FEDERAL RESERVE BANK OF DALLAS

DALLAS, TEXAS 75222

Circular No. 81-3
January 8, 1981

TITLE 12 - CHAPTER XII - INTEREST ON DEPOSITS

Proposed Rules Affecting IRA and Keogh Savings Plans, the Effective Date of Ceiling Interest Rates on the 26-Week Money Market Certificate (MMC) and 2 1/2 Year or Longer Small Saver Certificate (SSC), and the Penalty For Early Withdrawal From A Time Deposit in the Event of the Depositor's Bankruptcy; Final Rules Affecting the Penalty For Early Withdrawals From an IRA or Keogh Retirement Time Account and a Plan For Phasing Out Finders Fees.

TO ALL MEMBER BANKS
AND OTHERS CONCERNED IN THE
ELEVENTH FEDERAL RESERVE DISTRICT:

The Depository Institutions Deregulation Committee has requested comment on three proposals and has also adopted two final rules regarding the rate of interest to be paid on deposits at federally insured depository institutions. The changes are summarized as follows:

1. Proposal - The Committee has requested comment on a proposal consisting of five options for changes in rules affecting IRA and Keogh retirement savings plans in order to enable depository institutions to tailor IRA and Keogh plans to the specific needs of individual savers and to market conditions. The following five options are designed to make savings for retirement more attractive:

   (1) Reduce the minimum maturity of the special IRA/Keogh account from three years to one year.
   (2) & (3) Alternative plans for simplifying the handling of, and payment of interest on, periodic routine additions to IRA and Keogh accounts.
   (4) Ceiling rate options for increasing, revising or eliminating ceiling rates on IRA and Keogh accounts; including no ceiling, a fixed ceiling greater than the prevailing 8 percent, or establishment of the floating rate ceiling.
   (5) Creation of the new type of IRA/Keogh time deposit with no ceiling rate or other regulatory restrictions other than the general regulatory limits on time deposits, early withdrawal penalty and the 14-day minimum maturity of notice period.

   The Committee has also proposed that institutions obtain certification from depositors that they are eligible for IRA/Keogh accounts in order to avoid misuse of such accounts. The Committee has asked for comment on these proposals by March 20, 1981, and in addition (see pages 8 and 9 of Docket Number D-0017) particularly requested comment on a number of specific questions.

2. Proposal - The ceiling rates of interest applicable to the 26-week Money Market Certificate (MMC) and the 2 1/2 Year or Longer Small Saver Certificate (SSC) are determined by the yield on 6-month Treasury bills and the average yield for 2 1/2 Treasury securities, respectively. These rates are variable and under current procedures are announced Monday and become effective on Thursday. The Committee proposed to make the effective day Tuesday or Wednesday rather than Thursday. The Committee asked for comments by February 16, 1981, as to which day would be preferable.

3. Proposal - The Committee is considering amending the penalty for early withdrawal of funds from time accounts to permit the funds to be withdrawn without penalty in the event of the bankruptcy of the depositor. This would avoid imposition of a penalty that might otherwise reduce the assets available to pay claims against the debtor's estate. The Committee requested comment on a number of questions regarding this proposal through February 16, 1981.

4. Final Rule - The Committee adopted a rule, effective December 15, 1980, providing that the minimum required penalty for early withdrawal of funds from an IRA or a Keogh plan account within seven days of the establishment of the account may not exceed interest earned to the time of withdrawal. Effective June 2, 1980, the Committee revised the early withdrawal penalty to require an invasion of the principal of the deposit where time deposit funds are withdrawn in the early months after the date of deposit. Internal Revenue Service regulations, however, provide that if specified required disclosure statements are not given to an IRA depositor seven days before the IRA is established, the depositor must be given the right to revoke the IRA within seven days of its establishment. The regulations provide that if the depositor exercises the right of revocation, he or she must be refunded the entire amount of the consideration paid for the IRA. The revision of the rule, as adopted by the Committee, is intended to eliminate the present conflict between the current penalty rule and IRS regulations regarding IRA's.

5. Final Rule - Effective December 31, 1980, the Committee adopted a rule that permits those institutions that have depended heavily on the use of finders fees to attract small denomination (under $100,000) time and savings deposits to phase out the use of such finders fees over the next eighteen months. The rule applies to institutions that can demonstrate that finders fees accounted, on average, for 25 percent or more of their outstanding domestic small-denomination time and savings deposits over the 10-quarter period ending June 30, 1980. The base for the phase out is the amount of domestic small-denomination time and savings deposits outstanding on June 30, 1980, on which finders fees had been paid. The base amount

5. Final Rule - Continued

may not be exceeded during the phaseout period. The maximum amount of small-denomination time and savings deposits that may be raised through the continued use of finders fees is limited to 85 percent of the amount of domestic small-denomination time and savings deposits on which finders fees had been paid maturing in the semi-annual period ending June 30, 1981, and 60 percent and 40 percent of the amount of such deposits maturing in the semi-annual periods ending December 31, 1981 and June 30, 1982, respectively.

Enclosed are copies of a press release and Federal Register notices which should be kept by member banks in the Regulation Q section of their Regulations binders. Questions concerning the actions taken should be directed to the Consumer Affairs section of the Bank Supervision and Regulations Department, extension 6169.

