

FEDERAL RESERVE BANK  
OF NEW YORK

[ Circular No. 8338 ]  
May 8, 1978

AMENDMENT TO REGULATION Q

Automatic Transfers Of Funds  
From Savings Accounts To Checking Accounts

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

Following is the text of a statement issued by the Board of Governors of the Federal Reserve System:

The Board of Governors of the Federal Reserve System today [May 1, 1978] approved a plan that will permit individual customers of member banks to transfer funds automatically from their savings to their checking accounts.

Member banks may offer the new service beginning November 1, 1978. It will increase the convenience and efficiency of savings accounts and can be used to cover checking overdrafts or to maintain a minimum level of funds in a checking account.

The Board said that it will closely monitor the flow of funds to thrift institutions and to banks after automatic transfer becomes effective, to determine what, if any changes, take place, as a result of the action.

Automatic transfers will only be possible if arrangements are made in advance by the bank and the customer. Use of the service will be entirely voluntary on the part of the customer. Banks will be permitted, but not required, to offer the service.

The Board acted after extensive review of a record number of responses—1,380—to its proposal of the automatic transfer plan issued in early February. A majority of 721 (52 per cent) of the individuals, groups, governmental agencies and institutions responding favored the proposal.

Customers making automatic transfer arrangements with their banks can avoid the substantial fees banks usually charge for overdraft checks. Similarly, customers using the service will be able to keep checking accounts at a predetermined level, to avoid check service charges. Participating depositors, as well as merchants and others to whom overdraft checks are written, can avoid the embarrassment of having such checks returned.

The automatic transfer service will be an alternative for depositors in member banks to two services already permitted under Board rules: transfers from savings by telephone and preauthorized bill payment. It will also be an alternative to plans under which banks automatically make loans to cover customer's checks.

The principal features of the automatic transfer service plan adopted by the Board are:

1. Customers of banks offering arrangements for the automatic transfer of funds from savings to checking accounts may make an agreement with their bank for the transfer of funds to cover their checks, or to maintain a predetermined amount in their checking account. This means that without further instructions funds may be withdrawn from savings accounts and transferred to checking accounts to pay for checks for which there are insufficient funds in the customer's checking account.

2. No penalty—such as a forfeiture of interest or a service charge—will be required for automatic transfers, at least initially. The Board said, however, that competitive and other developments will remain under continuing review and will be considered again by the Board no later than November 1, 1979—one year after the effective date.

3. The service will be available only to individuals.

4. Automatic transfer service may be offered beginning November 1, 1978. Banks will therefore have a reasonable period to evaluate the costs and benefits of the automatic transfer service and to prepare for an orderly introduction of the service, including possible service charges.

5. The service will be entirely voluntary, both on the part of the bank and of the customer and may be cancelled in accordance with the terms of the automatic transfer agreement between the bank and the customer. No transfers may be made without the customer's consent.

(OVER)

6. Participating banks are required to disclose prominently, and to call to the attention of depositors, the fact that the bank—as in the past—reserves the right in an automatic transfer plan to require not less than 30 days' notice of withdrawal from savings accounts.

7. Arrangements may be made between thrift institutions (such as savings and loan associations) and member banks for the automatic transfer of funds from the thrift institution to checking accounts in the commercial bank.

In addition to the expected benefits to individuals, there will be a saving benefiting the public at large through lower operational costs of the Federal Reserve System due to a reduction in the number of checks written on accounts with insufficient funds. Such checks must be returned to the bank on which they are written, and they involve costly hand processing and multiple handling.

Approval of the automatic transfer service announced today amends Regulation Q — payments of interest on deposits. The Board has had the new service under consideration since it was first proposed in March 1976. The proposal was revised and issued for further comment in February of this year.

The proposal in February would have imposed on automatic transfers from savings a minimum forfeiture of interest equal to the amount of interest earned in the last 30 days on the sum transferred. Instead, the plan adopted by the Board imposes no penalty, at least initially.

A 52.2 per cent majority of responses received was favorable to the Board's plan. Individuals (424) overwhelmingly favored the idea. Some elderly respondents noted it would be particularly helpful to them because they found visits to the bank difficult.

