FEDERAL RESERVE BANK OF NEW YORK

Circular No. 8551
April 4, 1979

REGULATION Q

Comment Invited on Proposals Relating to New Types of Savings Deposits

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

The Board of Governors of the Federal Reserve System, the Federal Home Loan Bank Board, and the Federal Deposit Insurance Corporation have issued the following joint announcement:

A series of measures designed to help individuals obtain a higher rate of return on their savings was proposed today [April 3] for public comment by the Federal regulators of financial institutions.

Comment was requested by May 4 on possible actions that could be taken on individual proposals or in combination. The regulators emphasized that the following proposals are open to change on such specifics as maturity, rate, penalty or other terms on the basis of public comment received:

1. Creation of a five-year certificate of deposit with a maximum rate of interest based on but below the rate on U.S. Treasury securities of similar maturity.

2. Introduction of a bonus savings account that would pay an extra 1/2 percent on the minimum balance held in the account over a 12-month period.

3. Creation of a rising-rate certificate featuring higher liquidity and an interest rate ceiling that increases during the term of the certificate.

4. Elimination of all minimum deposit requirements on certificates of less than four years (required currently only at savings and loan associations) and reducing the minimum amount to $500 for other certificate accounts, except for the $10,000 minimum required for six-month (26-week) money market certificates.

These actions were proposed jointly by the Federal Home Loan Bank Board for federally insured savings and loan associations, the Federal Reserve Board for all national and State member banks, and by the Federal Deposit Insurance Corporation for federally insured nonmember banks and savings banks.

Today's proposals are consistent with an announcement made by the agencies on March 8, when new rules were issued for the six-month money market certificate. At that time, the agencies said they were reviewing the terms on other types of deposits "with a view toward providing improved savings opportunities for the small saver."

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Five-year CDs

In seeking public comment on the proposal for a five-year CD, the agencies suggested a ceiling rate for commercial banks that would be 1 1/4 percentage points below an average five-year rate based on U.S. Treasury securities. The ceiling for thrift institutions would be 1 percentage point below the same Treasury rate.

Ceilings for newly issued CDs would change once each month. Beginning the first Thursday of every month, the ceiling rate for new instruments issued that month would be based on the average five-year rate for the preceding calendar week as determined by the Treasury. Under this formula, the nominal ceilings for April 1979 would be 7.95 percent for commercial banks and 8.20 percent for thrift institutions. The corresponding effective yields, including continuous compounding, would be 8.39 percent for banks and 8.67 percent for thrifts.

The penalty for premature withdrawal on this instrument would be forfeiture of six months' interest.

Bonus savings accounts

Under this proposal, a lump-sum bonus could be paid on the minimum in a savings account maintained by an individual or qualified nonprofit organization during a 12-month period.

This bonus would be in addition to the maximum rates on savings accounts of 5 percent for commercial banks and 5 1/4 percent for savings banks and savings and loan associations.

Rising-rate certificates

The maturity for the proposed rising-rate certificate would be 8 years and the interest rate ceiling would rise in accordance with the following schedule:

MAXIMUM RATES PAYABLE

Period	Commercial Banks	S&Ls and MSBs
0-1 year	6	6 1/4
Over 1 - 2 1/2 years	6 1/2	6 3/4
Over 2 1/2 - 4 years	7	7 1/4
Over 4 - 5 years	7 1/2	7 3/4
Over 5 - 8 years	8	8 1/4

Interest at the above rates would be paid only for the period indicated. The 6 percent rate for commercial banks, for example, would be paid during the first year of the certificate; the ceiling rate would rise to 6 1/2 percent only for the period from 1 year to 2 1/2 years, and so on. Compounding will be allowed on these accounts.

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The penalty for early withdrawal during the first year would be forfeiture of three months' interest. No penalty would be required after that. Additions to the account could be made only during the first year.

Minimum denomination

Presently, there is a $1,000 minimum required for certain categories of time deposits. The agencies proposed reducing this minimum to $500 although institutions would be free to establish a higher minimum if they desired.

The regulators noted that cost studies indicate that the four proposed measures may have a greater financial impact on thrifts, due to their asset structure, than commercial banks. The proposals, by affecting deposit flows and the cost of deposit funds, may impact somewhat on mortgage rates.

With regard to Federal credit unions, the National Credit Union Administration is not mandating specific maturities--which may range from 90 days on out--for its share certificate accounts (similar to CDs). However, in order to maintain consistency among financial institutions, the maximum rates payable on such certificates would be set 1/4 percent above the ceiling rates specified for commercial banks.

In transmitting the statement to the Reserve Banks, the Board of Governors also noted:

These proposed actions would not change the ceiling rates currently in effect for outstanding deposits. Also, the ceiling rate that may be paid on IRA and Keogh accounts and on government time deposits would remain at 8 percent regardless of the ceilings established for five-year CDs or eight-year rising rate certificates.

The only changes proposed in the penalty for early withdrawal are on the five-year CD and the rising-rate certificate. The penalty on all other certificates would remain unchanged--namely, the loss of three months interest and reduction of remaining interest to the passbook rate on the amount of funds withdrawn. However, public comment is sought on whether the proposed six-month penalty on the five-year certificate should apply to all other CDs.

The text of the proposals will be mailed to all member banks in this District when available. It will also be published in the Federal Register.

Comments on the proposals should be submitted by May 4 and may be sent to our Consumer Affairs and Bank Regulations Department.

PAUL A. VOLCKER,
President.

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