Sincerely yours,

William H. Wallace

First Vice President

Enclosures

DEPOSITORY INSTITUTIONS DEREGULATION COMMITTEE PRESS RELEASE

COMPTROLLER OF THE CURRENCY | FEDERAL DEPOSIT INSURANCE CORPORATION | FEDERAL HOME LOAN BANK BOARD
FEDERAL RESERVE BOARD | NATIONAL CREDIT UNION ADMINISTRATION | TREASURY DEPARTMENT

For immediate release December 19, 1980

The Depository Institutions Deregulation Committee[1/] today requested comment on three proposals, one consisting of five options for changes in rules affecting IRA and Keogh retirement savings plans, another concerning the effective dates of ceiling interest rates on variable rate time deposits and the third a suggestion for limiting the penalty for early withdrawal from a time deposit in the event the depositor becomes bankrupt.

The Committee has also adopted two final rules, one modifying the penalty for early withdrawals from an IRA or Keogh retirement time account within seven days of establishing the account and the other a plan for phasing out fees paid to finders of time deposits.

The Committee's official notices of its actions, and background information concerning them, are attached. A summary of the Committee's proposals, and of the final rules adopted, follows.

Proposals

1. IRA[2/] and Keogh[3/] accounts: (Attachment A)

To enable depository institutions to tailor IRA and Keogh retirement savings plans to the specific needs of individual savers

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1/ Established by the Depository Institutions Deregulation and Monetary Control Act of 1980, to phase out interest rate ceilings on time and savings deposits over the next six years. The members of the Committee are the heads of the agencies listed on this page.

2/ IRA -- Individual Retirement Account -- plans were authorized by the Employee Retirement Security Act of 1974 (ERISA) permitting individuals not covered by a retirement plan to deposit funds on a tax deferred basis in an IRA.

3/ Keogh (H.R. 10) plan accounts were authorized by the Self-Employed Individuals Tax Retirement Act of 1962, permitting self-employed persons to establish their own pension fund through tax deferred deposits in a special retirement account.

and to market conditions, and to carry out the aim of the Congress to encourage individual savings for retirement, the Committee requested comment on the following five options designed to make savings for retirement more attractive:

1. Reduce the minimum maturity of the special IRA/Keogh account from three years to one year (Page 4 of Attachment A for details).

2. and 3. Alternative plans for simplifying the handling of, and payment of interest on, periodic routine additions to IRA and Keogh accounts (Pages 5 and 6 of Attachment A).

4. Ceiling rate options for increasing, revising or eliminating ceiling rates on IRA and Keogh accounts, including no ceiling, a fixed ceiling greater than the prevailing 8 percent, or establishment of a floating rate ceiling (Page 7 of Attachment A).

5. Creation of a new type of IRA/Keogh time deposit with no ceiling rate or other regulatory restrictions other than the general regulatory limits on time deposits, early withdrawal penalty and the 14-day minimum maturity of notice period.

In addition, to avoid misuse of IRA/Keogh accounts, the Committee proposed that institutions obtain certification from depositors that they are eligible for such accounts.

In making these proposals, the Committee said:

> The Committee believes that the proposals presented would...encourage savings and, by enhancing the competitive posture of depository institutions vis-a-vis nondepository institutions, would enable depository institutions to function more safely and soundly in increasingly competitive financial markets.

The Committee asked for comment on all these options, or on any other feature of its proposals, and in addition (Pages 8 and 9 of Attachment A) particularly requested comment on a number of specific questions.

The Committee asked for comment on these proposals by March 20, 1981.

2. The effective date for ceiling rates on Money Market Certificates and Small Savers Certificates. (Attachment B)

The ceiling rates of interest applicable to the 26-week Money Market Certificate (MMC) and the 2 1/2 year or longer Small Saver Certificate (SSC) are determined by the yield on six-month Treasury bills and the average yield for 2 1/2 year Treasury securities. Under current procedures these rates are announced Monday and become effective on Thursday.

In order to link the ceiling rates payable on MMCs and SSCs more closely to market rates, the Committee proposed to make the effective day Tuesday or Wednesday, rather than Thursday.

The Committee requested comment as to which day would be preferable, taking into account the time needed by institutions to make changes to implement new rates and problems institutions may encounter in obtaining new ceiling rate information and making it known to the public.

The Committee asked for comment on this proposal by February 16, 1981.

3. Early withdrawal of time deposit funds in the event of bankruptcy (Attachment C)

The Committee is considering amending the penalty for early withdrawal of funds from time accounts to permit the funds to be withdrawn without penalty in the event of the bankruptcy of the depositor.

This would avoid imposition of a penalty that might otherwise reduce the assets available to pay claims against the debtor's estate.

The Committee requested comment on a number of questions regarding this proposal, on Page 3 of Attachment C.

The Committee will receive comment on the proposal through February 16, 1981.

Final Rules

1. The Committee adopted a rule, effective December 15, 1980, providing that the minimum required penalty for early withdrawal of funds from an IRA or a Keogh plan account within seven days of establishment of the account may not exceed interest earned to the time of withdrawal.

The early withdrawal penalty rule before this revision required an invasion of the principal of the deposit for such a withdrawal.

Revision of the rule, as explained in Attachment D, makes it parallel to regulations of the Internal Revenue Service.

2. Effective December 31, 1980, the Committee adopted a rule that permits those institutions that have depended heavily on the use of finder's fees to attract small denomination (under $100,000) time and savings deposits to phase out the use of such finder's fees over the next 18 months.

Details of the plan are given in Attachment E.

The Committee will meet again in March to consider an agenda that will be announced later.

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DEPOSITORY INSTITUTIONS DEREGULATION COMMITTEE

[12 CFR Part 1204]

(Docket No. D-0017)

Notice of Proposed Rulemaking

Retirement Accounts

AGENCY: Depository Institutions Deregulation Committee.

ACTION: Proposed rulemaking.

