FEDERAL RESERVE BANK
OF NEW YORK

[ Circular No. **9225**
December 31, 1981 ]

# REGULATION Q

## Technical Amendments Conforming the Regulation to DIDC Rules

*To All Depository Institutions, and Others Concerned,*
*in the Second Federal Reserve District:*

The Board of Governors of the Federal Reserve System has amended its Regulation Q, "Interest on Deposits," in order to conform the regulation to the rules adopted by the Depository Institutions Deregulation Committee (DIDC) relating to:

1) Time deposits of less than $100,000 with maturities of 2½ years to less than 4 years;

2) ceiling rates for 26-week money market time deposits;

3) qualified tax-exempt savings certificates; and

4) new IRA/Keogh time deposits.

Enclosed is a copy of the text of the technical amendments to Regulation Q, effective December 16, 1981. Questions regarding the regulation may be directed to our Consumer Affairs and Bank Regulations Department (Tel. No. 212-791-5914).

ANTHONY M. SOLOMON,
*President.*

# Board of Governors of the Federal Reserve System

# INTEREST ON DEPOSITS

## AMENDMENTS TO REGULATION Q

*(effective December 16, 1981)*

**FEDERAL RESERVE SYSTEM**

**12 CFR Part 217**

**[Docket No. R-0379]**

**Interest on Deposits; Regulation Q; Technical Amendments**

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

**ACTION:** Technical amendments.

**SUMMARY:** Pursuant to its authority under section 19 of the Federal Reserve Act, as amended, the Board has amended Regulation Q (Interest on Deposits) to incorporate the rules of the Depository Institutions Deregulation Committee ("DIDC"), adopted pursuant to the Depository Institutions Deregulation Act of 1980 (Title II of Pub. L. 96–221). The amendments to Regulation Q are technical and conform the Board's rules to those of the DIDC.

**EFFECTIVE DATE:** December 16, 1981.

**FOR FURTHER INFORMATION CONTACT:** Gilbert T. Schwartz, Associate General Counsel (202/452–3625), Paul S. Pilecki, Senior Attorney (202/452–3281), or Beverly A. Belcamino, Attorney (202/452–3623), Legal Division, Board of Governors of the Federal Reserve System, Washington, D.C. 20551.

**SUPPLEMENTARY INFORMATION:** The Depository Institutions Deregulation Act of 1980 (Title II of Pub. L. 96–221) transfers to the DIDC the authority conferred by section 19(j) of the Federal Reserve Act (12 U.S.C. 371b) upon the Board (and the similar authority of the Federal Deposit Insurance Corporation and the Federal Home Loan Bank Board which are contained in other statutes) to prescribe rules relating to the payment of interest on deposits. The DIDC has issued final regulations and amendments to existing rules as follows: (1) Time deposits of less than $100,000 with maturities of 2½ years to less than 4 years (12 CFR 1204.106; 46 FR 20155 and 37020); (2) ceiling rates for 26-week money market time deposits (12 CFR 1204.104; 46 FR 20155, 51897 and 55507); (3) qualified tax-exempt savings certificates (12 CFR 1204.116; 46 FR 45121); and (4) new IRA/Keogh time deposits (12 CFR 1204.118; 46 FR 53395 and 58285). In view of these actions by the DIDC, the Board is amending Regulation Q to incorporate these changes.

The following table presents the provisions of Regulation Q that have been amended by the DIDC's actions.

TABLE OF REGULATION Q CHANGES

| DIDC Rule | | Regulation Q provision affected |
|---|---|---|
| 1204.104 | Ceiling rates for 26-week money market certificates. | 217.7(f). |
| 1204.106 | Time deposits of less than $100,000 with maturities of 2½ years to less than 4 years. | 217.7(g). |
| 1204.116 | Qualified tax-exempt savings certificates. | 217.7(b), 217.3(a), 217.7(i) (new paragraph). |
| 1204.118 | IRA/Keogh time deposits. | 217.7(e). |

Because these amendments are necessary to conform the Board's rules to those of the DIDC, the Board for good cause finds that the notice, public procedure, and deferral of effective date provisions of 5 U.S.C. 553 (b) and (d) with regard to this action are unnecessary and contrary to the public interest.

**PART 217—INTEREST ON DEPOSITS**

Pursuant to the Board's authority under section 19 of the Federal Reserve Act (12 U.S.C. 461, 371b) to prescribe rules to effectuate the purposes of that section and to prevent evasions thereof, Regulation Q, 12 CFR Part 217, is amended as follows:

1. Section 217.3 (12 CFR 217.3) is amended by revising paragraph (a) to read as follows:

**§ 217.3 Interest on time and savings deposit.**

(a) *Maximum rate.* Except as provided in this section, no member bank shall, directly or indirectly, by any device whatsoever, pay interest on any time or savings deposit at a rate in excess of such applicable maximum rate as the Board of Governors of the Federal Reserve System shall prescribe from time to time in § 217.7. Except as provided in § 217.7(i), in ascertaining the rate of interest paid, the effects of compounding of interest may be disregarded. The maximum rate of interest that may be paid by a member bank on an additional deposit to any existing time deposit shall not exceed the maximum rate that may be paid in accordance with § 217.7 on the date the additional deposit is made.

