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**FEDERAL RESERVE BANK OF DALLAS**

Station K, Dallas, Texas 75222

Circular No. 84-53  
April 11, 1984

**TO:** All member banks and others concerned in the Eleventh Federal Reserve District

**ATTENTION:** Chief Executive Officer

**SUBJECT:** Policy statement concerning advertisements for time deposits that pay more than one fixed rate and a proposal to amend Regulation Q -- Interest on Deposits -- to incorporate the substance of the policy statement into the regulation

**SUMMARY:** The Board of Governors of the Federal Reserve System issued a policy statement on March 22, 1984 concerning the advertisement of multiple rate accounts. The policy statement addresses misleading advertising which indicates a high rate of interest for one period in large print while printing the lower rate in much smaller type. The policy statement also addresses advertising which refers to IRA accounts as being tax-free or tax-exempt.

In addition, the Board is proposing to amend its Regulation Q to incorporate the policy statement into the regulation. Interested parties are invited to submit comments to William W. Wiles, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, N.W., Washington, D.C., 20551. Comments must be received by May 22, 1984 and should refer to Docket No. R-0514.

**ATTACHMENTS:** Board's press release, policy statement and Regulation Q proposal as submitted for publication in the Federal Register

**MORE INFORMATION:** Legal Department, Extension 6171

**ADDITIONAL COPIES:** Public Affairs Department, Extension 6289

# FEDERAL RESERVE press release



For immediate release

March 23, 1984

The Federal Reserve Board today issued a policy statement concerning advertisements for time deposits that pay more than one fixed rate over the term of the account.

At the same time, the Board published for public comment a proposal to amend its Regulation Q--Interest on Deposits--that would incorporate the substance of the policy statement into the regulation.

The policy statement provides that advertisements for time deposits that pay more than one fixed interest rate should set forth, in equal size type, each rate of interest to be paid together with the length of time each rate will be paid and the average effective annual yield for the entire term of the account. Further, advertisements for deposits to be used in connection with Individual Retirement Accounts (IRAs) should not refer to such accounts as being tax-free or tax-exempt.

The Board's action was taken in response to recent advertisements where an initial high rate of interest appears in large print while a lower rate to be paid for the predominant part of the account appears in much smaller type. The Board expressed concern that such advertisements are potentially misleading and confusing to depositors. The Board anticipates that the Federal Deposit Insurance Corporation, the Federal Home Loan Bank Board, and the Comptroller of the Currency will issue similar policy statements in the near future.

The Board also requested comment on alternatives to the policy statement, and other advertising and disclosure issues that may warrant consideration under Regulation Q. The Board requested comment by May 22, 1984.

The Board's policy statement and its notice of proposed amendments to Regulation Q are attached.

FEDERAL RESERVE SYSTEM

REGULATION Q

[12 C.F.R. Part 217]

INTEREST ON DEPOSITS

[Docket No. R-0513]

Advertising of Multiple Rate Accounts

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Policy statement.

SUMMARY: The Board of Governors has issued a policy statement concerning potentially misleading advertising practices for time deposits used as investments for Individual Retirement Accounts. The Board believes that advertisements for time deposits that state in large type an initial rate that is effective for a period of a few months and then state in smaller type a lower rate that will be effective for the remaining term of the time deposit can be misleading to consumers. Such advertisements should state both rates in type of equal size in order not to be regarded as misleading, and include a conspicuous statement of the average effective annual yield. In addition, advertisements for deposits to be used in connection with Individual Retirement Accounts should not refer to contributions to such accounts as "tax-free" or "tax-exempt." This action was taken to assure that depository institutions provide meaningful and accurate information and to assist consumers to make comparisons of interest rates being offered on time deposits.

EFFECTIVE DATE: March 22, 1984.

FOR FURTHER INFORMATION CONTACT: Gilbert T. Schwartz, Associate General Counsel (202-452-3625), or Paul S. Pilecki, Senior Counsel (202-452-3281), Legal Division, Board of Governors of the Federal Reserve System, Washington, D.C. 20551.