SUMMARY: The Depository Institutions Deregulation Committee ("Committee") is considering proposed rules that would: (1) enable time deposits held in Individual Retirement Accounts ("IRAs") and Keogh (H.R. 10) plans to accommodate routine additions more conveniently; (2) reduce the three-year maturity of the special IRA/Keogh deposit category to one year; (3) increase, revise, or eliminate the current 8 per cent ceiling rate of interest payable on the special IRA/Keogh deposit category; and (4) create a new IRA/Keogh time deposit with a minimum required maturity of 14 days and no prescribed ceiling rate of interest. The proposed rules would facilitate the use of time deposits for retirement savings and encourage the increased use of IRA/Keogh plans consistent with the intent of Congress in the Employee Retirement Income Security Act of 1974 to encourage individuals to save for their retirement.

DATES: Comments must be received by March 20, 1981.

ADDRESS: Interested parties are invited to submit written data, views, or arguments regarding the proposed rules to Normand R. V. Bernard, Federal Reserve Building, 20th Street and Constitution Avenue, N.W., Washington, D.C. 20551. All material submitted should include the Docket Number D-0017. Such material will be made available for inspection and copying upon request except as provided in Section 1202.5 of the Committee's Rules Regarding Availability of Information (12 CFR § 1202.5).

FOR FURTHER INFORMATION CONTACT: John Harry Jorgenson, Attorney, Board of Governors of the Federal Reserve System (202/452-3778), F. Douglas Birdzell, Counsel, Federal Deposit Insurance Corporation (202/389-4261), Allan Schott, Attorney-Advisor, Department of Treasury (202/566-6798), Rebecca Laird, Senior Associate General Counsel, Federal Home Loan Bank Board (202/377-6446), Debra A. Chong, Attorney, Office of the Comptroller of the Currency (202/447-1632), or Anthony F. Cole, Deputy General Counsel, Depository Institutions Deregulation Committee (202/452-3612).

SUPPLEMENTARY INFORMATION: Although the intent of the Employee Retirement Income Security Act of 1974 ("ERISA") is to encourage qualified individuals to develop their own pension plans, IRAs and Keoghs have not been fully utilized. In 1977, only 3.3 per cent of eligible taxpayers in the $11,000 to $15,000 income class held some form of retirement account in a depository or nondepository institution, while 52.4 per cent of those with incomes of $50,000 or more held some form of retirement account. (Latest available data.) In view of the Congressional intent to encourage individuals to save for their retirement, the Committee is considering regulatory actions that would increase the attractiveness of IRA/Keogh accounts at depository institutions by reducing present administrative obstacles to periodic additions to IRA/Keogh time deposits and by increasing the yield available to retirement savers.

The current regulations of the Board of Governors of the Federal Reserve System ("Federal Reserve"), the Federal Deposit Insurance Corporation ("FDIC"), and the Federal Home Loan Bank Board ("FHLBB"), provide that IRA/Keogh funds may be invested in a regular savings account or in any time deposit category including the special three-year, 8 per cent IRA/Keogh account. The interest rate ceilings on time deposits held in IRAs or Keoghs are the same as on nonretirement accounts, except that there is no differential in the rates that banks and thrifts may pay on IRA/Keogh funds invested in the 26-week money market certificate, in the 2½ year or longer small saver certificate, or the special three-year IRA/Keogh deposit category.

The agencies' regulations governing account additions, however, are not uniform and complicate the use of time deposits, particularly variable ceiling time deposits, for periodic deposits to IRAs or Keoghs. Under Federal Reserve and FDIC rules, each addition to a time deposit is regarded either as having a separate and distinct maturity equal to the originally agreed upon maturity or as resetting the maturity of the entire account. Federal Reserve and FDIC regulations also require that the rate of interest paid on an addition to any existing time deposit not exceed the applicable ceiling rate on the date the additional deposit is made. This makes it impractical to use variable ceiling rate accounts to make routine additions to IRA/Keogh accounts. Under FHLBB rules, a fixed ceiling time deposit may be structured to provide for routine periodic additions. Each time an addition is made, however, the maturity of the entire account is reset for a period equal to the term of the original account. No additions to variable ceiling accounts are permitted.

The Committee requests comment on five options designed to reduce the administrative complexities associated with IRA/Keogh time deposits and to provide a more attractive yield to retirement savers. Option 1 reduces the minimum maturity of the existing special three-year IRA/Keogh account to one year. Options 2 and 3 provide for the creation of a new IRA/Keogh one-year notice account that would facilitate the receipt of periodic deposits. Option 4 presents three alternative

ceiling rate options that could be applied to the currently authorized special three-year account, the one-year account described in Option 1, or the notice accounts presented in Options 2 and 3. Option 5 provides for the creation of a new 14-day IRA/Keogh time deposit with no prescribed ceiling rate of interest. A discussion of the five options follows.

Option 1 -- Reduce IRA/Keogh Account Maturity to One Year

When the existing special three-year IRA/Keogh account was established in 1977, the minimum maturity of the account coincided with the ERISA provisions permitting the tax penalty-free rollover of IRA funds from one trustee to another once every three years. Tax penalty-free IRA rollovers, however, are now permitted once a year. In order to keep the maturity of the special IRA/Keogh account consistent with tax law, the Committee proposes to reduce the minimum maturity of the special three-year IRA/Keogh account to one year.

Reducing the maturity to one year, if accompanied by a significant increase in or elimination of the 8 per cent ceiling rate on the special IRA/Keogh account, would provide depository institutions with greater flexibility in designing and marketing retirement savings programs. However, reducing the maturity of the account may contribute to a reduction in depository institution account stability, if depositors make use of their annual reinvestment privileges to rollover their existing IRA/Keogh accounts into tax qualified retirement plans at other institutions.

