required reserves of a member bank on time deposits under the old structure will be computed by using its average reserve ratio on total time deposits during the 14-day period from July 24 - August 6, 1980. This average ratio will be used throughout the entire phase-in period. A former member bank that did not maintain Federal reserves during this period and, thus, did not report deposits to the Federal Reserve may use the period from August 14-27, 1980 as its base period for purposes of determining its average reserve ratio on time deposits. Required reserves on remaining deposits (including savings deposits) will be computed using the existing ratios.

The current reserve ratios on time deposits are as follows:

By original maturity	
less than 180 days	
- \$0 - 5 million	3%
- over \$5 million	6%
180 days to less than 4 years	2-1/2%
4 years or more	1%

Time deposits are subject, at present under the Federal Reserve Act, to a 3% minimum reserve ratio. The average reserve ratio on time deposits will be computed by dividing the daily average total amount of required reserves on such deposits by the daily average total time deposits for the 14-day period.

Member banks will begin to phase-down to the new reserve requirement structure during the reserve maintenance period beginning November 13, 1980. Required reserves computed under the old structure will be reduced at that time by 1/4 of the difference between required reserves under the old structure and required reserves under the new structure. By having an initial reserve reduction of 25 per cent rather than 1/8 as originally proposed, member banks will be compensated for the two-month delay in implementation of the new reserve requirements. The phase-down adjustment will increase by 1/8 of the difference between reserves computed under the old and new structures, beginning in September 1981, and at each six-month interval thereafter until the new reserve structure is fully implemented.

Nonmember Banks and Thrift Institutions. Reserve requirements of nonmember banks and thrift institutions will be phased in over an eight-year period. Nonmember institutions (other than U.S. branches and agencies of foreign banks) will be required to hold an amount equal to 1/8 of reserve requirements calculated under the Act, starting with the reserve maintenance period which begins on Thursday, November 13, 1980. During the seven-day maintenance period beginning on that date, a nonmember depository institution will maintain reserves based on its deposits and vault cash outstanding during the seven-day computation period beginning October 30, 1980. Thereafter, the amount of required reserves will increase by an additional 1/8 of the reserve requirements under the Act on the first maintenance period beginning after September 1 of each succeeding year until the new reserve structure is fully implemented.

The Act provides a special phase-in provision for certain State-chartered nonmember depository institutions located in a State outside the continental United States. The Board's proposed Regulation D would have applied this provision to such institutions located in Alaska and Hawaii. However, because the Alaska Omnibus Act (Pub. L. 86-70) provides that Alaska is part of the "continental United States," the special phase-in provision of the Monetary Control Act can only apply to certain State-chartered nonmember depository institutions in Hawaii. State-chartered nonmembers in Alaska that were engaged in business on July 1, 1979, and that were not Federal Reserve members will receive the eight-year phase-in applicable to other depository institutions.

Deposits or Accounts Authorized After April 1, 1980. The Act exempts from the transitional phase-in provisions any category of deposits or accounts that are first authorized pursuant to Federal law in any State after April 1, 1980. This provision most immediately applies

to interest-bearing negotiable order of withdrawal (NOW) accounts that are authorized in States outside of New England,^{2/} New York and New Jersey on December 31, 1980. Therefore, depository institutions outside of New England, New York and New Jersey maintaining NOW accounts will be required to maintain reserves against such accounts at the full transaction account reserve ratio.

In computing reserves required to be maintained on net NOW accounts, a depository institution located outside of New England, New York and New Jersey will be permitted to deduct from its total NOW accounts a portion of its cash items in process of collection and balances due on demand from other depository institutions equal to the ratio of its NOW accounts to its total transaction accounts. In order to provide the most benefit to depository institutions, the Board will permit the the \$25 million low reserve tranche for transaction accounts to apply to transaction accounts subject to the highest reserve ratio. Under this approach, a nonmember depository institution outside of New England, New York and New Jersey phasing in reserves may apply the \$25 million tranche to its NOW accounts initially with any remaining portion applied to other transaction accounts subject to the phase-in. Transaction accounts in excess of \$25 million (other than NOW accounts) will be subject to a reserve ratio of 12 per cent, but the effective reserve ratio applicable to these accounts will be lower than 12 per cent because of the phase-in. A member bank may apply the \$25 million low reserve tranche to demand deposits or NOW accounts in computing its reserve requirements.

Branches and Agencies. Under the amendments to Regulation D adopted in connection with implementation of the IBA, branches and agencies were granted a phase-in of reserve requirements over a two-year period. This phase-in period is similar to that allowed to nonmember banks joining the Federal Reserve System. The Board has determined to allow branches and agencies to phase-in to the new reserve requirement structure that becomes effective on November 13, 1980, rather than requiring a more complicated and burdensome procedure of phasing up to member bank actual reserve requirements by the end of two years, and then phasing down to the new structure over the next two years in line with member banks. On November 13, when revised Regulation D becomes effective, branches and agencies will begin to maintain reserves subject to a two-year phase-in schedule similar to that proposed in June. Reporting will not be required of branches and agencies until the reserve computation period that begins on October 30, 1980. The deposits of new branches and agencies of a foreign bank that has existing United States branches or agencies will be entitled only to the remaining phase-in, if any, available to the existing United States branches or agencies.

