FEDERAL DEPOSIT INSURANCE CORPORATION

12 C.F.R. Part 329

Interest on Deposits

AGENCY: Federal Deposit Insurance Corporation.

ACTION: Proposed Rule.

SUMMARY: The Board of Directors of the Federal Deposit Insurance Corporation ("FDIC") proposes to revise and simplify Part 329 of the FDIC's regulations, 12 C.F.R. Part 329 ("Interest on Deposits"). The proposal reflects changes made in the Federal Deposit Insurance Act ("FDI Act"), 12 U.S.C. §§ 1811-1831d. The FDIC is proposing two alternative responses to these changes. The first one ("Revision") is designed to maintain parity between Part 329 and proposed Regulation Q as recently published by the Board of Governors of the Federal Reserve System ("FRB"). See 51 Fed. Reg. 31 (1986). The second one is a simpler and more liberal rule ("Alternative Rule"). The FDIC specifically requests full comment both on the Revision and on the Alternative Rule.

DATE: Comments must be submitted on or before ________, 1986 [30 days after publication of notice in the Federal Register].

ADDRESS: Send comments to: Hoyle L. Robinson, Executive Secretary, Federal Deposit Insurance Corporation, 550 - 17th Street, N.W., Washington, D.C., 20429. Comments may be hand delivered to, and are available for reviewing in, Room 6108 on weekdays between the hours of 8:30 a.m. and 5:00 p.m.

FOR FURTHER INFORMATION CONTACT: Jules Bernard, Senior Attorney, Legal Division, Federal Deposit Insurance Corporation, 550 - 17th Street, N.W, Washington, D. C., 20429, 202-389-4171.

SUPPLEMENTARY INFORMATION: Prior to 1980, Congress directed the FDIC and the FRB to regulate interest rates that banks paid on deposits. The agencies did so in three ways. They enforced the law forbidding banks to pay interest on demand deposits. They set limits on the rates banks could pay on time and savings deposits. Finally, they regulated the way banks advertised the rates. See 12 U.S.C. §§ 371a, 371b, & 1828(g)(1); see also 12 C.F.R. Parts 217 (the FRB's Regulation Q) & 329 (the FDIC's rules).

In 1980 Congress transferred the authority to limit rates paid on time and savings deposits (but not the other two kinds of authority) from the two agencies to the Depository Institutions Deregulation Committee (DIDC). See 12 U.S.C. § 3502. The DIDC's rules superseded those of the agencies where the DIDC's rules differed from those that the agencies had adopted. See 12 C.F.R. Part 1204.

The DIDC and all its rules will expire on April 1, 1986. The agencies' rule-making authority will also change in significant ways on that date. Banks will still be forbidden to pay interest on demand deposits, however, and the

agencies will continue to have authority to regulate banks' advertising practices.[1]

The FDIC proposes two responses to these changes, presented in the alternative. One is the Revision. The Revision generally conforms to the FRB's proposed Regulation Q. The other is the Alternative Rule, which is somewhat more liberal than proposed Regulation Q. The FDIC seeks full comment on all aspects of the Revision and of the Alternative Rule. The FDIC specifically seeks a full discussion of the question whether it would be preferable to adopt the Revision or the Alternative Rule.

Ordinarily the FDIC provides a 60-day comment period for proposed regulations. See "Development and Review of FDIC Rules and Regulations," 1 FED. DEPOSIT INS. CORP. 5057, 5058 (May 21, 1979). Inasmuch as the statutory basis for Part 329 will be altered at the end of March, however, the FDIC considers that it is necessary to reduce the comment period on the proposed rule to 30 days.

I. The Revision.

A. The regulation.

1. Defining "demand deposit."

The Revision defines "demand deposit" to include:

--any deposit that has an original maturity or notice period of less than seven days, or regarding which the bank reserves less than seven days' notice of an intended withdrawal,[2] and

--any deposit that otherwise resembles a Money Market Deposit Account (MMDA) as currently defined by the DIDC, but that allows the depositor to

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[1] The FRB has issued a proposal to revise the advertising rules set forth in Regulation Q. See 51 Fed. Reg. 1379 (1986). The FDIC is not now proposing to make any changes in the advertising rules set forth in Part 329, except as may be necessary to eliminate obsolete provisions. The FDIC will consider issues related to advertising separately.