Options 2 and 3 -- Create IRA/Keogh Notice Account to Facilitate Periodic Deposits

Option 1 is modest in scope, adjusting the maturity of IRA/Keogh time deposits to accommodate an earlier change in ERISA; it does not solve the problems associated with routine periodic additions under current regulations. Consequently, to reduce administrative complexities, the Committee is considering establishing an IRA/Keogh notice account that would facilitate the receipt of periodic additions. Options 2 and 3 present alternative methods for structuring this account. A notice account is an account from which funds may not be withdrawn prior to the expiration of a period of notice which must be given by the depositor a specified number of days in advance of withdrawal. Notice could take a variety of forms including a specific written notice from the depositor or arrangements in which notice is given automatically on the anniversary of the account or each time a deposit is made.

Under Option 2:

(a) A one-year notice of intent to withdraw on a specified date is required;

(b) The institution may accept regular additions to the account at any time up to 14 days before the expiration or end of the notice period, and all funds on deposit could be withdrawn upon the expiration of the notice period;

(c) Interest could be paid on all additions to the account at the specified contract rate; and

(d) An early withdrawal penalty would be imposed on withdrawals made prior to the expiration of the one-year notice period.

Under Option 3:

(a) A one-year notice of intent to withdraw on a specified date is required;

(b) The institution may accept regular additions to the account at any time, but the amount withdrawn could not exceed the amount on deposit at the time of notice;

(c) Interest could be paid on all additions to the account at the specified contract rate; and

(d) An early withdrawal penalty would be imposed on withdrawals made prior to the expiration of the one-year notice period.

A strength of these options is that they establish IRA/Keogh accounts that readily accommodate routine periodic additions and can easily be understood by both account holders and the institutions authorized to offer the accounts. Under both Options 2 and 3 the one-year notice required for withdrawal accommodates IRA depositors' annual rollover privilege as provided by the amended ERISA; it also facilitates depositor shifting to more attractive retirement investment alternatives when they exist, as contemplated by the recent amendment to ERISA. The Committee believes that structuring either account as a one-year notice account is preferable to establishing an account with a stated maturity of one year that could accept periodic deposits. A notice account would tend to lessen deposit volatility since funds would not mature automatically at the end of a year.

Option 2 would make the administration of the notice account less complex since all funds on deposit could be withdrawn at one time. Under Option 2, however, depository institutions may be concerned that even after notice is given depositors would be able to earn interest at the contract rate on funds on deposit for as little as 14 days.

Option 4 -- Increase, Revise, or Eliminate IRA/Keogh Interest Rate Ceiling

Options 2 and 3 deal primarily with the administrative problems of making routine additions to IRA/Keogh accounts, but do not address the issue of what deposit rate ceilings, if any, should be applied. The Committee is considering the following ceiling rate options that could be applied to the currently authorized special three-year account, the one-year account described in Option 1, or the notice accounts presented in Options 2 and 3.

(a) Prescribe no ceiling rate of interest;

(b) Establish a fixed ceiling at a rate greater than 8 per cent. Within the ceiling rate limitations, an institution could change the rate paid on the account with one year's notice or change the rate immediately if required by a regulatory ceiling rate change; or

(c) Establish a floating ceiling indexed to the rate on U.S. Government securities of specified maturity (e.g., 91 day, 182 day, one year, or two and a half year Treasury security yield). Changes in the ceiling rate could occur quarterly, semi-annually, or annually.

Option 5 -- Create 14-Day IRA/Keogh Time Deposit

The Committee also is considering establishment of an IRA/Keogh plan time deposit with a minimum required maturity or notice period of 14 days. No ceiling rate of interest payable on this special category would be prescribed. This option would provide maximum flexibility to depository institutions in structuring retirement accounts. Under this option, an institution could choose any maturity (so long as the 14-day minimum maturity requirement is satisfied) or rate (for example, fixed or floating) for the deposit.

The Committee believes that the proposals presented would enable depository institutions to tailor IRA/Keogh plans to specific saver needs and market circumstances and thereby attract and retain relatively stable retirement funds. In addition, these proposals would encourage savings and, by enhancing the competitive posture of depository institutions vis-a-vis nondepository institutions, would enable depository institutions to function more safely and soundly in increasingly competitive financial markets. The Committee is concerned, however, that adoption of any of the proposals making IRA/Keogh accounts significantly more attractive could encourage depositors not qualified to open IRA/Keogh

accounts to open such accounts. To lessen the potential for abuse, the Committee is considering adoption of a provision requiring an appropriate official of the depository institution to obtain certification from each depositor that he or she qualifies to hold an IRA/Keogh account. Such certification for IRAs might include presentation of a W-2 form indicating eligibility.

To aid in its consideration, the Committee requests comment on the five options discussed above. Specific comments also are requested on:

(1) The minimum required early withdrawal penalty that should be imposed on withdrawals prior to the receipt and expiration of the one-year notice period under Option 2 and 3;

(2) The minimum required early withdrawal penalty that should be imposed on premature withdrawals under Option 5;

(3) The potential for misuse of IRA/Keogh accounts under any of the options and steps that might be taken to lessen the potential for misuse;

(4) The ceiling rate options (e.g., no ceiling, fixed rate ceiling, or floating ceiling) that would be most attractive to depository institutions and their customers;

(5) The Treasury bill security that should be selected as the index if a floating rate ceiling is adopted (Option 4c) and the frequency of change in the ceiling rate (e.g., quarterly, semi-annually, annually);

(6) The potential impact of the proposals on deposit stability at depository institutions;

(7) The effect of the proposals on the earnings of depository institutions;

(8) Whether, in the event any of the options is adopted, institutions should be authorized to permit existing IRA/Keogh depositors to immediately convert their accounts without imposition of the early withdrawal penalty; and

(9) Any other proposals that would reduce the administrative complexities of using time deposits to fund IRAs and Keoghs.

