

FEDERAL RESERVE BANK OF DALLAS

DALLAS, TEXAS 75222

Circular No. 80-213

November 6, 1980

TITLE 12 - PART 217 - INTEREST ON DEPOSITS

Fixed Rate Obligations Issued by Bank Holding Companies

TO ALL MEMBER BANKS,  
BANK HOLDING COMPANIES  
AND OTHERS CONCERNED IN THE  
ELEVENTH FEDERAL RESERVE DISTRICT:

The Board of Governors of the Federal Reserve System has issued an interpretation, effective October 17, 1980, providing that fixed rate obligations issued by bank holding companies with a stated maturity of five years or more and with respect to which no more than 5 percent of the original principal amount of the issue may be redeemed in any one year, with a limitation of \$25,000 per investor per year, are not subject to Regulation Q interest rate limitations.

Printed on the following pages is a copy of the Board's material submitted for publication in the Federal Register. These pages more fully explain the Board's action. Any questions concerning the interpretation should be directed to the Consumer Affairs Section of our Bank Supervision and Regulations Department, Ext. 6171.

Sincerely yours,

Robert H. Boykin

First Vice President

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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.

TITLE 12--BANKS AND BANKING

CHAPTER II--FEDERAL RESERVE SYSTEM

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

[Regulation Q, Docket No. R-0329]

Part 217--Interest on Deposits

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Final interpretation.

SUMMARY: This interpretation provides that Regulation Q interest rate limitations do not apply to fixed rate obligations issued by bank holding companies with a stated maturity of five years or more and with respect to which no more than 5 per cent of the original principal amount of the issue may be redeemed in any one year, with a limitation of \$25,000 per investor per year.

EFFECTIVE DATE: October 17, 1980.

FOR FURTHER INFORMATION CONTACT: Gilbert T. Schwartz, Assistant General Counsel (202/452-3623), or Anthony F. Cole, Senior Attorney (202/452-3612), Legal Division, Board of Governors of the Federal Reserve System, Washington, D.C. 20551.

SUPPLEMENTARY INFORMATION: 12 CFR 217 is amended by adding a new section 217.156 to read as follows:

§ 217.156 Application of Regulation Q to fixed rate obligations issued by the parent bank holding company of a member bank.

(a) The Board has received a request for an interpretation that sections 217.1(h) and 217.7(h) of Regulation Q (12 CFR §§ 217.1(h) and 217.7(h)) do not apply to small denomination fixed rate obligations with limited redemption features issued by bank holding companies. The obligations in question generally have a stated maturity of from 10 to 25 years, but are redeemable at the option of the holder subject to limitations as to the amount that any holder may redeem in any year (usually \$25,000) and as to the aggregate amount that may be redeemed in any year (usually 5 per cent of the original principal amount of the issue).

(b) Sections 217.1(h) and 217.7(h) were adopted by the Board effective March 14, 1980, and apply Regulation Q interest rate ceilings to certain obligations issued by a member bank's parent bank holding company. Section 217.1(h) specifically provides that the "deposits" of a member bank includes an obligation that is: (1) issued in a denomination

of less than \$100,000; (2) required to be registered with the SEC; (3) issued or guaranteed in whole or in part by the member bank's parent which is a bank holding company (regardless of the use of the proceeds); and (4) issued with an original maturity or redemption period of four years or less. Section 217.7(h) specifies the ceiling rates of interest payable on such obligations.

Sections 217.1(h) and 217.7(h) were adopted in view of the Board's concern of the potential adverse impact the widespread issuance by bank holding companies of principally floating rate notes with a redemption feature aimed at the retail market was likely to have on deposit flows among depository institutions. The Board's concern was based on its belief that such obligations, which typically are issued at rates substantially in excess of Regulation Q ceiling rates payable on time deposits of comparable maturity, were competitive with consumer deposits issued by depository institutions.

(c) The Board believes that the obligations in question are distinguished from those that were the subject of the Board's principal concerns in two ways. First, they carry a fixed rate of interest; second, the amount that may be redeemed in any year is limited to 5 per cent. The Board regards this limited redemption feature as having an effect similar to a sinking fund which ensures that repayments are not concentrated, while at the same time preserving the long-term nature of the obligation. In view of these considerations, the Board does not believe that such obligations would be a major source of competition for deposits issued by depository institutions.

(d) Accordingly, the Board has determined that obligations issued by a member bank's parent which is a bank holding company will not be regarded as having a redemption period of four years or less under section 217.1(h) and, thus, will not be subject to the interest rate limitations specified in section 217.7(h), if they have the following characteristics: (1) the obligations possess a fixed rate of interest that does not change during the life of the obligation; (2) no more than 5 per cent of the original principal amount of the issue may be redeemed at the option of the holders in any one year; (3) no more than \$25,000 per holder may be redeemed in any one year; and (4) the obligations possess a minimum stated maturity of five years or more. The five year minimum maturity requirement (i.e., 25 per cent higher than the current more than four year requirement) offsets the possible 25 per cent maximum reduction (5 per cent per year for five years) in the amount outstanding after five years and is regarded as necessary to preserve the objective of the four year minimum maturity requirement in section 217.1(h). The Board also believes that in order to ensure that potential purchasers are aware of the limited nature of the redemption feature, those limitations should be prominently disclosed in any materials or solicitations concerning such obligations.

The Board has issued this interpretation based upon its statutory authority under section 19 of the Federal Reserve Act, 12 U.S.C. § 461.

By order of the Board of Governors, October 23, 1980.

(Signed) Theodore E. Allison

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Theodore E. Allison  
Secretary of the Board

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