[2] Following the FRB's lead, the Revision establishes a seven-day notice period as the line of demarcation between demand deposits and other deposits. Part 329 is out of date in this respect. It speaks of a 14-day minimum term or notice period for time deposits, and of 14 days' reserved notice for most kinds of savings deposit. See 12 C.F.R. § 329.1(c), (d), & (e)(1)(iii). The DIDC has provided for time deposits with terms as short as seven days, however. Id. § 1204.121. Moreover, the DIDC only requires 7 days' reserved notice for NOW accounts (i.e., interest-bearing deposits that are accessible by negotiable or transferable orders of withdrawal) and for MMDAs. Id. §§ 1204.108(b)(4) & 1204.122(d). These accounts are both classed as "savings deposits" by Part 329. Id. § 329.1(e)(1)(iii).

exceed the number of third-party transfers or preauthorized payments that are allowed for MMDAs under the DIDC's current rules:[3] provided, that a deposit of this kind does not qualify as a "demand deposit" if the depositor is eligible to hold a NOW account.[4]

The Revision specifies that NOW accounts and ATS accounts[5] are not subject to the prohibition against paying interest on demand deposits. Strictly speaking, there is no need for this provision. These accounts may only be held by depositors that are eligible to hold NOW accounts. Accordingly, they do not qualify as "demand deposits," and are not subject to the prohibition in the first place. Nevertheless, the Revision includes this provision in order to maintain parity with proposed Regulation Q.[6]

The Revision, like proposed Regulation Q, makes provision for a special kind of account that "is subject to withdrawals by telephonic or data transmission order or instruction and which consists of funds the entire beneficial interest of which is held by a party eligible to hold a NOW account."[7] Unlike proposed Regulation Q, the Revision imposes a seven-day reserved-notice period on these accounts (herein referred to as "electronic NOW accounts").

The Revision deviates from proposed Regulation Q in this respect. The FDIC believes, however, that NOW accounts and electronic NOW accounts should be defined in essentially identical terms. Of course, the FDIC could eliminate the reserved-notice requirement in both cases. The FDIC seeks comment on

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[3] The limit is "six transfers per month or statement cycle (or similar period) of at least four weeks . . . and no more than three of the six such transfers may be by check, draft or similar order " Id. § 1204.122.

[4] Only natural persons, nonprofit organizations, and public units may hold NOW accounts. See 12 U.S.C. § 1832(a)(2).

[5] ATS accounts are defined by statute as "savings deposits" from which the depositor may make withdrawals "through payment to the bank itself or through transfer of credit to a demand deposit or other account pursuant to written authorization from the depositor to make such payments or transfers in connection with checks or drafts drawn upon the bank." Only natural persons are eligible to hold ATS accounts. Id. § 1828(g)(2).

[6] In this regard the Revision complies with the requirements of section 18(g)(1) of the FDI Act, which specifies: "[S]uch exceptions from this prohibition [against paying interest on demand deposits] shall be made as are now or may hereafter be prescribed with respect to deposits payable on demand in member banks by section 19 of the Federal Reserve Act, as amended, or by regulation of the Board of Governors of the Federal Reserve System." Id. § 1828(g)(1).

[7] The Revision provides that the rules governing eligibility for NOW accounts apply to electronic NOW accounts as well.

whether it would be preferable to adopt the Revision's approach, or to eliminate the reserved-notice requirement for both kinds of account, or to conform strictly with proposed Regulation Q as drafted by the FRB.

The Revision, like proposed Regulation Q, specifies that electronic NOW accounts are not subject to the prohibition against paying interest on demand deposits. In the Revision's case, this exemption is superfluous, since electronic NOW accounts (as defined by the Revision) can never qualify as "demand deposits." The Revision includes the exemption in order to follow proposed Regulation Q.