By order of the Committee, December 18, 1980.

(Signed) Normand R. V. Bernard

Normand R. V. Bernard
Executive Secretary of the Committee

[SEAL]

DEPOSITORY INSTITUTIONS DEREGULATION COMMITTEE

[12 CFR Part 1204]

(Docket No. D-0016)

Notice of Proposed Rulemaking

Effective Date of Ceiling Rates on MMCs and SSCs

AGENCY: Depository Institutions Deregulation Committee.

ACTION: Proposed rulemaking.

SUMMARY: The Depository Institutions Deregulation Committee ("Committee") proposes to adopt rules reducing the period between the announcement and the effective date of the ceiling rates of interest payable on the 26-week money market certificate (MMC) and on the 2-1/2 year and longer small saver certificate (SSC). Under the current rules, the ceiling rates of interest payable on MMCs and SSCs are announced on Monday and are effective the following Thursday. Under the proposed rules, the ceiling rates of interest announced on Monday would become effective on the following Tuesday or, as an alternative, Wednesday.

DATES: Comments must be received by February 16, 1981.

ADDRESS: Interested parties are invited to submit written data, views, or arguments regarding the proposed rules to Normand R. V. Bernard, Executive Secretary, Depository Institutions Deregulation Committee, Federal Reserve Building, 20th Street and Constitution Avenue, N.W., Washington, D.C. 20551. All material submitted should include the Docket Number D-0016. Such material will be made available for inspection and copying upon request except as provided in Section 1202.5 of the Committee's Rules Regarding Availability of Information (12 CFR § 1202.5).

FOR FURTHER INFORMATION CONTACT: F. Douglas Birdzell, Counsel, Federal Deposit Insurance Corporation (202/389-4261), John Harry Jorgenson, Attorney, Board of Governors of the Federal Reserve System (202/452-3778), Allan Schott, Attorney-Advisor, Treasury Department (202/566-6798), Rebecca Laird, Senior Associate General Counsel, Federal Home Loan Bank Board (202/377-6446), Debra A. Chong, Attorney, Office of the Comptroller of the Currency (202/447-1632), or Anthony F. Cole, Deputy General Counsel, Depository Institutions Deregulation Committee (202/452-3612).

SUPPLEMENTARY INFORMATION: The ceiling rate of interest payable on MMCs is tied to the discount yield (auction average) on the most recently issued six-month United States Treasury bills. United States Treasury bills maturing in six months normally are auctioned on Monday and, under

current rules, the ceiling rate of interest based on the discount yield (auction average) is effective the following Thursday, the day on which the Treasury bills are issued. This ceiling rate is effective until the next issuance of six-month United States Treasury bills. The ceiling rate of interest payable on SSCs is tied to the average 2-1/2 year yield for United States Treasury securities as determined bi-weekly by the United States Treasury. The average 2-1/2 year yield on United States Treasury securities is announced by Treasury on Monday afternoon (based on the average 2-1/2 year yield for the five business days ending on Monday) and, under current rules, the ceiling rates based on that average 2-1/2 year yield are effective for a two-week period beginning on the following Thursday.

In order to more closely link the ceiling rates of interest payable on MMCs and SSCs with current market rates, the Committee proposes to adopt rules reducing the time between the announcement and effective date of the ceiling rates. Under the proposed rules, the ceiling rates announced on Monday would be effective for new MMCs or SSCs issued on the following Tuesday or Wednesday rather than on the following Thursday. Comment is requested on whether a Tuesday or, as an alternative, a Wednesday effective date would allow sufficient time for institutions to make any changes necessary for implementation of the new ceiling rates. Comment is particularly requested on potential problems that institutions may encounter in (1) obtaining information on the new ceiling and (2) posting or advertising the new ceiling rate.

By order of the Committee, December 18, 1980.

(Signed) Normand R. V. Bernard

Normand R. V. Bernard
Executive Secretary of the Committee

[SEAL]

DEPOSITORY INSTITUTIONS DEREGULATION COMMITTEE

[12 CFR Part 1204]

(Docket No. D-0015]

Notice of Proposed Rulemaking

Penalty for Early Withdrawals of Time Deposit Funds in the Event of Bankruptcy

AGENCY: Depository Institutions Deregulation Committee.

ACTION: Proposed rulemaking.

SUMMARY: The Depository Institutions Deregulation Committee ("Committee") is considering amending the penalty for early withdrawals of time deposit funds to permit penalty-free withdrawal in the event of bankruptcy of the depositor.

DATES: Comments must be received by February 16, 1981.

ADDRESS: Interested parties are invited to submit written data, views, or arguments regarding the proposed rule to Normand R. V. Bernard, Executive Secretary, Depository Institutions Deregulation Committee, Federal Reserve Building, 20th Street and Constitution Avenue, N.W., Washington, D.C. 20551. All material submitted should include the Docket Number D-0015. Such material will be made available for inspection and copying upon request except as provided in Section 1202.5 of the Committee's Rules Regarding Availability of Information (12 CFR § 1202.5).