The amendments to Regulations D and Q (Interest on Deposits (12 CFR Part 217)) that were adopted in March in connection with implementation of the IBA will go into effect on September 4, 1980, as originally

^{2/} Massachusetts, New Hampshire, Connecticut, Rhode Island, Vermont and Maine.

scheduled, although reserves will not be required to be held until November 13, 1980. Federal Reserve credit facilities also will be available beginning September 4, 1980. System services will be made available to branches and agencies beginning in November 1980 when they actually begin holding reserves. However, clearing balances may be required commensurate with the level of services provided. This will promote competitive equality with member banks and take into account the shorter reserve requirement phase-in period applicable to branches and agencies.

De Novo Banks and New Members. The Act provides an eight-year phase-in only for nonmember depository institutions engaged in business on July 1, 1979. Consequently, a de novo nonmember depository institution opening after July 1, 1979, would be required to maintain full reserve requirements beginning on the effective date of the Act. In addition, under the Act, a de novo member or a nonmember joining the System ("new member") would be required to maintain full present member bank reserve requirements, and then phase down to the new requirements of the Act. Current Board policy provides a two-year transitional period to full reserve requirement levels for de novo and new member banks.

The Board believes that, in order to provide an orderly adjustment to reserve requirements, it is appropriate for the Federal Reserve to continue its policy of providing a 24-month transitional phase-in for all de novo depository institutions and new members. Under the Board's action, de novo institutions and new members will be phased in to the new reserve requirements under the Act rather than to present member bank reserve requirements. New member banks on or after September 1, 1980, will not be required to report deposits or maintain reserves until the revised regulation becomes effective. This transition policy will also apply to a newly formed Edge or Agreement Corporation, or a foreign bank establishing its initial branch or agency in the United States.

Former Members and Mergers. On April 23, 1980, the Board announced an interpretation (12 CFR 204.120; 45 Fed. Reg. 28305) of section 19(b)(8)(D) of the Federal Reserve Act (12 U.S.C. § 461(b), as amended by section 103 of the Act). This interpretation applies to the reserves required of any bank that was a member of the Federal Reserve System on July 1, 1979, and which subsequently withdraws from membership. That interpretation also establishes a System policy for reserve requirements of depository institutions involved in mergers.

Coverage of the Act

During the comment period, several questions were received concerning the scope of institutions covered by the Act. The Board has determined that industrial banks that engage in a deposit-taking

function are covered by the Act and are subject to reserve requirements on their transaction accounts and nonpersonal time deposits, since they are eligible for Federal deposit insurance.

New York Investment (Article XII) Companies, on the other hand, are not subject to reserve requirements under the IBA, and since they accept credit balances rather than deposits, they are not eligible for Federal deposit insurance. Consequently, the Board has concluded that New York Investment Companies are not depository institutions subject to the Act.

Under the Act, bankers' banks are not subject to Federal reserve requirements. Bankers' banks are defined as depository institutions that are organized solely to do business with other financial institutions, do not do business with the general public, and are owned primarily by the financial institutions with which they do business. Questions have arisen with respect to how the Board will apply these criteria in individual cases, particularly with regard to corporate central credit unions. The Board will consider in the near future the issue of what institutions qualify for the exemption.

Quarterly Reporting for Certain Depository Institutions

The Board recognizes that many very small depository institutions--especially credit unions--may not be equipped to report to the Federal Reserve and to maintain reserves on a weekly basis. Moreover, given the substantial number of such very small institutions that might have small amounts of reservable liabilities, the Federal Reserve could encounter operational difficulty in processing reports of these institutions on a weekly basis. In an effort to reduce the reporting and reserve management burdens of very small depository institutions and to reduce the processing burden of the Reserve Banks, depository institutions with total deposits of less than \$5 million will report their deposits to the Federal Reserve for a 7-day computation period only once each calendar quarter and maintain reserves over a subsequent three-month period based on such deposits reported.

Quarterly reporting will be staggered so that each month one-third of all quarterly reporters will report deposit data for one week. Reserves will be maintained during a period beginning two weeks after the start of the computation period and ending one week after the end of the institution's next computation period. Balances to be held at the Federal Reserve over the three-month maintenance period, either directly or indirectly on a pass-through basis, would equal required reserves based on the deposit report for one week less vault cash held during the seven-day reporting period. An institution will remain eligible for quarterly reporting until its total deposits are \$5 million or more for two consecutive quarterly reports. Depository institutions eligible for quarterly reporting and reserve maintenance would retain the option of reporting and maintaining required reserves on a weekly rather than quarterly basis. Additional details will be supplied to depository institutions in the near future.

The quarterly reporting system will commence in January 1981. Small member banks will continue to report deposits and maintain reserves on a weekly basis until that time. Eligible nonmember institutions will not be required to report or maintain reserves until the quarterly procedure begins. It should be noted that Edge and Agreement Corporations and U.S. branches and agencies of foreign banks will not be eligible for quarterly reporting and reserve maintenance. Rather, all such institutions will--regardless of size--be required to report and to maintain reserves on a weekly basis.

