FEDERAL RESERVE BANK OF NEW YORK

[Circular No. 8215 November 10, 1977]

AMENDMENTS TO REGULATION Q

—Penalty for Early Withdrawal of Time Deposits —Payment of Time Deposits Before Maturity

To All Member Banks, and Others Concerned, in the Second Federal Reserve District:

The following statement was issued by the Board of Governors of the Federal Reserve System in connection with two amendments to its Regulation Q, "Interest on Deposits":

The Board of Governors of the Federal Reserve System today modified its rules to provide consumers with more flexibility in handling their time deposit accounts. A change in the rules concerning early withdrawal of time deposits will:

1. Permit member banks, at the request or upon permission of their depositors, to extend the maturity of a time deposit without penalty when there is no increase in the rate of interest.

2. Permit member banks to pay a time deposit before maturity without penalty upon the death of any owner of the deposit, whether or not that owner's name appears on the deposit. This will ease the administrative burden in the settlement of estates.

Current rules under Regulation Q—Interest on Time and Savings Deposits—require that an extension of maturity be treated as a payment of a time deposit before maturity subject to the penalty for early withdrawal. Also, a member bank may pay a time deposit before maturity without penalty following the death of a person whose name appears on the deposit.

The new rules will become effective December 1, 1977. The Board's rules in this respect will then be the same as those of the Federal Deposit Insurance Corporation and of the Federal Home Loan Bank Board.

Reductions in the maturity as well as increases in the rate of interest paid on the deposit will continue to be treated as an early withdrawal subject to penalty.

The penalty for withdrawal of a time deposit before maturity is (a) a reduction of the interest rate paid on the portion of the time deposit withdrawn to the maximum permissible passbook savings rate, and (b) a loss of three months interest on the portion withdrawn.

Customers entering into a time deposit contract must be supplied with a written statement specifying that the customer has contracted to keep the funds on deposit for a fixed time, and describing the penalty for early withdrawal.

In submitting the amendments for publication in the *Federal Register,* the Board of Governors issued the following explanatory notice:

Penalty for Early Withdrawals

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Final rule.

SUMMARY: The Board of Governors of the Federal Reserve System has approved an amendment to the fourth sentence of section 217.4(d) of Regulation Q (12 C.F.R. 217). That sentence currently provides that any amendment of a time deposit contract that results in either an increase in the rate of interest paid or a change in the maturity of the deposit constitutes a payment of the time deposit before maturity subject to the early withdrawal penalty rule contained in section 217.4(d). As amended, that sentence provides that an amendment of a time deposit contract that results in an increase in the rate of interest paid on the deposit or a reduction in the maturity of the deposit constitutes a payment of the time deposit before maturity. The amendment enables member banks, at the request or upon permission of their depositors, to extend the maturity of an outstanding time deposit without treating such extension of maturity as a withdrawal before maturity so long as the rate of interest paid on the time deposit is not increased.

EFFECTIVE DATE: December 1, 1977.

FOR FURTHER INFORMATION CONTACT: Allen L. Raiken, Assistant General Counsel, Legal Division, Board of Governors of the Federal Reserve System, Washington, D. C. 20551 (202-452-3625).

SUPPLEMENTARY INFORMATION: The fourth sentence of section 217.4(d) of Regulation Q treats an amendment of a time deposit contract that results in either an increase in the rate of interest paid or a change in the maturity of the deposit as a payment before maturity subject to the early withdrawal penalty. This provision was adopted in the summer of 1973 in response to volatile money market conditions. On July 5, 1973, the Board, in conjunction with the Federal Deposit Insurance Corporation ("FDIC") and the Federal Home Loan Bank Board, announced an increase in the prescribed maximum rates of interest payable on deposits by financial institutions subject to Federal regulation. As a result of this action, many banks moved to convert outstanding time deposits to deposits earning interest at the new higher prescribed maximum rates. The massive conversion of outstanding deposits, accomplished in many instances by extensions of maturity, created severe upward pressure on the cost of funds

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and threatened substantial disintermediation among depository institutions. As a result of this general credit situation, the Board acted to eliminate the conversion privilege by adopting the current provision contained in section 217.4(d) of Regulation Q.

The Board believes that the pressures on the general credit situation that necessitated the adoption of the conversion penalty rule in 1973 have now been substantially moderated. Accordingly, the Board believes that it is appropriate to restore to member banks the option of extending the maturity of outstanding time deposits without imposition of the early withdrawal penalty. The amendment adopted today permits member banks, at the request or upon permission of the depositor, to extend the maturity of an outstanding time deposit without the usually required penalty as long as the rate of interest paid on the time deposit is not increased. Under the provision, any amendment of a time deposit contract that results in a reduction in the maturity of the deposit will continue to be treated as a payment of the time deposit before maturity. The Board notes that this action conforms the Board's regulation with the provision contained in section 329.4 (e) of the FDIC's regulations and will, in certain circumstances, enable member banks to consolidate multiple outstanding certificates of deposit held by one customer. In addition, pursuant to longstanding Board policy, in the situation in which a member bank agrees to extend the maturity of an outstanding time deposit subsequent to a reduction in the maximum prescribed rate of interest payable on such time deposit, the rate of interest that may be paid on the time deposit from the date of conversion must not exceed the maximum rate permitted under the new rate schedule.