All savings and loan associations responding (370) were opposed. The large majority of commercial banks and bank holding companies who offered comments were in favor (254 out of 382). Comment was received from 45 members of Congress of whom 42 were opposed. Members of the Congress in favor included the majority and minority leadership of the Senate banking committee. Of 24 trade groups responding, 16 were opposed. There were 7 responses from government agencies, of which 6 were favorable. Favorable responses were made by the Department of Justice, the Comptroller of the Currency, the Federal Council on Wage and Price Stability, and the Office of Consumer Affairs of the Health Education and Welfare Department. The Pennsylvania Department of Banking also supported the proposal. The proposal was opposed by the Federal Home Loan Bank Board — which regulates savings and loan associations — on grounds that it would amount to authorizing the payment of interest on demand deposits in violation of the spirit, if not the letter, of Federal law.

The principal objections of those who did not favor the automatic transfer service approved today were that it would be a violation of the prohibition against paying interest on demand deposits, is a matter best left to the Congress or that it tends to give commercial banks a competitive edge over thrift institutions.

In giving its approval to the automatic transfer plan the Board said that in its view the service does not violate the prohibition against payment of interest on demand deposits since the key distinction between demand and savings deposits is preserved. This distinction, drawn in the Board's regulation, is that a bank must reserve the right to at least 30 days' notice prior to withdrawal of a savings deposit. Banks offering automatic transfer service are required to continue to reserve this right.

Further, the Board said that it has given serious consideration to competitive aspects, and concluded that the automatic transfer service will not seriously affect the flow of funds to thrift institutions since it is likely to affect most the division of commercial bank deposits among savings and demand deposits and is similar to preauthorized bill payment and telephone withdrawal services that both banks and savings and loan associations are presently permitted to offer.

Enclosed is a copy of the amendment to Regulation Q. Questions thereon 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

### AMENDMENT TO REGULATION Q

(effective November 1, 1978)

#### Withdrawals from Savings Deposits

**AGENCY:** Board of Governors of the Federal Reserve System.

**ACTION:** Final Rule.

**SUMMARY:** On February 2, 1978, the Board of Governors of the Federal Reserve System invited public comment on a revised proposed amendment to Regulation Q (Interest on Deposits) that would permit banks that are members of the Federal Reserve System to arrange with their depositors for the automatic transfer of funds from depositors' savings accounts to demand deposit (checking) and other accounts to cover checks drawn by depositors or to replenish or maintain a minimum balance in such accounts (43 FR 5008). The period for receipt of public comment on the proposed amendment expired on March 20, 1978. After consideration of the comments submitted and the views expressed therein, the Board has determined to adopt the proposed amendment with modifications, effective November 1, 1978. The amendment adopted differs slightly from the proposal in that it does not require the imposition of an interest forfeiture. However, the Board encourages member banks to develop charges for automatic transfers to reflect the costs of providing the service to depositors. The Board will monitor the development of this new service, including its competitive effects among various types of banks and nonbank depository institutions, and will review the appropriateness of making any modifications on or before the first anniversary of the effective date of this amendment.

As adopted, the transfer service is entirely voluntary, and automatic transfers may not be made unless previously authorized in writing by the depositor. In addition, the automatic transfer service will be available only to individuals and not to business and other organizations or governmental units. For purposes of this provision, a partnership is considered to be a business or other organization. The automatic transfer service will provide depositors with an alternative to existing arrangements, such as automatic overdraft loans, when there

are insufficient funds in depositors' checking accounts. The service should also increase the efficiency of the Federal Reserve's check clearing operations by reducing the number of return items processed by the System.

**EFFECTIVE DATE:** November 1, 1978.

**FOR FURTHER INFORMATION, CONTACT:** Allen L. Raiken, Associate General Counsel, ((202) 452-3625) or Gilbert T. Schwartz, Senior Attorney, ((202) 452-3623) Legal Division, Board of Governors of the Federal Reserve System, Washington, D.C. 20551.