In addition, the Board has deferred reserve requirements for institutions that have less than \$1 million in total deposits as of December 31, 1979. These institutions will be exempt from reporting and reserve maintenance until May 1981, at which time the Board will determine whether a further delay is warranted.

Contemporaneous Reserve Accounting

The Federal Reserve Board is disposed toward returning to contemporaneous reserve accounting, possibly by September 1981, if a further investigation of potential operational difficulties indicates that such a system is practical. Under contemporaneous reserve accounting, the reserve computation and reserve maintenance weeks would coincide. Reserve computation would be based on daily opening-of-business balances while reserves maintained would be based on daily close-of-business balances. Among the issues to be studied are the feasibility of such a reserve accounting system for all types of depository institutions, potential complications arising from pass-through arrangements, and the relation to reserve carryover.

Business Day Computation Period

The Board has determined not to adopt a business-day computation period at this time. However, the Federal Reserve Board expects that depository institutions will not engage in reserve avoidance practices under which reserve requirements are lowered by transactions that artificially increase cash items in the process of collection and "due from" deductions. Included among such practices are so-called "week-end Eurodollar arbitrage" transactions and borrowing arrangements involving the receipt of uncollected funds and repayment in collected (or Federal) funds. To ensure compliance, the Federal Reserve will monitor individual institutions and consider the need for implementation of additional measures, including adoption of a business-day reserve computation week.

* * * * *

The following table presents reporting categories that will be required of depository institutions, Edge and Agreement Corporations and United States branches and agencies of foreign banks.

Table

Reporting categories for institutions subject to reserve requirements:

1. Demand deposits due to banks.
2. Demand deposits due to other depository institutions.
3. Demand deposits due to the U. S. Government.
4. Other demand deposits (including noninterest-bearing negotiable orders of withdrawal).
5. Savings deposits authorized for automatic transfer (ATS accounts).
6. Savings deposits that permit more than three telephone or preauthorized transfers or payments per calendar month or that permit payments to third parties through automated teller machines, including remote service units.
7. Negotiable order of withdrawal (NOW) accounts; share drafts.
8. Demand deposits due from depository institutions.
9. Cash items in process of collection.
10. Other savings deposits (i.e., all savings deposits other than those included in items 5, 6, or 7 above)--personal.
11. Other savings deposits--nonpersonal.
12. Personal time deposits.
13. Nonpersonal time deposits with original maturities of 14 days or more but less than 4 years.
14. Nonpersonal time deposits with original maturities of 4 years or more.
15. Time deposits of \$100,000 or more.
16. Vault cash.
17. Funds received from issuance of obligations by affiliates and from the sale of ineligible bankers' acceptances have remaining maturities of less than 14 days.

18. Funds received from issuance of obligations by affiliates and from the sale of ineligible bankers' acceptances that have remaining maturities of 14 days or more but less than 4 years--personal.
19. Funds received from issuance of obligations by affiliates and from the sale of ineligible bankers' acceptances that have remaining maturities of 14 days or more but less than 4 years--nonpersonal.
20. Borrowings from offices of other depository institutions outside the United States, foreign national governments, and international institutions.
- *21. Gross balances due to own non-U. S. branches.
- *22. Gross balances due from own non-U. S. branches.
- *23. Assets sold to and held by own non-U. S. branches acquired from U. S. offices (including assets that are claims on both U. S. and non-U. S. residents).
- *24. Credit extended by own non-U. S. branches to U. S. residents.
- **25. Gross liabilities to the foreign bank (including its offices located outside the United States).
- **26. Gross claims on the foreign bank (including its offices located outside the United States).
- **27. Total assets less the sum of United States coin and currency, cash items in process of collection and unposted debits, balances due from domestic banks and other foreign banks, balances due from foreign central banks and net balances due from the foreign bank and the foreign bank's United States and non-United States offices.
- **28. Assets sold by a branch or agency to its foreign bank (including its offices located outside the United States) or its foreign parent bank holding company.

* To be reported only by U. S. depository institutions and Edge and Agreement Corporations.

** To be reported only by U. S. branches and agencies of foreign banks.

Effective November 13, 1980, pursuant to the Board's authority under sections 19, 25, and 25(a) of the Federal Reserve Act (12 U.S.C. §§ 461 et seq., 601 et seq., 611 et seq.) and section 7 of the International Banking Act of 1978 (12 U.S.C. § 3105), Regulation D (12 CFR Part 204) is revised to read as follows:

PART 204--RESERVE REQUIREMENTS OF DEPOSITORY INSTITUTIONS

Sec.

- 204.1 Authority, Purpose and Scope
- 204.2 Definitions
- 204.3 Computation and Maintenance
- 204.4 Transitional Adjustments
- 204.5 Emergency Reserve Requirement
- 204.6 Supplemental Reserve Requirement
- 204.7 Penalties
- 204.8 Reserve Ratios

FEDERAL RESERVE press release



For immediate release

August 27, 1980

The Federal Reserve Board today announced rules for nonmember depository institutions to follow if they pass required reserve balances through another institution to the Federal Reserve, and rules for these intermediaries to follow in handling the reserve balances of others.

The new rules will become effective November 13, 1980. The pass-through rules amend the Board's Regulation D (reserve requirements of depository institutions).