In view of the substantial public benefits that will immediately result from the adoption of this amendment, which relieves an existing regulatory restriction and permits member banks to extend the maturity of an outstanding time deposit, the Board has determined that notice and public participation with respect to this amendment are unnecessary and contrary to the public interest.

Payment of Time Deposits Before Maturity

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Final rule.

SUMMARY: This rule amends the provision contained in section 217.4(d) of Regulation Q (12 C.F R. § 217) concerning the payment of time deposits before maturity in the event of the death of persons named on the deposit instrument. Under the Board's current regulation, a member bank, upon the death of any person whose name appears on the time deposit passbook or certificate, is permitted to pay such time deposit before maturity without imposition of the usual early withdrawal interest forfeiture penalty. Under the regulation as amended, member banks will be permitted to pay a time deposit without imposition of the early withdrawal interest forfeiture penalty upon the death of any owner of the time deposit funds regardless of whether such person is named on the deposit instrument.

EFFECTIVE DATE: December 1, 1977.

FOR FURTHER INFORMATION, CONTACT: Allen L. Raiken, Assistant General Counsel, Legal Division, Board of Governors of the Federal Reserve System, Washington, D.C. 20551 (202-452-3625).

SUPPLEMENTARY INFORMATION: Effective June 5, 1975, the Board amended § 217.4(d) of Regulation Q to permit member banks to pay a time deposit prior to maturity without imposition of the normal early withdrawal penalty upon the death of any person whose name appears on the deposit instrument.[1] The amendment was adopted to facilitate the administration and settlement of estates. In adopting the amendment, the Board determined that for matters of administrative convenience the amendment should be limited to those instances involving the death of persons *named* on the deposit instrument. The Board believed that such a limited exception would minimize potential problems associated with determining true ownership of deposits. However, since adoption of this exception, the Board has received a number of requests that it amend its current death exception to include any owner whether or not named on the deposit instrument. Those requesting this change note that similar exceptions adopted by the Federal Deposit Insurance Corporation ("FDIC") and the Federal Home Loan Bank Board ("FHLBB") are applicable upon the death of any owner of a time deposit and urge the Board to amend its rule in order to permit uniform application of the death exception rule. Moreover, the Board has considered the experience of both the FDIC and the FHLBB under their broader exceptions, and has determined that the potential confusion and added administrative burden anticipated if the death exception were not limited to individuals named on the deposit instrument have not posed a substantial problem. Accordingly, the Board believes that it is appropriate to amend its death exception rule to permit member banks to pay a time deposit prior to maturity without imposition of the early withdrawal penalty upon the death of any owner of the time deposit, whether or not named on the deposit instrument. The Board believes that this amendment, which will liberalize the Board's death exception, will more fully effectuate the intent of the original rule to facilitate the administration of estates and will not increase the administrative burden on member banks in determining the owner of a time deposit instrument.

In view of the substantial public benefits that will immediately result from adoption of the amendment, which relieves an existing regulatory restriction and broadens the present Board rule regarding penalty-free payment of a time deposit prior to maturity in the event of a depositor's death, and in view of the extensive comments received at the time the present rule was adopted in June 1975, the Board has determined that notice and public participation with respect to this amendment are unnecessary and contrary to the public interest.

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[1] Section 217.4(d) of Regulation Q provides that where a time deposit, or any portion thereof, is paid before maturity, a member bank must assess an interest forfeiture penalty equivalent to a reduction of the rate of interest paid on the amount withdrawn to a rate not to exceed the rate prescribed for a savings deposit plus forfeiture of three months interest payable at such rate.

Enclosed is a copy of the amendments. Questions may be directed to our Consumer Affairs Division (Tel. No. 212-791-5919).

PAUL A. VOLCKER,
President.

Board of Governors of the Federal Reserve System

INTEREST ON DEPOSITS

AMENDMENTS TO REGULATION Q

Effective December 1, 1977, the fourth sentence of Section 217.4(d), and subsection (1) of Section 217.4(d) are amended as follows:

SECTION 217.4—PAYMENT OF TIME DEPOSITS BEFORE MATURITY

* * *

(d) **Penalty for early withdrawals.***** Any amendment of a time deposit contract that results in an increase in the rate of interest paid or in a reduction in the maturity of the deposit constitutes a payment of the time deposit before maturity.***

(1) where a member bank pays all or a portion of a time deposit upon the death of any owner of the time deposit funds;[11a]

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[11a] For the purposes of this provision, an "owner" of time deposit funds is any individual who at the time of his or her death has full legal and beneficial title to all or a portion of such funds or, at the time of his or her death, has beneficial title to all or a portion of such funds and full power of disposition and alienation with respect thereto.

For this Regulation to be complete, retain:

1) Regulation Q pamphlet, effective December 4, 1975.
2) Amendments effective March 1, 1976, July 26, 1976, November 8, 1976, March 24, 1977, and July 6, 1977.
3) Supplement effective December 4, 1975.
4) This slip sheet.

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