**SUPPLEMENTARY INFORMATION:** In response to notice published in the *Federal Register* (43 FR 5008), the Board has received and carefully reviewed almost 1,400 comments on the proposed amendment. A majority of those responding (52.2 percent) favored adoption of the proposal. Of the 382 commercial banks commenting, 254 (66.5 percent) favored adoption of the proposed amendment; 517 individuals responded, with 424 (82 percent) in favor of adoption; 370 savings and loan associations (100 percent of those responding) opposed adoption of the proposal. Those responding in favor generally commented that the proposal represents a convenience and benefit to consumers and that it would save overdraft charges that would be assessed if the service were not available. Those opposed to the proposal principally commented that the proposal would authorize the payment of interest on demand deposits in violation of law (12 U.S.C. § 371a) and that it would pre-empt Congressional action by creating nationwide negotiable order of withdrawal (NOW) accounts. Others commented that the proposal would give commercial banks an unfair competitive advantage over savings and loan associations and other thrift institutions. (A detailed summary of comments received is available upon request from the Board's Office of Public Affairs, telephone (202) 452-3204; 3215).

After consideration of the issues presented, the Board's Office of Public Affairs, telephone provide significant benefits to the public in

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, July 6, 1977, November 23, 1977, December 1, 1977, and July 6, 1978 (*in process of issuance*).
- 3) Supplement effective December 4, 1975.
- 4) This slip sheet.

the form of an additional convenient savings deposit withdrawal service. The amendment should also increase the efficiency of the Federal Reserve's check clearing operations by reducing the number of return items processed by the System. Consequently, the Board has determined to adopt the proposal, effective November 1, 1978.

The Board believes that the automatic transfer service does not violate the prohibition against the payment of interest on demand deposits. Section 19(a) of the Federal Reserve Act (12 U.S.C. § 461) authorizes the Board to define the terms "savings deposit" and "demand deposit." Pursuant to § 19, the distinction drawn in the Board's regulations between savings and demand deposits is that a bank must reserve the right to require at least 30 days notice prior to withdrawal from a savings deposit, while demand deposits are available on demand. The amendment does not alter this basic distinction, and member banks will continue to be required to reserve the right to impose at least a 30-day notice period on intended withdrawals of savings deposits as presently required in § 217.1(e) of Regulation Q (12 CFR 217).

Further, it is the Board's view that the amendment does not authorize member banks to establish NOW accounts, which involve the use of negotiable orders of withdrawal to effect transfers of funds directly from savings accounts for payments to third parties. Section 1832(a) of Title 12 of the *United States Code* prohibits the drawing of negotiable or transferable instruments for the purpose of making transfers to third parties against a deposit or account on which interest or dividends are paid except in the six New England States. The Board's amendment does not authorize member banks to permit depositors to draw negotiable or transferable instruments against interest bearing savings accounts for the purpose of making transfers to third parties and does not affect the restriction that, outside of New England, member banks may permit depositors to draw negotiable instruments only against non-interest bearing demand deposit accounts. The amendment only permits member banks to arrange in advance with depositors to withdraw funds automatically from a depositor's savings account to be transferred to a noninterest bearing demand deposit account against which checks may be drawn or other accounts. The effect of the amendment, therefore, is to provide depositors with a withdrawal service that is identical in its essential elements to withdrawal services that banks already are authorized to offer to depositors such as withdrawals in person or via telephone.

In adopting this amendment, the Board has given careful consideration to its potential effect on the competitive balance among financial

institutions, and has determined that adoption of the service will not seriously affect the flow of funds to thrift institutions under the existing ceiling rate structure. The amendment only enables member banks to offer an additional deposit withdrawal and transfer service similar to the preauthorized bill payment and telephone withdrawal services that both banks and savings and loan associations are presently permitted to offer. Thus, this additional service is likely to affect mainly the composition of commercial bank deposit liabilities, as depositors use the added convenience to hold somewhat less funds in demand deposit accounts that bear no interest and somewhat more in savings accounts.

The amendment, as adopted, is in essentially the form proposed, but with one modification. As proposed, the amendment would have required a forfeiture of interest in an amount no less than the amount of interest actually earned during the previous 30 days on the funds transferred from savings to checking accounts. As adopted, the amendment does not require the imposition of an interest forfeiture. This modification was adopted after consideration of comments received that indicated that the proposed required forfeiture of interest would necessitate substantial and costly operational changes by banks offering the automatic transfer service and would significantly lessen the benefits to consumers of the automatic transfer service. In order to maximize benefits to consumers, the Board has determined to adopt the amendment without a required interest forfeiture. However, during the first year after the effective date, the Board will monitor the effects of the automatic transfer service, including its effect on the competitive structure among banks and thrift institutions. The Board intends to work with the Federal Home Loan Bank Board and the Federal Deposit Insurance Corporation to gather information concerning the effects of the proposal on banks, savings and loan associations and other thrift institutions. Not later than one year after the effective date, the Board will review available data and will report its findings to the public.