Under the Monetary Control Act of 1980, depository institutions are required to satisfy reserve requirements fixed by the Federal Reserve on their transaction accounts and nonpersonal time deposits. These reserves may be held in vault cash, or if vault cash is not large enough to satisfy reserve requirements, balances must be held with Federal Reserve Banks.

Depository institutions that are members of the Federal Reserve System will continue to hold their reserves directly with the Federal Reserve Bank in their Federal Reserve District. Nonmembers may hold their reserves directly with the Federal Reserve or indirectly, by passing the reserves through another institution ("pass-through correspondent").

The Board's pass-through rules are described in the attached notice. Some highlights are:

--Correspondent institutions that may receive and pass through the reserve balances of nonmember depositories are the Federal Home Loan Bank, the National Credit Union Administration Central Liquidity Facility, or a depository institution (member or nonmember) that holds a required reserve

balance directly at a Federal Reserve Bank. The Board reserves the right to permit other institutions, on a case-by-case basis, to be pass-through correspondents. U.S. branches and agencies of foreign banks and Edge and Agreement corporations may pass their required reserves through other institutions or may themselves act as pass-through correspondents.

--A respondent will be able to choose one pass-through correspondent, and that correspondent must pass the reserve balances through directly to the Federal Reserve. Such arrangements may be initiated, terminated or changed upon notification satisfactory to the Reserve Bank involved.

--In pass-through arrangements, it is the responsibility of the correspondent to assure the maintenance of the correct level of its respondent's reserve balances. The pass-through rules approved by the Board clarify the precise responsibilities of the parties to a pass-through arrangement. Reserve Banks will compare only the aggregate required reserve balance with the total actual balance held in each reserve account maintained by the correspondent for determination of reserve deficiencies, penalty liability, and other reserve maintenance purposes.

--The correspondent institution passing balances through will maintain the reserve balances it receives, dollar-for-dollar, with the Federal Reserve Bank in whose territory^{1/} the main office of the respondent is located.

--Under the rules adopted by the Board, a correspondent may choose one of the two following options with respect to handling its own required reserves and those of its respondents in the same Federal Reserve territory.

^{1/} The service area of a Federal Reserve office.

1. The correspondent may maintain its own required reserve balances, as well as those of its respondents whose head office is located in the same territory as the correspondent's head office, in a single, commingled reserve account at the Federal Reserve Bank or Branch serving the territory, or
2. The correspondent may maintain its own reserve balance in the Federal Reserve Bank or Branch serving its territory, and, in addition, maintain a separate commingled reserve account for its respondents located in the same Federal Reserve territory.

--A depository institution maintaining a reserve balance on a pass-through basis is eligible for Federal Reserve System services provided separately from its local Federal Reserve office (but where reserve balances of nonmember institutions are zero or small, it may be necessary for the institution also to maintain an adequate clearing balance).

The Board's notice setting forth the Board's pass-through rules is attached.

Attachment

TITLE 12--BANKS AND BANKING

CHAPTER II--FEDERAL RESERVE SYSTEM

SUBCHAPTER A--BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

[Regulation D]

(Docket No. R-0309)

Part 204--RESERVE REQUIREMENTS OF DEPOSITORY INSTITUTIONS

Required Reserve Balance Pass-Through Rules

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Final rule.

SUMMARY: The Monetary Control Act of 1980 (Title I of P.L. 96-221) imposes Federal reserve requirements on all depository institutions that maintain transaction accounts or nonpersonal time deposits. A depository institution can satisfy its reserve requirements with a combination of vault cash and balances held at a Federal Reserve Bank. The Act authorizes a depository institution that is not a member of the Federal Reserve System to hold its required reserve balance at the Federal Reserve in one of two ways. It may deposit its required reserve balance directly with the Federal Reserve Bank of its District. Alternatively, in accordance with procedures adopted by the Board, it may elect to pass through its required reserve balance to the Federal Reserve through a correspondent. In order to implement the pass-through provisions of the Monetary Control Act, the Board is amending Regulation D to establish rules under which pass-through arrangements may be maintained.

EFFECTIVE DATE: November 13, 1980.

FOR FURTHER INFORMATION, CONTACT: Benjamin Wolkowitz, Section Chief (202/452-2686), Paul P. Burik, Economist (202/452-2556), Gilbert T. Schwartz, Assistant General Counsel (202/452-3625), Lee S. Adams, Senior Attorney (202/452-3623) or Paul S. Pilecki, Attorney (202/452-3281), Board of Governors of the Federal Reserve System, Washington, D.C. 20551.

SUPPLEMENTARY INFORMATION: Under the provisions of the Monetary Control Act of 1980 (Title I of P.L. 96-221), Federal reserves are required for all depository institutions with transaction accounts or nonpersonal time deposits, as those terms are defined in Section 103 of the Act. If these reserve requirements are not met in full by holdings of vault cash, a depository institution that is a member of the Federal Reserve

System must satisfy its remaining requirement by directly maintaining a balance at its local Federal Reserve Bank. A depository institution that is not a member of the Federal Reserve System and does not completely satisfy its reserve requirement with vault cash must satisfy its remaining requirement by maintaining a balance with the Federal Reserve. Such a required balance can be held in one of two ways at the nonmember institution's discretion. It may deposit its required reserve balance directly with the Federal Reserve Bank of its District, just as member banks do. Alternatively, a nonmember depository institution may elect to pass its required reserve balance through a correspondent. The correspondent will pass through this required reserve balance dollar-for-dollar to the Federal Reserve Bank in the District in which the main office of the respondent institution is located. A correspondent may be (i) a Federal Home Loan Bank, (ii) the National Credit Union Administration Central Liquidity Facility, or (iii) a depository institution that maintains a required reserve balance directly at a Federal Reserve Bank. In addition, the Board reserves the right to permit other institutions, on a case-by-case basis, to serve as pass-through correspondents.