SUPPLEMENTARY INFORMATION: The Federal Reserve Board has issued the following policy statement concerning advertisements for time deposits that have split, fixed interest rates and for accounts to be used as investments for Individual Retirement Accounts.

ADVERTISING OF MULTIPLE RATE TIME DEPOSITS AND  
INDIVIDUAL RETIREMENT ACCOUNTS

(a) The following advertising practice for deposits or accounts to be used as investments for Individual Retirement Accounts (IRAs) has come to the attention of the federal financial institution regulatory agencies with specific statutory authority to regulate advertising for deposits or other accounts. The advertisements display a rate of, perhaps, 15 percent in two to three inch type. In smaller, usually standard size, type, the advertisements state that the rate is paid only through a fixed date two or three months hence or for the first two or three months of the term of the account. For the remaining term of the account, which typically will be two to three years, the rate to be paid will be much lower, for example, 10.5 or 11 percent. In some cases, the maturity of the account is stated in bold type of a size similar to the higher interest rate.

(b) The Board believes that such advertisements are misleading and are in violation of section 217.6(g) of Regulation Q (12 CFR §§ 217.6(g)), which states that a member bank shall not make any advertisement related to interest paid on deposits that is inaccurate or misleading or that misrepresents its deposit contracts. In this regard, the display of a rate in substantially larger type than the rate that will apply for the predominant part of the term of the account is confusing to depositors and misrepresentative of the deposit contract. Moreover, such advertisements do not give meaningful information to consumers because the annual average effective yield over the life of the instrument will differ from the rates stated. (The staff of the Board has previously advised member banks that it regards any advertisement for a time deposit that states an annual rate of simple interest in excess of the average effective annual yield as inaccurate, misleading, and misrepresentative of their deposit contracts. ¶ 2-411.1 Federal Reserve Regulatory Service.)

(c)(1) Advertisements for time deposits where more than one rate is paid would not be regarded as misleading if each rate to be paid on the account is stated in the advertisement in type of equal size together with a conspicuous statement as to the length of time for which each rate is effective. This applies to accounts where a) it is known in advance what the rates to be paid throughout the life of the account will be and b) the initial rate to be paid is higher

than subsequent rates. In addition, such advertisements must include a conspicuous statement of the average effective annual yield for the deposit which assumes compounding of interest at least annually.

(2) For accounts subject to a variable interest rate that is determined by an index, the initial interest rate may be advertised; however, the advertisement must also include a conspicuous statement as to (i) the time period for which such rate applies, and (ii) the method by which the rates will be determined for future periods and the time period for which such rates will apply.

(3) For accounts that offer an initial fixed rate to be followed by a variable rate determined by an index during the remainder of the term of the account, the method of determining the variable rate shall be stated in type of the same size as the fixed rate. In addition, the time periods for which the initial fixed rate and subsequent rates apply must be conspicuously stated.

(d) It is also misleading and inaccurate for advertisements to refer to an IRA as a tax-free investment. Contributions to, and earnings on, IRAs are deferred from federal income taxes rather than exempt from taxes. Accordingly, such advertisements should not use the terms "tax-free" or "tax-exempt," or other similar language.

By order of the Board of Governors, March 22, 1984.

(signed) William W. Wiles

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William W. Wiles  
Secretary of the Board

FEDERAL RESERVE SYSTEM

REGULATION Q

[12 C.F.R. Part 217]

INTEREST ON DEPOSITS

[Docket No. R-0514]

Advertising of Interest on Deposits

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Proposed rulemaking.

SUMMARY: The Board is proposing to amend Regulation Q--Interest on Deposits to incorporate its Policy Statement of March 22, 1984, concerning advertising of split rate time deposits and Individual Retirement Account ("IRA") deposits and to clarify permissible advertising methods in view of the removal of federal deposit interest rate limitations. The Board is also requesting comments on other advertising and disclosure issues that may warrant consideration under Regulation Q.