FOR FURTHER INFORMATION CONTACT: F. Douglas Birdzell, Counsel, Federal Deposit Insurance Corporation (202/389-4261), John Harry Jorgenson, Attorney, Board of Governors of the Federal Reserve System (202/452-3778), Allan Schott, Attorney-Advisor, Treasury Department (202/566-6798), Rebecca Laird, Senior Associate General Counsel, Federal Home Loan Bank Board (202/377-6446) Debra A. Chong, Attorney, Office of the Comptroller of the Currency (202/447-1632), or Anthony F. Cole, Deputy General Counsel, Depository Institutions Deregulation Committee (202/452-3612).

SUPPLEMENTARY INFORMATION: The Committee is considering amending the early withdrawal penalty rule to authorize depository institutions to permit penalty-free early withdrawals of time deposit funds in the event of the bankruptcy of the depositor. Under current rules, federally insured commercial banks, mutual savings banks, and savings and loan associations are required, with certain exceptions, to impose a penalty upon the withdrawal of time deposit funds prior to maturity. The minimum required penalty generally is an amount equal to three months' simple

interest on the funds withdrawn where the original maturity of the time deposit is three months to one year, and an amount equal to six months' simple interest on the funds withdrawn where the original maturity of the time deposit is more than one year. With respect to time deposits with an original maturity of less than three months, the minimum required penalty for early withdrawal is a forfeiture of an amount equal to the amount of simple interest that could have been earned on the funds withdrawn if the funds had remained on deposit until maturity. (12 CFR § 1204.103).

Imposition of the early withdrawal penalty when funds are withdrawn in the event of bankruptcy may reduce the assets available to pay the claims against the debtor's estate. The Committee believes that adoption of a bankruptcy exception would not significantly increase the administrative burden of the penalty since the exception, as in the case of the current exceptions providing for penalty-free withdrawals in the event of death, incompetence and where an IRA/Keogh depositor is 59½ or disabled, would be subject to well-defined criteria.

Specific comment is requested on whether such an exception, if adopted, should:

(1) apply to corporations as well as to individuals with regular incomes and small sole proprietors;

(2) apply to liquidations (Chapter 7), municipal debt adjustments (Chapter 9), rehabilitations and reorganizations (Chapter 11) and, in the case of individuals, extended repayment plans (Chapter 13) under the bankruptcy code;*

(3) permit penalty-free withdrawals to be made upon the filing of a petition for bankruptcy or only upon an adjudication of bankruptcy or a court ordered distribution of the debtor's estate; and

(4) permit penalty-free withdrawals to be made by a debtor-in-possession as well as by a trustee in bankruptcy.

By order of the Committee, December 18, 1980.

(Signed) Normand R. V. Bernard

Normand R. V. Bernard
Executive Secretary of the Committee

[SEAL]

*Chapter references are to Title II of the United States Code entitled "Bankruptcy."

TITLE 12--BANKS AND BANKING

CHAPTER XII--DEPOSITORY INSTITUTIONS DEREGULATION COMMITTEE

[Docket No. D-0014]

Part 1204--INTEREST ON DEPOSITS

Penalty for Early Withdrawals of IRA/Keogh Time Deposit Funds

AGENCY: Depository Institutions Deregulation Committee.

ACTION: Final rule.

SUMMARY: The Depository Institutions Deregulation Committee ("Committee") has adopted a rule providing that where a time deposit held in an Individual Retirement Account ("IRA") or Keogh (H.R. 10) plan is paid before maturity within seven days of the establishment of the IRA or Keogh plan, the minimum required early withdrawal penalty is the forfeiture only of the interest earned on the time deposit.

EFFECTIVE DATE: December 15, 1980.

FOR FURTHER INFORMATION CONTACT: Debra A. Chong, Attorney, Office of the Comptroller of the Currency (202/447-1632), F. Douglas Birdzell, Counsel, Federal Deposit Insurance Corporation (202/389-4261), Daniel L. Rhoads, Attorney, Board of Governors of the Federal Reserve System (202/452-3711), Rebecca Laird, Senior Associate General Counsel, Federal Home Loan Bank Board (202/377-6446), Allan Schott, Attorney-Advisor, Treasury Department (202/566-6798), or Anthony F. Cole, Deputy General Counsel, Depository Institutions Deregulation Committee (202/452-3612).

SUPPLEMENTARY INFORMATION: Effective June 2, 1980, the Committee revised the penalty required to be imposed by depository institutions (federally insured commercial banks, mutual savings banks, and savings and loan associations) on withdrawals of time deposit funds prior to maturity (12 CFR § 1204.103, 45 Fed. Reg. 37801). Under the revised rule, where a time deposit with an original maturity of less than three months, or any portion thereof, is paid before maturity, the minimum required penalty is a forfeiture of an amount equal to the amount of interest that could have been earned on the funds withdrawn at the nominal rate of interest being paid on the deposit had the funds remained on deposit until maturity. Where funds are withdrawn prior to maturity from a time deposit with an original maturity of three months to one year or from a time deposit with an original maturity of more than one year, the minimum required penalty is, respectively, a forfeiture of an amount

at least equal to three months or six months of interest earned, or that could have been earned, on the funds withdrawn at the nominal rate of interest being paid on the deposit regardless of the length of time the funds withdrawn have remained on deposit.

Questions have been raised by a number of depository institutions concerning a conflict between the penalty rule and Internal Revenue Service ("IRS") regulations regarding IRAs. The penalty rule requires a reduction or invasion of principal where time deposit funds are withdrawn in the early months after the date of deposit. IRS regulations, however, provide that if specified required disclosure statements are not given to an IRA depositor seven days before the IRA is established, the depositor must be given the right to revoke the IRA within seven days of its establishment. The regulations further provide that if the depositor exercises the right of revocation, he or she must be refunded the entire amount of the consideration paid for the IRA (26 CFR §§ 1.408-1(d)(4)(ii)(A)(1) and (2) and (iii)(B)(14)).