The Federal Reserve Board is amending its Regulation D to provide rules for the holding of nonmember depository institution (respondent) reserve balances. The rules as adopted by the Board are very similar to the guidelines published for comment on June 26, 1980 (45 Fed. Reg. 44962). The Board determined to adopt these provisions as part of Regulation D rather than as guidelines in order to clarify the relationships between, and responsibilities of, the parties involved in pass-through arrangements. Included in the rules are requirements for reporting and maintaining pass-through reserve accounts and the responsibilities of the various parties in a pass-through arrangement. The rules also provide the conditions for using a pass-through account to post entries arising from transactions involving the use of Federal Reserve services.

Two modifications to the proposed guidelines were adopted by the Board. First, the Board determined that a Reserve Bank, at its discretion, may require a pass-through correspondent to consolidate in a single account the reserve balances of its respondents whose head offices are located in that Federal Reserve District rather than maintain separate accounts at each office within that Federal Reserve District. Secondly, the Board decided to reserve the right to permit institutions other than the Federal Home Loan Banks, the Central Liquidity Facility, and institutions holding Federal reserves, on a case-by-case basis, to serve as pass-through correspondents.

In response to the comments that were received, the Board clarified the rules to indicate that U.S. branches and agencies of foreign banks and Edge and Agreement Corporations could serve as pass-through correspondents or respondents. The Board also decided that a pass-through correspondent would have the option either to commingle its own reserve

balance with the reserve balances of its respondents located in the same Federal Reserve territory as the correspondent in a single account or to maintain two accounts--one for its own reserve balance and a second commingled account for the reserve balances of its respondents located in the same territory as the correspondent. The rules also contain more specific procedures that a correspondent is expected to follow in managing its pass-through accounts. For example, for purposes of determining required reserve deficiencies and imposing or waiving penalties for deficiencies in required reserves, Reserve Banks will compare the total reserve balance required to be maintained in each reserve account with the total actual reserve balance held in such reserve account by the correspondent.

Effective November 13, 1980, pursuant to the Board's authority under sections 19, 25, and 25(a) of the Federal Reserve Act (12 U.S.C. §§ 461 et seq., 601 et seq., 611 et seq.) and section 7 of the International Banking Act of 1978 (12 U.S.C. § 3105), Regulation D (12 CFR Part 204) is revised to read as follows:

1. Section 204.3 is amended to read as follows:

§ 204.3 -- COMPUTATION AND MAINTENANCE

* * * * *

(i) Pass-through rules.

(1) Procedure

- (i) A nonmember depository institution required to maintain reserve balances ("respondent") may select only one institution to pass through its required reserves. Eligible institutions through which respondent required reserve balances may be passed ("correspondents") are Federal Home Loan Banks, the National Credit Union Administration Central Liquidity Facility, and depository institutions that maintain required reserve balances at a Federal Reserve office. In addition, the Board reserves the right to permit other institutions, on a case-by-case basis, to serve as pass-through correspondents. The correspondent chosen must subsequently pass through the required reserve balances of its respondents directly to the appropriate Federal Reserve office. The correspondent placing funds with the Federal Reserve on behalf of respondents will be responsible for reserve account maintenance as described in subparagraphs (3) and (4) below.

- (ii) Respondent depository institutions or pass-through correspondents may institute, terminate, or change pass-through arrangements for the maintenance of required reserve balances by providing all documentation required for the establishment of the new arrangement and/or termination of the existing arrangement to the Federal Reserve Bank in whose territory the respondent is located. The time period required for such a change to be effected shall be specified by each Reserve Bank in its operating circular.
- (iii) U.S. branches and agencies of foreign banks and Edge and Agreement Corporations may (a) act as pass-through correspondents for any nonmember institution required to maintain reserves or (b) pass their own required reserve balances through correspondents. In accordance with the provision set forth in subparagraph (3) below, the U.S. branches and agencies of a foreign bank or offices of an Edge and Agreement Corporation filing a single aggregated report of deposits may designate any one of the other U.S. offices of the same institution to serve as a pass-through correspondent for all of the offices filing such a single aggregated report of deposits.

(2) Reports

- (i) Every depository institution that maintains transaction accounts or nonpersonal time deposits is required to file its report of deposits (or any other required form or statement) directly with the Federal Reserve Bank of its District, regardless of the manner in which it chooses to maintain required reserve balances.
- (ii) The Federal Reserve Bank receiving such reports shall notify the reporting depository institution of its reserve requirements. Where a pass-through arrangement exists, the Reserve Bank will also notify the correspondent passing respondent reserve balances through to the Federal Reserve of its respondent's required reserve balances.
- (iii) The Federal Reserve will not hold a correspondent responsible for guaranteeing the accuracy of the reports of deposits submitted by its respondents to their local Federal Reserve Banks.