DATES: Comments must be received by May 22, 1984.

ADDRESS: Interested parties are invited to submit written data, views, or arguments concerning the proposal to William W. Wiles, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, N.W., Washington, D.C. 20551, or such comments may be delivered to room B-2223 between 8:45 a.m. and 5:15 p.m. Comments may be inspected in room B-1122 between 8:45 a.m. and 5:15 p.m., except as provided in section 261.6(a) of the Board's Rules Regarding Availability of Information (12 C.F.R. § 261.6(a)).

FOR FURTHER INFORMATION CONTACT: Gilbert T. Schwartz, Associate General Counsel (202/452-3625); Paul S. Pilecki, Senior Counsel (202/452-3281); or Elaine M. Boutilier, Attorney (202/452-2418), Legal Division, Board of Governors of the Federal Reserve System, Washington, D.C. 20551.

SUPPLEMENTARY INFORMATION: The Board is authorized under Section 19(j) of the Federal Reserve Act (12 U.S.C. § 371b) to prescribe rules governing the advertisement of interest on time and savings deposits by member banks. The current regulation is codified in Regulation Q at 12 C.F.R. § 217.6--Advertising of Interest on Deposits. The Board believes that revisions to this regulation may be warranted in view of the deregulation of interest rate ceilings resulting from actions of the Depository Institutions Deregulation Committee ("DIDC") pursuant to the Depository Institutions Deregulation Act of 1980 (Title II of Pub. L. 96-221).

The DIDC has substantially deregulated the limitations on interest rate ceilings that previously existed. In this deregulated environment, depository institutions have greater freedom in structuring time and savings deposits. This freedom has led to a vast diversity in terms and conditions on deposit accounts, making it more difficult for the consumer to compare accounts. Consequently, the issue of whether customers are receiving meaningful information in advertisements for deposit accounts has become more important.



In recognition of this increased importance of advertising, on March 22, 1984, the Board adopted a Policy Statement concerning the advertising of split rate accounts, in particular, the potentially misleading advertising practices for deposits used as investments for IRAs. The Board anticipates that similar actions will be taken by the Comptroller of the Currency, the Federal Home Loan Bank Board, and the Federal Deposit Insurance Corporation. In summary, the Policy Statement provides that the Board believes that advertisements that state in large type an initial rate that is effective for a period of a few months and then state in smaller type a lower rate that will be effective for the remaining term of the deposit can be misleading to consumers. Such advertisements should state both rates in equal type in order not to be regarded as misleading. In addition, advertisements for deposits to be used in connection with IRAs should not refer to contributions to such accounts as "tax-free," "tax-exempt" or other similar terms. This action was taken to assure that depository institutions provide meaningful and accurate information and to assist consumers to make comparisons of deposit interest rates being offered.

The Board proposes that the principles set forth in its March 22, 1984 Policy Statement be incorporated into Regulation Q, as an amendment to 12 C.F.R. § 217.6. The Board is requesting comments on the proposed amendment, and also is interested in any alternative proposals that would achieve the goals of the Policy

Statement. In addition, the Board requests comments regarding other advertising and disclosure issues arising from the deregulation of interest rate ceilings, and whether existing provisions of Regulation Q should be modified to reflect the removal of interest rate ceilings. Currently, the regulation establishes a framework of deposit advertising rules aimed at full disclosure of the material elements of deposit instruments. As a general matter, Regulation Q prohibits any advertisements or solicitations relating to interest paid on deposits that are inaccurate, misleading, or misrepresentative of deposit contracts (12 C.F.R. § 217.6(g)). Other provisions of the regulation require that specific types of information appear in advertisements:

- (a) interest rates must be stated in terms of the annual rate of simple interest, and advertisements that display an effective annual yield based on compounding must state the annual rate of simple interest and the basis of compounding (12 C.F.R. § 217.6(a) and (b));
- (b) no interest rate can be advertised that states a yield based on a period of more than one year in order to ensure that effective yields are not artificially inflated (12 C.F.R. § 217.6(c));
- (c) if an advertised rate is payable only on a deposit that meets a specific time or amount requirement, such requirements must be stated clearly and conspicuously (12 C.F.R. § 217.6(d));
- (d) advertisements for time deposits must state that interest penalties apply in the event of early withdrawal (12 C.F.R. § 217.6(e));
- (e) member banks are required to inform customers at the time that an account is opened as to the method that will be used in computing and paying interest on the account, including any provision for nonpayment of interest (12 C.F.R. § 217.148).