Many depository institutions provide the required disclosure statement to depositors at the time the IRA is initially established and the funds are invested in a time deposit. In such circumstances, if the depositor subsequently decides to revoke the IRA within seven days and withdraw the time deposit funds, the institution is required under the current early withdrawal penalty rule to impose a penalty that will result in a forfeiture of principal. Invading principal, however, conflicts with the IRS provisions requiring that a depositor be refunded the entire amount of the consideration paid for the account under such circumstances. Although there is no conflict if the depository institution provides the disclosure statement seven days before the IRA is opened, for reasons of customer and administrative convenience many institutions choose to provide the disclosure simultaneously with the opening of the account.

In order to facilitate the administration and offering of retirement accounts, the Committee has adopted a rule eliminating the conflict between the current penalty rule and IRS regulations regarding IRAs. Although the conflicting IRS provisions do not apply to Keogh (H.R. 10) plans, in the interest of administrative simplicity, the rule also will apply to Keogh (H.R. 10) plans. Under this rule, where a time deposit held in an IRA or Keogh (H.R. 10) plan is withdrawn before maturity within seven days of the establishment of the IRA or Keogh, the minimum required early withdrawal penalty is the forfeiture of the interest earned on the time deposit, and no invasion of principal is required as under the current rule. Early withdrawals of IRA or Keogh time deposits made more than seven days after the opening of the IRA or Keogh will continue to be subject to the current early withdrawal penalty rule.

This action was taken by the Committee in view of the adverse effect on depository institutions and retirement savers occasioned by the conflict between the early withdrawal penalty rule and IRS regulations. In view of these considerations, and because this amendment relieves a restriction, the Committee finds that application of the notice and public participation provisions of 5 U.S.C. § 553 to this action would be contrary to the public interest and that good cause exists for making this action effective in less than 30 days.

Pursuant to its authority under Title II of Public Law 96-221, 94 Stat. 142 (12 U.S.C. §§ 3501 et seq.), to prescribe rules governing the payment of interest and dividends on deposits of federally insured commercial banks, savings and loan associations, and mutual savings banks, effective December 15, 1980, the Committee amends Part 1204 (Interest on Deposits) by adding section 113 as follows:

PART 1204--INTEREST ON DEPOSITS

* * * * *

§ 1204.113 -- Early Withdrawal of IRA and Keogh (H.R. 10) Plan Time Deposits.

Notwithstanding the provisions of 12 C.F.R. § 1204.103, where a time deposit, or any portion thereof, held in an Individual Retirement Account established in accordance with 26 U.S.C. § 408 is paid before maturity within seven days after the establishment of the Individual Retirement Account pursuant to the provisions of 26 CFR § 1.408-(1)(d)(4), or where a time deposit, or any portion thereof, held in a Keogh (H.R. 10) plan established in accordance with 26 U.S.C. § 401 is paid before maturity within seven days after the establishment of the Keogh (H.R. 10) plan, a depositor shall forfeit an amount at least equal to the interest earned on the amount withdrawn at the nominal (simple interest) rate being paid on the deposit.

By order of the Committee, December 18, 1980.

(Signed) Normand R. V. Bernard

Normand R. V. Bernard
Executive Secretary of the Committee

[SEAL]

TITLE 12--BANKS AND BANKING

CHAPTER XII--DEPOSITORY INSTITUTIONS DEREGULATION COMMITTEE

[Docket No. D-0012]

PART 1204--INTEREST ON DEPOSITS

Phaseout of Finders Fees

AGENCY: Depository Institutions Deregulation Committee.

ACTION: Final rule.

SUMMARY: The Depository Institutions Deregulation Committee ("Committee") has adopted a final rule permitting a phaseout of finders fee programs over an 18-month period for those depository institutions that can demonstrate that finders fees accounted, on average, for 25 per cent or more of their outstanding domestic small-denomination time and savings deposits over the ten-quarter period ending June 30, 1980. The base for the phaseout is the amount of domestic small-denomination time and savings deposits outstanding on June 30, 1980, on which finders fees had been paid. This base amount may not be exceeded during the phaseout period. The maximum amount of small-denomination time and savings deposits that may be raised through the continued use of finders fees is limited to 85 per cent of the amount of domestic small-denomination time and savings deposits on which finders fees had been paid maturing in the semi-annual period ending June 30, 1981, and 60 per cent and 40 per cent of the amount of such deposits maturing in the semi-annual periods ending December 31, 1981 and June 30, 1982, respectively.

EFFECTIVE DATE: December 31, 1980.

FOR FURTHER INFORMATION CONTACT: Debra A. Chong, Attorney, Office of the Comptroller of the Currency (202/447-1632), F. Douglas Birdzell, Counsel, Federal Deposit Insurance Corporation (202/389-4261), Daniel L. Rhoads, Attorney, Board of Governors of the Federal Reserve System (202/452-3711), Allan Schott, Attorney-Advisor, Treasury Department (202/566-6798), Rebecca Laird, Senior Associate General Counsel, Federal Home Loan Bank Board (202/377-6446), or Anthony F. Cole, Deputy General Counsel, Depository Institutions Deregulation Committee (202/452-3612).