Although the amendment does not require the imposition of an interest forfeiture, on the basis of comments received, the Board expects that banks will impose service charges that reflect, among other factors, the costs of providing the service to depositors. The Board believes that such charges imposed by member banks are appropriate. Accordingly, the Board encourages all member banks to evaluate their costs for providing the automatic transfer service and, in light of competitive circumstances, to develop charges for the service. Member banks are urged to impose such charges in the form of an interest forfeiture to afford depositors the opportunity to report such amounts

as interest forfeited for income tax purposes to the extent permissible under Federal and State law.

The amendment does not impose a minimum denomination requirement on the amount of savings funds that may be transferred automatically. However, member banks may, if so desired, impose such a minimum denomination requirement.

Member banks will continue to be required to reserve the right to impose at least a 30-day notice period on intended automatic withdrawals of savings deposits as presently required in § 217.1(e) of Regulation Q (12 CFR 217). It is required that such reservation specifically be called to the depositor's attention and be stated prominently in written arrangements authorizing the transfer service entered into by banks and their depositors. In addition, as in all advertisements, announcements, and solicitations, member banks are expected to describe accurately the terms and conditions under which savings deposits may be automatically withdrawn and transferred pursuant to this rule.

The amendment will not affect arrangements whereby a thrift institution has agreed with its customer to transfer funds automatically or otherwise to the customer's demand deposit account at a member bank in accordance with a preauthorized agreement. Similarly, the amendment does not affect the ability of a member bank to use a depositor's savings deposit in satisfaction of a debt where the bank is authorized to do so under local law.

Under the terms of the proposal announced by the Board on February 2, member banks would be required to maintain data on funds transfers via the automatic transfer service in a manner that would facilitate data collection by the Board. In this connection, the Board has determined that member banks should maintain the following data on a monthly basis with regard to the automatic transfer service: the total amount of savings deposits subject to automatic transfer, the total amount of savings funds actually transferred, the number of such automatic transfers during the month, and the interest forfeiture or other charges imposed by the bank.

In view of the comments received which indicated that a delayed effective date of 60 days, as proposed by the Board in its February 2 release, was not sufficient, the Board has determined that the amendment will become effective

on November 1, 1978. The Board believes that delaying the effective date of the amendment for approximately six months will provide sufficient time for member banks to effect the operational and marketing changes necessary to introduce the automatic transfer service in an orderly and beneficial fashion.

#### Text of Amendment

Pursuant to its authority under § 19 of the Federal Reserve Act (12 U.S.C. §§ 461, 371b), effective November 1, 1978, the Board of Governors amends § 217.5(c)(2) and (3) of Regulation Q (12 CFR 217.5(c) (2) and (3)) to read as follows:

#### SECTION 217.5—WITHDRAWAL OF SAVINGS DEPOSITS

\* \* \*

#### (c) Manner of payment of savings deposits.

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(2) Notwithstanding the provisions of subparagraph (1) of this paragraph, withdrawals may be permitted by a member bank to be made automatically or as a normal practice from a savings deposit that consists only of funds in which the entire beneficial interest is held by one or more individuals through payment to the bank itself or through transfer of credit to a demand deposit or other account pursuant to a written authorization from the depositor to make such payments or transfers in order to cover checks or drafts drawn upon the bank or to maintain a specified balance in or to make periodic transfers to such accounts. In accordance with § 217.1(e) (2) of this Part, a member bank must reserve the right to require the depositor to give notice in writing of an intended withdrawal not less than 30 days before such withdrawal is made. Such notice shall be prominently disclosed and specifically brought to the depositor's attention at the time the automatic transfer service is authorized. A member bank may not require a depositor to authorize such automatic transfers to be made from savings deposits.

(3) A member bank may permit depositors to maintain deposits subject to negotiable orders of withdrawal where authorized by Federal law.

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