(3) Account Maintenance

- (i) A correspondent that passes through required reserve balances of respondents whose main offices are located in the same Federal Reserve territory in which the main office of the correspondent is located shall have the option of maintaining such required reserve balances in one of two ways: (a) A correspondent may maintain such balances, along with the correspondent's own required reserve balances, in a single commingled account at the Federal Reserve Bank office in whose territory the correspondent's main office is located, or (b) A correspondent may maintain its own required reserve balance in an account with the Federal Reserve Bank office in whose territory its main office is located. The correspondent, in addition, would maintain in a separate commingled account the required reserve balances passed through for respondents whose main offices are located in the same Federal Reserve territory as that of the main office of the correspondent.
- (ii) A correspondent that passes through required reserve balances of respondents whose main offices are located outside the Federal Reserve territory in which the main office of the correspondent is located shall maintain such required reserve balances in a separate commingled account at each Federal Reserve office in whose territory the main offices of such respondents are located.
- (iii) A Reserve Bank may, at its discretion, require a pass-through correspondent to consolidate in a single account the reserve balances of all of its respondents whose main offices are located in any territory of that Federal Reserve District.

(4) Responsibilities of Parties

- (i) Each individual depository institution is responsible for maintaining its required reserve balance with the Federal Reserve Bank either directly or through a pass-through correspondent.
- (ii) A pass-through correspondent shall be responsible for assuring the maintenance of the appropriate aggregate level of its respondents' required reserve balances. A Reserve Bank will compare the total reserve balance required to be maintained in each reserve account with the total actual reserve balance held in such reserve account for purposes of determining required

reserve deficiencies, imposing or waiving penalties for deficiencies in required reserves, and for other reserve maintenance purposes. A penalty for a deficiency in the aggregate level of the required reserve balance will be imposed by the Reserve Bank on the correspondent maintaining the account.

- (iii) Each correspondent is required to maintain detailed records for each of its respondents in a manner that permits Reserve Banks to determine whether the respondent has provided a sufficient required reserve balance to the correspondent. A correspondent passing through a respondent's reserve balance shall maintain records and make such reports as the Federal Reserve System requires in order to insure the correspondent's compliance with its responsibilities for the maintenance of a respondent's reserve balance. Such records shall be available to the Federal Reserve Banks as required.
- (iv) The Federal Reserve Bank may terminate any pass-through relationship in which the correspondent is deficient in its recordkeeping or other responsibilities.
- (v) Interest paid on supplemental reserves (if such reserves are required under section 204.6 of this Part) held by respondent(s) will be credited to the commingled reserve account(s) maintained by the correspondent.

(5) Services

- (i) A depository institution maintaining its reserve balances on a pass-through basis may obtain available Federal Reserve System services directly from its local Federal Reserve office. For this purpose, the pass-through account in which a respondent's required reserve balance is maintained may be used by the respondent for the posting of entries arising from transactions involving the use of such Federal Reserve services, if the posting of these types of transactions has been authorized by the correspondent and the Federal Reserve. For example, access to the wire transfer, securities transfer, and settlement services that involve charges to the commingled reserve account at the Reserve Bank will require authorization from the correspondent and the Reserve Bank for the type of transaction that is occurring.

- (ii) In addition, in obtaining Federal Reserve services, respondents maintaining their required reserves on a pass-through basis may choose to have entries arising from the use of Federal Reserve services posted to:
 - (a) with the prior authorization of all parties concerned, the reserve account maintained by any institution at a Federal Reserve Bank, or
 - (b) an account maintained for clearing purposes at a Federal Reserve Bank by the respondent.
- (iii) Accounts at Federal Reserve Banks consisting only of respondents' reserve balances that are passed through by a correspondent to a Federal Reserve Bank may be used only for transactions of respondents. A correspondent will not be permitted to use such pass-through accounts for purposes other than serving its respondents' needs.
- (iv) A correspondent may not apply for Federal Reserve credit on behalf of a respondent. Rather, a respondent should apply directly to its Federal Reserve Bank for credit. Any Federal Reserve credit obtained by a respondent may be credited, at the respondent's option and with the approval of the parties concerned, to the reserve account in which its required reserves are maintained by a correspondent, to a clearing account maintained by the respondent, or to any account to which the respondent is authorized to post entries arising from the use of Federal Reserve services.

By order of the Board of Governors of the Federal Reserve System, August 27, 1980.

(Signed) Theodore E. Allison

Theodore E. Allison
Secretary of the Board

[SEAL]

The

***MONETARY
CONTROL
ACT***

of 1980

The Monetary Control Act of 1980 (P.L. 96-221), enacted on March 31, 1980, is designed to improve the effectiveness of monetary policy by applying new reserve requirements set by the Federal Reserve Board to all depository institutions. Among its other key provisions, the Act 1) authorizes the Federal Reserve to collect reports from all depository institutions; 2) extends access to Federal Reserve discount and borrowing privileges and other services to non-member depository institutions; 3) requires the Federal Reserve to set a schedule of fees for Federal Reserve services; and 4) provides for the gradual phase-out of deposit interest rate ceilings, coupled with broader powers for thrift institutions.

