

X-9039

INTERPRETATION OF BANKING ACT OF 1933

(Copies to be sent to all Federal reserve banks)

November 26, 1934.

Mr. _____, President,
_____ National Bank of _____,
_____.

Dear Sir:

This refers to your letter of August 21, 1934, addressed to the Board's General Counsel, with regard to the interpretation of the ruling published on page 394 of the Federal Reserve Bulletin for June, 1934, as to the absorption of exchange or collection charges by member banks under the provisions of section 19 of the Federal Reserve Act. You state that the _____ clearing house banks are at present employing a uniform analysis of account formula which includes exchange charges and other out-of-pocket expenses and you request a ruling on the question whether the waiving of any exchange charges or other out-of-pocket expenses would be in violation of the law. It is understood that you wish to be informed whether any such exchange charges or other out-of-pocket expenses may lawfully be included in an analysis of an account which also includes a credit allowed the customer for interest or for the reasonable value of the account to the bank. In this connection, you also ask whether it would be permissible for the clearing house rules to be amended to provide for waiving of out-of-pocket charges for a nominal sum for

any one customer without regard for the amount of his balance, in order to eliminate the annoyance of inconsequential charges against an account.

Replying to your first question you are advised that the waiving of any exchange charges or other out-of-pocket expenses and the inclusion of such charges or expenses by a member bank in an analysis of an account which also includes a credit allowed the customer for interest or for the reasonable value of the account to the bank, would involve a payment of interest to the extent that such credit offsets such charges waived and absorbed by the bank, and would, accordingly, be in violation of the law if the deposit is payable on demand, except as indicated below.

The Federal Reserve Board has recently had occasion to consider whether member banks of the Federal Reserve System may lawfully operate in accordance with the provisions of a clearing house rule reading as follows:

"No bank shall make a regular practice of absorbing for any customer all exchange or collection charges or other out-of-pocket expenses incurred on behalf of such customer; but, in exceptional circumstances, when it would create friction or misunderstanding to charge a customer for isolated items of trivial amounts, the banks may absorb such individual items, including isolated exchange and collection charges and charges for telephone calls, telegrams and similar items, provided that the banks act in good faith and do not utilize the absorption of such items as a basis for soliciting accounts or attempting to obtain an advantage over competitors."

Where the amount of such items absorbed does not vary with or bear a substantially direct relation to the amount of the customer's balance, the absorption of such items can not be considered an indirect payment of interest within the meaning of section 19 of the Federal

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Reserve Act, unless such items are included in an analysis of accounts which involves their being offset in whole or in part by an analysis credit allowed to the customer for interest or the earning value of the account. Even where the bank analyzes accounts in this manner, it is believed that the absorption of isolated items of the character described above in trivial amounts may be disregarded in accordance with the rule that the law takes no notice of inconsequential matters. The Board, therefore, sees no objection to the adoption of a rule substantially in accordance with that quoted above.

Your letter suggests that a member bank be permitted to absorb such charges in amounts up to \$2.00 per month for any one customer in order to eliminate the annoyance of inconsequential charges against an account. While the Board does not feel that it would be advisable to prescribe any fixed amount of charges which might be absorbed under the above-quoted rule, it is believed that such a rule will afford a satisfactory basis for treatment of exchange charges and other out-of-pocket expenses by member banks which may see fit to operate under a rule of this kind.

Very truly yours,

(Signed) Chester Morrill
Chester Morrill,
Secretary.