SUPPLEMENTARY INFORMATION: At its September 9 meeting, the Committee adopted a rule, effective December 31, 1980, defining finders fees (fees paid to a person who introduces a depositor to an institution) as a payment of interest to the depositor for purposes of determining compliance with interest-rate ceilings limitations (45 F.R. 68641). This action was taken in view of the increased use of finders fees and the consideration that finders fees, in some cases, may be used to circumvent interest

rate ceilings. In taking this action, the Committee was aware that some institutions may have relied extensively on the use of finders fees to attract or retain deposits and that immediate application of the rule on December 31, 1980, could cause hardship for such institutions. Accordingly, the Committee requested public comment on a proposal to provide a two-year phaseout of finders fee programs for those institutions that could demonstrate that finders fees had accounted, on average, for 25 per cent or more of their outstanding domestic small-denomination time and savings deposits over the ten-quarter period ending June 30, 1980.

After consideration of the more than 80 comments received on the proposal (73 opposed, 5 in favor), the Committee has adopted a final rule permitting a phaseout of finders fee programs over an 18-month period for those institutions that can demonstrate that finders fees accounted, on average, for 25 per cent or more of their outstanding domestic small-denomination time and savings deposits over the ten-quarter period ending June 30, 1980. The base for the phaseout is the amount of domestic small-denomination time and savings deposits outstanding on June 30, 1980, on which finders fees had been paid. This base amount may not be exceeded during the phaseout period. The maximum amount of small-denomination time and savings deposits that may be raised through the continued use of finders fees is limited to 85 per cent of the amount of domestic small-denomination time and savings deposits on which finders fees had been paid maturing in the semi-annual period ending June 30, 1981, 60 per cent of the amount of such deposits maturing in the semi-annual period ending December 31, 1981, and 40 per cent of the amount of such deposits maturing in the semi-annual period ending June 30, 1982. Any maturing domestic small-denomination time deposit on which a finders fee had been paid and that is renewed, whether or not a finders fee is paid upon renewal, must be included in the amount of deposits obtained through the use of finders fees for purposes of determining compliance with the above percentage limitations.

Under the rule, an institution will be required to obtain advance certification from its primary federal supervisor that it satisfies the eligibility criteria necessary to qualify for the phaseout. In addition, all finders fees must be paid in cash, except that an institution may utilize as finders fees any merchandise it owned on December 1, 1980. In order to minimize any potential adverse effect on competing depository institutions during the phaseout of finders fees, a qualifying institution will not be permitted to advertise the continued availability of finders fees by television, radio, or other mass media of general circulation (such as newspapers and magazines). However, direct contact with depositors or former sponsors of depositors or display or distribution of promotional materials in an institution's offices will be permitted.

Pursuant to its authority under Title II of Public Law 96-221, 94 Stat. 142 (12 U.S.C. § 3501 et seq.), to prescribe rules governing the payment of interest and dividends on deposits of federally insured commercial banks, savings and loan associations, and mutual savings banks, effective December 31, 1980, the Committee amends Part 1204 (Interest on Deposits) by adding section 114 as follows:

PART 1204 -- INTEREST ON DEPOSITS

* * * * *

§ 1204.114 -- Phaseout of Finders Fees

(a) Notwithstanding the provisions of 12 CFR § 1204.110, during the period from December 31, 1980 through June 30, 1982 (the "phaseout period"), any fee paid by a qualifying depository institution to a person who introduces a depositor to the institution (a "finders fee") shall not be regarded as a payment of interest to the depositor for purposes of determining compliance with interest rate ceilings, if the institution complies with all of the requirements set forth in subsection (b). For purposes of this section, a qualifying depository institution is a depository institution that has been certified by its primary federal supervisor to have demonstrated that finders fees have accounted for 25 per cent or more of its outstanding domestic small-denomination (under $100,000) time and savings deposits, on average, over the ten-calendar quarter period ending June 30, 1980.

(b) A qualifying depository institution must comply with all of the following requirements to be eligible for the phaseout granted under subsection (a) of this section:

(1) During the phaseout period, the maximum amount of small-denomination (under $100,000) time and savings deposits that may be raised through the use of finders fees may not exceed 85 per cent of the amount of domestic small-denomination (under $100,000) time and savings deposits on which finders fees had been paid that mature in the semi-annual period ending June 30, 1981, 60 per cent of the amount of such deposits that mature in the semi-annual period ending December 31, 1981, and 40 per cent of the amount of such deposits that mature in the semi-annual period ending June 30, 1982. Provided, however, that during the phaseout period, the amount of small-denomination (under $100,000) time and savings deposits on which finders fees are paid may not exceed the amount of domestic small-denomination (under $100,000) time and savings deposits outstanding on June 30, 1980 on which finders fees had been paid.

(2) Any maturing domestic small-denomination (under $100,000) deposit on which a finders fee had been paid and that is renewed, whether automatically or otherwise, whether or not a finders fee is

paid upon renewal, must be included in the amount of deposits raised through the use of finders fees for the purpose of determining compliance with the above per cent limitations.

(3) All finders fees must be paid in cash, except that an institution may utilize as finders fees any merchandise it owned on December 1, 1980.

(4) Any advertisement, announcement or solicitation concerning the continued availability of finders fees during the phaseout period by an institution shall be limited to contacting directly the institution's depositors or former sponsors of depositors or to displaying or distributing promotional materials in an institution's offices. During the phaseout period, an institution shall not advertise the continued availability of finders fees by television, radio, billboards or other mass media of general circulation (such as newspapers, magazines).

By order of the Committee, December 18, 1980.

(Signed) Normand R. V. Bernard

Normand R. V. Bernard
Executive Secretary of the Committee

[SEAL]