The Federal Deposit Insurance Corporation and the Federal Home Loan Bank Board have virtually identical rules for institutions subject to their respective jurisdictions.

The Board is interested receiving comments on existing advertising and disclosure practices that may be harmful to individuals. In addition, the Board is interested in comments on changes that could be made to the existing advertising provisions to reflect the removal of interest rate ceilings on deposits. Such comments could, for example, discuss the proper method of advertising floating or variable interest rates, or requiring that rates for deposits be stated in terms of the average effective annual yield rather than requiring that the simple rate be used.

#### Regulatory Flexibility Analysis

The Regulatory Flexibility Act (5 U.S.C. § 601 et seq.) requires the Board to consider the impact of this proposal on small entities. In this regard, it is the Board's view that the proposal would not impose any additional reporting or recordkeeping requirements. The purpose of this proposal is to request comment on any alternatives that the public believes may be preferable to the Board's March 22, 1984 Policy Statement. Suggested alternatives will be considered when comments are analyzed. The proposed rule would apply only to commercial banks which are members of the Federal Reserve System. It is not anticipated that the proposal will have a

negative impact on the ability of small depository institutions to attract deposits, and the proposal should benefit consumers in their efforts to obtain the most favorable deposit terms.

List of Subjects in 12 C.F.R. Part 217

Advertising, Banks, banking; Federal Reserve System; Foreign banking.

Pursuant to its authority under section 19(j) of the Federal Reserve Act (12 U.S.C. § 371b) the Board proposes to amend section 217.6 of Regulation Q (12 C.F.R. Part 217) by revising paragraph (a), and by redesignating paragraph (g) as subparagraph (g)(1) and adding a new subparagraph (g)(2) as follows:

§ 217.6 -- ADVERTISING OF INTEREST ON DEPOSITS

\* \* \* \* \*

(a) Rate of interest.

(1) Interest rates shall be stated in terms of the annual rate of simple interest. In no case shall a rate be advertised that is in excess of the rate being paid on the deposit.

(2)(i) Advertisements for time deposits where more than one rate is paid must state each rate to be paid on the account in type of equal size together with a conspicuous statement as to the length of time for which each rate is effective and a conspicuous statement of the average effective annual yield for the deposit which assumes compounding of interest at least annually. This applies to accounts where

(A) it is known in advance what the rates to be paid throughout the life of the account will be and,

(B) the initial rate to be paid is higher than subsequent rates.

(ii) For accounts subject to a variable interest rate that is determined by an index, the initial interest rate may be advertised; however, the advertisement must also include a conspicuous statement as to (A) the time period for which such rate applies, and (B) the method by which the rate will be determined for future periods and the time period for which such rate will apply.

(iii) For accounts that offer an initial fixed rate to be followed by a variable rate determined by an index during the remainder of the term of the account, the method of determining the variable rate shall be stated in type of the same size as the fixed rate. In addition, the time periods for which the initial fixed rate and subsequent rates apply must be conspicuously stated.

\* \* \* \* \*

(g) Accuracy of advertising. (1) \* \* \*

(2) It is misleading and inaccurate for advertisements to refer an Individual Retirement Account ("IRA") as a "tax-free," "tax exempt" (or other similar language) investment. Contributions to, and earnings on, IRAs

are deferred from federal income taxes rather than exempt from taxes.

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By order of the Board of Governors of the Federal Reserve System, March 22, 1984.

(signed) William W. Wiles

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William W. Wiles  
Secretary of the Board