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2. Section 217.7 (12 CFR 217.7) is amended by revising paragraph (b) to read as follows:

**§ 217.7 Maximum rates of interest payable by member banks on time and savings deposits.**

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(b) *Fixed-ceiling time deposits of less than $100,000.* Except as provided in paragraphs (a), (d), (e), (f), (g), and (i), no member bank shall pay interest on any time deposit at a rate in excess of the applicable rate under the following schedule:

For this Regulation to be complete, retain:
1) Regulation Q pamphlet, effective January 15, 1981.
2) Supplement to Regulation Q, effective January 15, 1981.
3) This slip sheet.

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| Maturity | Maximum percent |
|---|---|
| 14 days or more but less than 90 days | 5¼ |
| 90 days or more but less than 1 year | 5¾ |
| 1 year or more but less than 2-½ years | 6¾ |
| 2-½ years or more but less than 4 years | 6½ |
| 4 years or more but less than 6 years | 7¼ |
| 6 years or more but less than 8 years | 7½ |
| 8 years or more | 7¾ |

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3. Section 217.7 (12 CFR 217.7) is amended by revising paragraph (e) to read as follows:

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(e) *Individual Retirement Account and Keogh (H.R. 10) Plan deposits of less than $100,000.* (1) Except as provided in paragraphs (a), (e) (2), and (g) of this section, a member bank may pay interest on any time deposit with a maturity of three years or more that consists of funds deposited to the credit of, or in which the entire beneficial interest is held by, an individual pursuant to an Individual Retirement Account agreement or Keogh (H.R. 10) Plan established pursuant to 26 U.S.C. (I.R.C. 1954) 219, 401, 404, 408 and related provisions at a rate not in excess of 8 percent.[2]

(2) A member bank may pay interest at any rate as agreed to by the depositor on any time deposit with a maturity of one and one-half years or more, that consists of funds deposited to the credit of, or in which the entire beneficial interest is held by, an individual pursuant to an Individual Retirement Account agreement or Keogh (H.R. 10) Plan established pursuant to 26 U.S.C. (I.R.C. 1954) 219, 401, 404, 408 and related provisions. An institution may permit additional deposits to be made to such a time deposit at any time prior to its maturity without extending the maturity of all or a portion of the entire balance in th~ account.

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4. Section 217.7 (12 CFR 217.7) is amended by revising paragraph (f) to read as follows:

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(f) *26-week money market time deposits of less than $100,000.* Except as provided in paragraphs (a), (b) and (d) of this section, a member bank may pay interest on any nonnegotiable time deposit of $10,000 or more, with a maturity of 26 weeks, at a rate not to exceed the ceiling rates set forth below. The ceiling rate shall be based on the higher of either (1) The rate established and announced (auction average on a discount basis) for U.S. Treasury bills with maturities of 26 weeks at the auction held immediately prior to the date of deposit ("Bill Rate"), or (2) the average of the four rates established and announced (auction average on a discount basis) for U.S. Treasury bills with maturities of 26 weeks at the four auctions held immediately prior to the date of deposit ("Four-Week Average Bill Rate"). Rounding any rate to the next higher rate is not permitted and interest may not be compounded during the term of this deposit.

| Bill rate or 4-week average bill rate | Interest rate ceiling |
|---|---|
| 7.50 percent or below | 7.75 percent. |
| Above 7.50 percent | One-quarter of one percentage point plus the higher of the bill rate or 4-week average bill rate. |

A member bank may offer this category of time deposit to all depositors. However, a member bank may pay interest on any nonnegotiable time deposit of $10,000 or more with a maturity of 26 weeks which consists of funds deposited to the credit of, or in which the entire beneficial interest is held by:

(1) The United States, any state of the United States, or any county, municipality or political subdivision thereof, the District of Columbia, the Commonwealth of Puerto Rico, the Virgin Islands, American Samoa, Guam, or political subdivision thereof; or

(2) An individual pursuant to an Individual Retirement Account agreement or Keogh (H.R. 10) Plan established pursuant to 26 U.S.C. (I.R.C. 1954) 219, 401, 404, 408 and related provisions at a rate not to exceed the ceiling rate payable on the same category of deposit by any Federally insured savings and loan association or mutual savings bank.[3]

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5. Section 217.7 (12 CFR 217.7) is amended by revising paragraph (g) to read as follows:

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(g) *Time deposits of less than $100,000 with maturities of 2½ years to less than 4 years.* Except as provided in paragraphs (a), (b), (d), and (e) of this section, a member bank may pay interest on any nonnegotiable time deposit with an original maturity of 2½ years to less than four years at a rate not to exceed the higher of one-quarter of one percent below the average 2½ year yield for U.S. Treasury securities as determined and announced by the U.S. Department of the Treasury immediately prior to the date of deposit, or 9.25 percent. Such announcement is made by the U.S. Department of the Treasury every two weeks. The average 2½ year yield will be rounded by the U.S. Department of the Treasury to the nearest 5 basis points. The rate paid on any such deposit cannot exceed the ceiling rate in effect on the date of deposit. A member bank may offer this category of time deposit to all depositors. However, a member bank may pay interest on any nonnegotiable time deposit with a maturity of 2½ years to less than 4 years which consists of funds deposited to the credit of, or in which the entire beneficial interest is held by:

