

INTERPRETATION OF BANKING ACT OF 1933

(Copies to be sent to all Federal reserve banks)

April 3, 1934.

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Gentlemen:

This refers to your letters of August 4, 1933, October 2, 1933, and January 23, 1934, regarding the question whether allowances made by a member bank to a customer in connection with the discharge of his obligation with respect to a banker's acceptance constitutes a payment of interest directly or indirectly on a deposit which is payable on demand in violation of Section 19 of the Federal Reserve Act as amended.

You state that, in consideration of the bank's agreeing to accept time drafts, the customers of the bank agree, expressly or impliedly, to pay to the bank or its successors or assigns the amount of each such acceptance on the last business day before its maturity or on demand at any time prior thereto, together with the amount of the bank's commission and the amount of all charges and expenses incurred by the bank in connection with the transaction. You further state that it sometimes happens that the customer desires to discharge his obligation before the last business day before the maturity of the acceptance, and that, in order to encourage such desire, the bank accepts payments at a discount rate based upon the number of days

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yet to run until the maturity, thus making an allowance for the unexpired period during which the customer, in the absence of a demand from the bank, might have retained his funds.

If the funds paid to the bank by the customer in such circumstances are not credited to his deposit account on the books of the bank but are applied immediately to the discharge of his obligation to place the bank in funds to retire the acceptances, it would seem that such funds do not constitute deposits and that, therefore, the prohibition upon the payment of interest on deposits payable on demand is not applicable. If, however, the funds are credited to the customer's deposit account and are not applied in discharge of the customer's obligation until the date of maturity of the acceptance, it is the view of the Board that a deposit arises. If such deposit is to be used to discharge the customer's obligation within 30 days or is otherwise payable within 30 days, it constitutes a demand deposit and an allowance or discount in connection with such deposit calculated according to the number of days remaining before maturity of the acceptance must be considered an indirect payment of interest in violation of the prohibition of Section 19 of the Federal Reserve Act upon the payment of interest on any deposit which is payable on demand.

Very truly yours,

(Signed) Chester Morrill,
Chester Morrill,
Secretary.