

**FEDERAL RESERVE BANK
OF NEW YORK**

[Circular No. **10710**]
June 2, 1994]

PAYMENTS SYSTEM RISK
Interpretation Regarding Daylight Overdrafts
of Government-Sponsored Enterprises

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

The Board of Governors of the Federal Reserve System has issued an interpretation of its Policy Statement on Payments System Risk to include a comprehensive policy towards daylight overdrafts incurred by Government-sponsored enterprises, recognizing the unique nature of the fiscal agency relationship that exists between the Federal Reserve and those entities. Under the payments system risk reduction program, Government-sponsored enterprises that maintain accounts at Reserve Banks should not incur daylight overdrafts in these accounts and are not permitted to adopt a positive daylight overdraft net debit cap.

The Board of Governors has waived all fees on daylight overdrafts in accounts of Government-sponsored enterprises until October 13, 1994, and has granted a temporary exemption from such fees for daylight overdrafts incurred in the principal and interest accounts of these enterprises beyond that time.

The Board also indicated that it plans to study the effects of changing the timing of principal and interest payments in the accounts of Government-sponsored enterprises to eliminate overdrafts in those accounts, and will make a final decision on the future application of daylight overdraft penalty fees to Government-sponsored enterprises at a later date.

Printed on the following pages is the text of the Board's official notice regarding this matter. Questions may be directed to Donald R. Anderson, Manager, Accounting Department (Tel. No. 212-720-5250), or to Anthony Fressola, Chief, Accounting Control Division (Tel. No. 212-720-5803).

WILLIAM J. McDONOUGH,
President.

FEDERAL RESERVE SYSTEM

**Interpretation of the Payments System Risk Reduction Policy;
Daylight Overdrafts of Government-Sponsored Enterprises**

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Interpretation.

SUMMARY: As part of its payments system risk reduction program, the Board is adopting an interpretation of its Policy Statement on Payments System Risk. Under the payments system risk reduction program, government-sponsored enterprises that maintain accounts at Reserve Banks should not incur daylight overdrafts in these accounts and are not permitted to adopt a positive daylight overdraft net debit cap. Furthermore, the Board interprets the Policy Statement on Payments System Risk to include government-sponsored enterprises under the policy on daylight overdraft fees. Until October 13, 1994, fees on daylight overdrafts in accounts of government-sponsored enterprises will be waived. A temporary exemption from daylight overdraft fees is granted for daylight overdrafts in principal and interest accounts of government-sponsored enterprises. This interpretation supports the Board's payments system risk reduction program by providing a comprehensive policy towards daylight overdrafts incurred by government-sponsored enterprises while at the same time recognizing the unique nature of the fiscal agency relationship between the Federal Reserve and these entities.

DATES: Effective April 28, 1994.

FOR FURTHER INFORMATION CONTACT: Jeffrey C. Marquardt, Assistant Director (202/452-2360), Paul Bettge, Manager (202/452-3174), Division of Reserve Bank Operations and Payment Systems; Stephanie Martin, Senior Attorney (202/452-3198), Legal Division; for the hearing impaired only: Telecommunications Device for the Deaf, Dorothea Thompson (202/452-3544).

SUPPLEMENTARY INFORMATION:

Background

The term "government-sponsored enterprise" (GSE) is generally used to refer to corporations chartered by Congress to perform certain financial market functions deemed to be in the public interest. These entities include, but are not limited to, the Federal National Mortgage Association (Fannie Mae), the Federal Home Loan Mortgage Corporation (Freddie Mac), the Student Loan Marketing Association (Sallie Mae), and entities of the Federal Home Loan Bank System and the Farm Credit System. These GSEs are owned by private shareholders and their obligations are not guaranteed by the U.S. government.

Congress authorized the Reserve Banks to act as depositaries, custodians, and fiscal agents for these entities. Under agreements with the GSEs, the Reserve Banks issue and redeem the GSEs' debt and asset-backed securities over the Fedwire system, in addition to providing other payment services generally related to these fiscal agency services.

The Board's payments system risk (PSR) policies and guidelines have addressed daylight overdrafts by government-sponsored enterprises that maintain accounts with Federal Reserve Banks only in certain limited instances. In 1985, the Board determined that Federal Home Loan Banks should not be allowed a positive net debit cap and should be discouraged from incurring daylight overdrafts in their accounts with the Reserve Banks. In June 1986, the Board similarly determined that the Farm Credit System Banks should be discouraged from incurring overdrafts.