Because the Revision and proposed Regulation Q define electronic NOW accounts differently, however, the scope of the exemption provided by the Revision is a bit narrower than that afforded by proposed Regulation Q. The Revision's exemption only applies to deposits that have a seven-day notice requirement. Proposed Regulation Q affords the exemption to all electronic NOW accounts--even ones having having a reserved-notice period of less than seven days, and which therefore qualify as "demand deposits" under proposed Regulation Q. The FDIC seeks comment on whether it would be preferable to limit the exemption to electronic NOW accounts that have the reserved-notice requirement, or to extend the exemption to all electronic NOW accounts (including those that are payable on demand).

2. Repealing obsolete provisions.

The Revision drops the definitions of "savings deposit" and "time deposit," the rules for computing and paying interest on such accounts, and the rules for withdrawing funds from them. There is no need for these provisions after March 31, 1986. The Revision also drops the special advertising rules for accounts that once had a separate regulatory status, but which no longer do so.

The Revision drops the penalty for premature withdrawals from time deposits. The FDI Act will not require the FDIC to impose penalties of this kind after March 31, 1986; and the FDIC does not believe that penalties are needed merely to enforce the prohibition against paying interest on demand deposits. The FDIC considers that it is more appropriate to address possible violations of the prohibition on a case-by-case basis. In eliminating early-withdrawal penalties from Part 329, the Revision follows the FRB's proposed Regulation Q.[8]

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[8] The FRB has retained a more limited set of early-withdrawal penalties in proposed Regulation D. See 51 Fed. Reg. 27 (1986). The penalties are "safe-harbor" provisions that protect banks against the retroactive imposition of higher reserve requirements in certain cases. Proposed Regulation D says that if a bank allows a depositor to withdraw funds from a time deposit within the first six days, the FRB will not impose higher reserve requirements if the bank requires the depositor to pay a minimum penalty equal to seven days' simple interest on the amount withdrawn. In addition, if a nonpersonal time deposit has a stated maturity of one and one-half years or more, and if the bank allows the depositor to withdraw funds after six days but before one and

Banks may still impose early-withdrawal penalties for their own purposes, however. When they do, they must include a clear and conspicuous statement that they will impose a "substantial penalty" for early withdrawals.

In connection with the proposed modification of Part 329, the FDIC's Board of Directors proposes to withdraw its policy statement entitled "Premiums Not Considered Payment of Interest or Dividends," id. 5023 (March 24, 1970), which says that certain de minimis payments are not regarded as being the payment of "interest." The policy statement is obsolete in its present form, having been superseded by the DIDC's rules. See 12 U.S.C. § 1204.109. Moreover, the Board believes that there will soon be no need for this exception from the prohibition against paying interest on demand deposits, inasmuch as the Revision effectively exempts all consumer deposits from that prohibition. The FDIC specifically asks for comment on whether it is appropriate to eliminate the premium rule.

The Board also proposes to withdraw four General Counsel's opinions. Opinion No. 2, "Computation of Interest on Time and Savings Deposits," 1 FED. DEPOSIT INS. CORP. 5522 (Feb. 10, 1978) allows banks to divide the year into four equal quarters of 91 1/4 days each for the purpose of computing interest on nondemand deposits. Opinion No. 3, "Interest Rate Differential on Loans Secured by Time Deposits," id. 5523 (Feb. 16, 1978), speaks of the mandatory differential between the rate a bank charges on a loan secured by a deposit and the rate paid on the underlying deposit. Opinion No. 4, "Advertising of 6-Month Variable Rate (Money Market) Time Deposits," id. 5524 (undated) prescribes special rules for advertising six-month time deposits. Opinion No. 5, "Computation of Interest on Time and Savings Deposits During Leap Years," id. 5526 (Nov. 20, 1979), prescribes methods for computing interest during leap years. These opinions will all be obsolete.