WHO IS COVERED?

Uniform reserve requirements are imposed on all depository institutions, including commercial banks, savings banks, savings and loan associations, credit unions, and industrial banks that have transaction accounts or nonpersonal time deposits. Under the terms of the International Banking Act of 1978, the same reserve requirements will also be extended to U.S. agencies and branches of foreign banks. The revised reserve requirement rules also affect Edge Act and Agreement corporations.

REPORTING REQUIREMENTS

The Act requires all depository institutions to file reports which the Board determines to be necessary or desirable for the control or monitoring of the monetary and credit aggregates. All reports are to be made directly to the Federal Reserve.

The Board has deferred until May 1981 all reserve requirements and reporting for institutions with total deposits of less than \$1 million. The Board has also adopted quarterly rather than weekly reporting and reserve maintenance for institutions with total deposits of \$1 million to \$5 million. The quarterly reporting and maintenance procedures will begin in January 1981. Reporting forms, manuals, and other materials will be sent to quarterly respondents later this year.

All other nonmember institutions will report deposits as of October 30, 1980, and will begin maintaining reserves on November 13, 1980. Member banks will begin

Thrift Institutions

The Act also authorizes various new investment authorities for federally chartered savings and loan associations and permits them to offer credit card services and to exercise trust and fiduciary powers; expands authority to make real estate loans; authorizes Federal mutual savings banks to make commercial, corporate and business loans, subject to limitations, and to accept demand deposits in connection with a commercial, corporate, or business loan relationship; and in other ways expands the powers of thrift institutions.

FOR FURTHER INFORMATION

For more detailed information about the Act and implementing regulations, a depository institution may write to the Board of Governors of the Federal Reserve System or to its District Reserve Bank. Press releases will be issued in connection with proposals and final action on the provisions of the Act. If your institution has not been receiving such releases, please ask your District Bank to add your name to its mailing list.

In mid-September, Reserve Banks will begin a series of meetings with depository institutions to familiarize them with the new regulations and procedures.

phasing down their reserve requirements at that time also. Reporting forms, manuals, and other materials will be sent to these institutions within the next several weeks.

RESERVE REQUIREMENTS

What Reserve Requirements are Established?

Transaction Accounts. The reserve requirement on the first \$25 million of transaction accounts is 3 percent. A reserve requirement of 12 percent is established on that portion of total transaction accounts above \$25 million. The Board is required to index the \$25 million tranche annually, beginning in 1982, at 80 percent of increases or decreases in transaction accounts of all depository institutions for the previous year.

Transaction accounts are defined to include demand deposits, NOW accounts, ATS accounts, share draft accounts, and accounts subject to telephone or pre-authorized transfer when the depositor is authorized to make more than three transfers per calendar month. Accounts that permit the depositor to make third party payments through automated teller machines or remote service units are also covered. Telephone and preauthorized transfers made to third parties or to another deposit account of the same depositor are counted toward the three permissible transfers per month; telephone or preauthorized withdrawals paid directly to the depositor are not. Further, a savings account is not regarded as a transaction account merely because it permits a depositor to make loan and associated payments to the institution itself.

Nonpersonal Time Deposits. All depository institutions are required to maintain reserves against nonpersonal time deposits (including savings deposits) with maturities of less than 4 years at a ratio of 3 percent. Nontransferable personal time deposits will not be subject to reserve requirements. Time deposits with maturities of four years or more are subject to a zero percent reserve ratio.

The Act defines a nonpersonal time deposit as any time deposit or account that is transferable, or any time deposit or account held by a party other than a natural person. Under the Board's regulation, all time deposits issued to natural persons prior to October 1, 1980 are to be regarded as personal time deposits even if they are transferable. A time deposit issued on or after that date, to be a personal time deposit, must be held by a natural person and bear a statement indicating that it is not transferable.

In determining the fee schedule, the Board must price explicitly all services covered by the fee schedule, and must price all services covered by the fee schedule to non-member depository institutions at the same fee schedule applicable to member banks. However, nonmembers may be required to hold balances sufficient for clearing purposes and may be subject to any other terms that the Board applies to member banks.

PHASE-OUT OF INTEREST RATE CEILINGS

The Act provides for the orderly phase-out of limitations on the maximum rates of interest and dividends that may be paid on deposits. A Depository Institutions Deregulation Committee—with the Secretary of the Treasury, Chairman of the Federal Reserve Board, Chairman of the Board of Directors of the Federal Deposit Insurance Corporation, Chairman of the Federal Home Loan Bank Board, and Chairman of the National Credit Union Administration, as voting members, and Comptroller of the Currency as a non-voting member—is required to meet at least quarterly in order to achieve the phase-out.

POWERS OF DEPOSITORY INSTITUTIONS

General

The Act authorizes banks to continue to provide automatic transfer services from savings to checking accounts; authorizes savings and loan associations to establish remote service units to credit and debit savings accounts, or credit payments on loans, and provide related financial transactions; and authorizes federally insured credit unions to offer share draft accounts.