(1) The United States, any state of the United States, or any county, municipality or political subdivision thereof, the District of Columbia, the Commonwealth of Puerto Rico, the Virgin Islands, American Samoa, Guam, or political subdivision thereof; or

(2) An individual pursuant to an Individual Retirement Account agreement or Keogh (H.R. 10) Plan established pursuant to 26 U.S.C. (I.R.C. 1954) 219, 401, 404, 408 and related provisions at a rate not to exceed the ceiling rate payable on the same category of deposit by any Federally insured savings and loan association or mutual savings bank.[4]

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6. Section 217.7 (12 CFR 217.7) is amended by adding a new paragraph (i) as follows:

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(i) *Tax-exempt savings certificate.* (1) A member bank may pay interest on a nonnegotiable tax-exempt savings certificate ("ASC") provided that the time deposit has an original maturity of exactly one year, is available in denominations of $500 and any other denomination, at the discretion of the member bank, and has an annual investment yield to maturity equal to 70 percent of the average investment yield for the most recent auction of 52-week U.S. Treasury bills prior to the calendar week in which the ASC is issued.[5]

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[2] * * *

[3] * * *

[4] * * *

[5] When institutions credit interest more frequently than annually, the computation of interest must be adjusted to reflect the effects of compounding so that the annual investment yield to the depositor remains at the rate stipulated by law. Specifically, the formula used to derive the nominal interest rate at which interest can be credited is as follows:

$I=[(1=c/100^{(d/369)}]-1$

$r=100\times(365/d)\times I$

where: c = the annual investment yield required to be paid on the ASCs (in pe[illegible]t per annum)

D = the average number of [illegible]ays in a compounding period (365-day year)

I = the amount of interest earned during a (365-day year) compounding period per dollar in the account at the beginning of the period.

r = the correspondeing nominal rate of interest (365-day basis, in percent per annum)

For institutions using continuous compounding, the nominal interest rate would be defined as: $r=100[1n(1+(c/100))]$, where "ln" signifies the natural logarithm of the expression that follows it.

(2) A member bank must provide each depositor the following notice, in a form that the depositor may retain at the time of opening a deposit under this paragraph:

The Economic Recovery Tax Act of 1981 authorizes a lifetime exclusion from gross income for federal income tax purposes of up to $1,000 ($2,000 in the case of a joint return) for interest on tax-exempt savings certificates. Regardless of how much interest is earned on this or any other tax-exempt savings certificate, including interest earned on such certificates from other institutions, and regardless of during which taxable years that interest is earned, no more than a total of $1,000 ($2,000 in the case of a joint return) can be excluded from federal gross income for all taxable years. Furthermore, interest earned on a specific certificate cannot be excluded from federal gross income if (A) that certificate is used as collateral for any loan, or (B) any part of the principal of that certificate is redeemed or disposed of prior to maturity.

(3)(i) A member bank may not issue ASCs after March 31, 1982, under this paragraph unless an executive officer of the member bank certifies, in a form determined by the member bank, that the member bank has complied with the "qualified residential financing" requirement set out in 26 U.S.C. 128. The certification must be maintained by the member bank in its files and must be available to the member bank's primary supervisory agency upon request. The certification shall include appropriate supporting documentation, as determined by the member bank.

(ii) A member bank issuing ASCs during any calendar quarter must use at least 75 percent of the lesser of:

(A) The proceeds from ASCs issued during a calendar quarter, or

(B) "Qualified net savings," to provide "qualified residential financing" by the end of the subsequent calendar quarter and may not issue additional ASCs unitl the 75 percent requirement is satisfied.

(iii) For purposes of determining compliance with the "qualified residential financing" requirement, the following applies:

(A) The term "qualified net savings" includes interest or dividends credited to deposit accounts;

(B) The amount of "qualified residential financing" is to be determined net of repayment of principal and paydowns, but sales of such assets may not be netted;

(C) The term "any loan for agricultural purposes" is defined to have the same meaning as items described in the instructions to the Report of Condition of all Insured Commercial Banks, schedule A, item 4 "Loans to Finance Agricultural Production and Other Loans to Farmers," and schedule A, item 1(b) "Real Estate Loans Secured by Farmland," and

(D) "Qualified residential financing" includes a firm commitment to purchase any assets eligible for such investment.

(iv) If a member bank provides for automatic renewal of an ASC, depositors must be notified in writing at least 15 days in advance of the maturity of an ASC in the event the member bank cannot renew the ASC because of its failure to satisfy the residential financing requirement. Failure to give such notice shall not result in automatic renewal of the ASC.

(v) This paragraph (i) expires January 1, 1983.

By order of the Board of Governors of the Federal Reserve System, December 17, 1981.
William W. Wiles,
*Secretary of the Board.*