3. Conforming with the language of proposed Regulation Q.

The Revision changes the language of certain provisions of Part 329 without altering their substance. These provisions are ones where the FDIC and the FRB have parallel requirements, and where the meaning and the regulatory consequences of the provisions are meant to be identical in Part 329 and Regulation Q, but where the language of the two regulations differs. The Revision modifies Part 329's language to conform with that proposed by the FRB simply for the sake of uniformity.

In this connection, the Revision adopts the FRB's definition of "interest." The change reflects the long-standing interpretation of the FDIC (and of the FRB). The Revision also replaces Part 329's descriptions of NOW and ATS accounts with those given by the FRB. None of these changes alters the substance of Part 329 in any way.

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[8] (cont.) one-half years after the date of deposit, the FRB will not impose higher reserve requirements if the bank requires the depositor to pay a minimum penalty equal to one month's simple interest on the amount withdrawn. Id. 27, 29 (1986).

B. Discussion.

There are a number of arguments in favor of the approach taken in the Revision. The Revision makes it clear that the same rules apply to all insured banks, both those that belong to the Federal Reserve System and those that do not. Accordingly, the Revision avoids creating any competitive or regulatory imbalances. At the same time, the Revision preserves the essential features of the current definition of "demand deposit." Accordingly, the Revision does not produce any significant disruption in the banking industry.

The FDIC's assessment and insurance rules both have special rules for "demand deposits." Banks may deduct 1/6 of their "demand deposits" from the assessment base; the assessment rules explicitly refer to the definition provided for that term in Part 329. See 12 C.F.R. § 327.03. In addition, IRAs, Keogh Plans, and public units are separately insured for "demand deposits" on one hand and "time and savings deposits" on the other. Id. §§ 330.8 & 330.10. The Revision does not affect the FDIC's assessments nor its insurance liabilities significantly.

Finally, the Revision reinforces the line of demarcation between transactions balances and less-volatile funds that the FRB has established in Regulation D. See id. Part 204.

On the other hand, this approach presents certain difficulties in interpretation. Like the present rule, the Revision provides that a nondemand deposit that belongs to a business enterprise is a "demand deposit" if the depositor may make more than the allowable number of transfers from it per month. It is not clear, however, what the consequences are when a bank allows its customers to violate the transfer limits. The account might well be regarded as a "demand deposit" ab initio,[9] and the bank would not pay any interest on it in the future. But it is not clear what effects--if any--would arise from the retroactive reclassification of the deposit.

The Revision (like the current regulation) can lead to strange results. For example, if a business enterprise uses its own computers to communicate with

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[9] The FRB has ruled that, if a bank authorizes a depositor to make more than six third-party transfers from an account opened as an MMDA, the account is a "transaction account" under Regulation D (which category excludes MMDAs), and has been so right from the beginning. On the other hand, if the depositor merely exceeds the permitted number of transfers from an MMDA in an occasional basis, and does so inadvertently and without explicit authorization from the bank, the FRB considers that the account remains an MMDA. If the depositor does so regularly, the bank must close the account--but the account, immediately prior to closing, is still regarded as an MMDA, at least under Regulation D. See 1 FED. RES. REG. SERVICE 1-285 (1983).

The FRB has not ruled on the status of such an account under Regulation Q. Presumably the FRB would follow the same line of analysis in order to preserve uniformity between Regulations D and Q. In order to maintain parity between Regulation Q and Part 329, the FDIC might well do the same.

its bank, and instructs the bank to transfer funds from its MMDA to its checking account, it may do so only six times per month. But if it persuades the bank to install an automated teller machine on its premises, and performs exactly the same transaction through the automated teller, the business enterprise may do so as often as it likes.

The Revision also continues a deficiency in the current rule in that the FDIC's examiners cannot immediately tell whether a deposit is a "demand deposit" or not. Depending on the circumstances, the examiner must consider not only the terms of the deposit contract, but also the depositor's conduct as well.