The Board has never addressed daylight overdrafts of other GSEs, including those for which the Reserve Banks act as fiscal agents in issuing and redeeming their securities. Further, when the Board approved in 1992 the policy of charging fees for daylight overdrafts beginning in April 1994, it did not address the question of whether GSEs would be subject to the fees. However, the policy did not exclude GSEs or any other class of account-holders from the fees.¹ In addition, in 1994, the Board adopted a penalty fee for daylight overdraft incurred by institutions that do not have regular discount window access, although GSEs were not included in this penalty fee policy.

The Federal Reserve is not obligated to provide intraday credit to the GSEs in the form of daylight overdrafts as part of its fiscal agency functions; indeed, the GSEs have

¹ The Board's policy statement on daylight overdraft fees states that "each Reserve Bank will charge a fee for average daily daylight overdrafts in Federal Reserve accounts [emphasis added]."

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generally agreed not to incur overdrafts in their accounts. However, many of the GSEs have nonetheless incurred daylight overdrafts. The Board believes that, with the advent of daylight overdraft fees for depository institutions on April 14, 1994, it is particularly important that the GSEs not be permitted unlimited free access to intraday Federal Reserve credit. Such access would represent a benefit not available to depository institutions and could serve to undermine the Board's payment system risk reduction program.

As a result, the Board interprets the Policy Statement on Payments System Risk to include GSEs under the policy on daylight overdraft fees. In addition, the Board has determined that a capital-based fee deductible, as permitted for depository institutions, will not be permitted for the GSEs. These entities do not have regular access to the discount window and should not be permitted the same access to intraday credit as depository institutions. However, because a number of these entities have not been formally subject to the PSR policy in the past and have not previously been explicitly advised that daylight overdraft fees would apply to their accounts, the Board has determined that they should be afforded some period within which to make the necessary adjustments to their payment systems and practices. As a result, daylight overdraft fees for daylight overdrafts in GSEs' accounts will be waived until October 13, 1994.

Furthermore, the Board recognizes that, in large part, the GSEs' daylight overdrafts are related to regular payments of

principal and interest (P&I) on securities that they issue through the Federal Reserve. These payments are initiated by the Reserve Banks, and the Federal Reserve's daylight overdraft posting rules specify that these payments will be made before 9:15 a.m. Eastern time. These posting times were primarily designed to grant depository institutions the benefit of P&I payments prior to debits being made to their accounts from their purchases of new issues of government securities. The GSEs typically do not fund debits to their accounts resulting from P&I payments until they issue new securities later in the day, causing daylight overdrafts in their Federal Reserve accounts.

To eliminate these daylight overdrafts, the Reserve Banks could delay making P&I payments on the GSEs' securities until sufficient funds were available in their accounts. This would likely require that the P&I payments be made later in the day. Delaying the P&I payments might increase the magnitude and duration of daylight overdrafts for the depository institutions that receive the corresponding credits.

For this reason, the Board is permitting a temporary exemption of overdrafts incurred in GSEs' P&I accounts (special accounts which are used only for the payment of principal and interest), until the potential benefits and drawbacks of shifting the timing of P&I payments can be analyzed. This analysis will be performed once the initial impact of daylight overdraft fees on depository institutions has been assessed. In addition, the

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Board has not ruled out future application of the daylight overdraft penalty fee to GSEs' daylight overdrafts.

Interpretation of the Policy Statement on Payments System Risk

Under the Board's payments system risk reduction program, government-sponsored enterprises that maintain accounts at Reserve Banks should not incur daylight overdrafts in these accounts and are not permitted to adopt a positive daylight overdraft net debit cap. Furthermore, the Board interprets the Policy Statement on Payments System Risk to include government-sponsored enterprises under the policy on daylight overdraft fees. A capital-based fee deductible is not permitted for government-sponsored enterprises. However, a temporary exemption from daylight overdraft fees is granted for daylight overdrafts in principal and interest accounts of government-sponsored enterprises. Fees on daylight overdrafts in accounts of government-sponsored enterprises will be waived until October 13, 1994.

By order of the Board of Governors of the Federal Reserve System, May 9, 1994.

Signed, William W. Wiles



William W. Wiles,
Secretary of the Board.
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