The Act also extends nationwide the authority for depository institutions to offer NOW accounts, effective December 31, 1980. NOW accounts may consist solely of funds in which the entire beneficial interest is held by one or more individuals or by an organization operated primarily for religious, philanthropic, charitable, educational, or other similar purposes and not operated for profit.

The insurance of accounts of federally insured banks, savings and loan associations, and credit unions has been increased from \$40,000 to \$100,000.

The Board has also shortened the minimum maturity of all time deposits to 14 days from the present 30 days.

Supplemental Reserves. Under certain conditions, and after consultation with other depository institution regulators, the Board is authorized to impose a supplemental reserve requirement of not more than 4 percent on every depository institution. Interest will be paid on supplemental reserves.

Eurocurrency Reserve Requirements. The Board has set a 3 percent reserve requirement on certain Eurocurrency activity, the same ratio as on nonpersonal time deposits. These are: net borrowings from related foreign offices; gross borrowings from unrelated foreign depository institutions; loans to U.S. residents made by overseas branches of domestic depository institutions; and sales of assets by depository institutions in the United States to their overseas offices.

How Will Reserve Requirements be Phased In?

Larger nonmember institutions will begin posting reserves on November 13, 1980; smaller institutions in early January; reserve and reporting requirements have been deferred for institutions with deposits of less than \$1 million until May 1981. Until November, member banks will continue to post reserves under existing requirements. The Board has proposed to phase in reserve requirement provisions of the Act as follows:

Nonmember Institutions. The Act provides for an eight-year phase-in period of reserve requirements for nonmember banks and thrift institutions. During the first ten-month period beginning in November 1980 the amount of required reserves will be one-eighth of the full requirement and will increase by one-eighth in September of each of the following 7 years. NOW accounts, other than those previously authorized in New England, New York and New Jersey, will be subject immediately to the full reserve requirement on transactions accounts.

Member Banks. Reserve requirements for member banks on transaction accounts and time and savings deposits will be phased down by one-fourth of the difference between the amount under the old and new reserve requirement structures on November 13, 1980; by an additional one-eighth in September, 1981; and by an additional one-eighth at six-month intervals thereafter. To reduce reporting and processing burdens, reserve requirements on time

deposits under the old structure will be determined by applying the average reserve ratio on time deposits for the two week period ending August 6, 1980 to the total amount of time deposits. This fixed average reserve ratio on time deposits will be used throughout the phase-in period. NOW accounts, other than those previously authorized in New England, New York and New Jersey, will be subject immediately to the full reserve requirement on transaction accounts.

De novo banks and banks that become member banks after March 31, 1980, will have a two-year phase-in period.

Former Member Banks. Under the Act any bank that withdrew from membership on or after July 1, 1979, must maintain reserves beginning on the date of enactment as if it had been a member bank on that date. Reserve requirements for these banks have been deferred by the Board until August 28, 1980. The date of withdrawal from membership for a state member bank will be determined by the date on which the Federal Reserve Bank received notice of the decision of the bank's board of directors (and shareholders when required by state law) to withdraw from membership. For national banks, the withdrawal date is the date on which a state charter was issued.

What are Eligible Reserves?

Reserve requirements may be met with funds deposited directly at the Federal Reserve, funds held at the Federal Reserve that are passed through a correspondent, and vault cash. A depository institution that is a member of the Federal Reserve System must hold its required reserves directly with the Federal Reserve. A nonmember institution may deposit its required reserve balance directly with the Federal Reserve or pass its required reserve balance through a correspondent. Such a correspondent may be a Federal Home Loan Bank; the National Credit Union Administration Central Liquidity Facility; or a depository institution that holds a reserve balance with the Federal Reserve.

Vault cash means United States currency and coin (with the exception of silver and gold coins) owned by a depository institution that may, at any time, be used to satisfy depositors' claims. It includes United States currency and coin in transit to a Federal Reserve Bank or a correspondent depository institution for which the reporting depository institution has not yet received credit, and United States currency and coin in transit from a Federal Reserve

Bank or a correspondent depository institution when the reporting depository institution's account at the Federal Reserve or correspondent bank has been charged for such shipment.

DISCOUNT WINDOW

Any depository institution holding reservable transaction accounts or nonpersonal time deposits is entitled to the same borrowing privileges as member banks.

In administering the borrowing privileges, the Federal Reserve is to take into consideration the special needs of savings and other depository institutions for access consistent with their long-term asset portfolios and their sensitivity to national money market trends. In general, access is available only after they have fully used reasonable alternative sources of funds. However, the discount window will be available on a temporary basis to cover immediate cash or reserve needs, when institutions are unable to gain timely access to their special industry lenders.

PRICING OF SERVICES

The Monetary Control Act requires the Board to publish for comment a set of pricing principles and a proposed schedule of fees for Federal Reserve Bank services by September 1, 1980. The Board will begin actual pricing of some services in January 1981 and price all services by September 1981.

The following services are covered by the fee schedule:

1. Currency and coin services of a nongovernmental nature.
2. Check-clearing and collection.
3. Wire transfer.
4. Automated clearinghouse.
5. Settlement.
6. Securities safekeeping.
7. Federal Reserve float.
8. Any new service the Federal Reserve System offers, including but not limited to, payment services to effectuate electronic funds transfer.

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