It should be noted that the Federal Home Loan Bank Board (FHLBB) is developing its own rules regarding the use of third-party transfers from interest-bearing accounts. If the FHLBB adopts a more liberal rule, S&Ls and Federal savings banks (which are subject to the FHLBB's rules) could have a competitive advantage over other banks.

II. The Alternative Rule.

A. The regulation.

1. Defining "demand deposit."

The Alternative Rule defines "demand deposit" as:

> any deposit from which the depositor may, as a matter of legal right, withdraw the funds from the bank upon demand: Provided, that the term "demand deposit" does not include a nonbusiness deposit.

The Alternative Rule defines the term "nonbusiness deposit" as one owned by an depositor that is specified in 12 U.S.C. § 1832(a)--i.e., a depositor that is eligible to hold a NOW account. In effect, the Alternative Rule treats all deposits owned by such depositors (whether payable on demand or not) as NOW accounts.[10] There does not seem to be any practical reason to maintain a special category of interest-free deposit for these depositors, since as a practical matter they can hold interest-bearing accounts that have all the powers of demand deposits.

In this regard, the Alternative Rule reaches the same result as proposed Regulation Q, but by a slightly different road. The Alternative Rule and

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[10] The FDI Act gives the FDIC explicit authority to define the term "demand deposit." 12 U.S.C. § 1828(g)(1). The FDI Act does not require the FDIC to adopt the same definition as the FRB: it merely provides that, if the FRB excepts any "deposits payable on demand" from the prohibition against paying interest on demand deposits, the FDIC may not impose that prohibition on nonmember banks in connection with such deposits. Id.

proposed Regulation Q both exclude NOW accounts and ATS accounts from the category "demand deposits." The Alternative Rule excludes electronic NOW accounts from that category as well. Proposed Regulation Q does not do so, but then exempts them from the prohibition against paying interest on demand deposits. The practical effect is the same in either case.

Insofar as other depositors are concerned, the Alternative Rule is more liberal than proposed Regulation Q. The Alternative Rule allows banks to pay interest on any deposit--no matter who the beneficial owner may be--so long as the deposit is not payable on demand. Accordingly, banks may pay interest on all reserved-notice deposits--even when the accounts offer unlimited third-party transfer powers, and even when the accounts are owned by businesses. Of course, the FRB might classify such accounts as "transaction accounts" under Regulation D, see 12 C.F.R. § 204.2(e), and could subject them to higher reserve requirements.

2. Other provisions.

The Alternative Rule omits all references to NOW accounts, electronic NOW accounts, and ATS accounts. Otherwise the Alternative Rule is the same as the Revision.

B. Discussion.

A principal benefit of the Alternative Rule is that it is simple and clear. Accordingly, it is easy for banks to understand, and for the FDIC to enforce.[11] The Alternative Rule should be helpful in removing artificial constraints on banking services, and make it possible for banks to price transaction services--and bid for transaction balances--explictly. Currently banks compensate depositors for such deposits, but in indirect ways--*e.g.*, by waiving fees. In addition, the current rules favor larger businesses over smaller ones. Larger businesses evidently find that it is cost-effective to use messengers to avoid the restrictions on third-party transfers from MMDAs, while smaller businesses find that it is not cost-effective to do so. The Alternative Rule eliminates any such bias against small businesses.

On the other hand, because the Alternative Rule does not limit third-party transfers from nondemand accounts, banks belonging to the Federal Reserve

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[11] The Alternative Rule fully implements the law forbidding banks to pay interest on demand deposits. When Congress adopted that law in 1935, Congress only spoke of deposits payable on demand. In the 1980's, Congress authorized depositors of all kinds--even for-profit business enterprises--to write checks drawn on nondemand accounts (*i.e.*, MMDAs). Congress did not limit the number of checks that a depositor may write on an MMDA. Congress only said that, if the number did not exceed three per month, the MMDA is not a "transaction account" under the FRB's Regulation D, and the bank does not have to post higher reserves. The DIDC has put an absolute ceiling on checks drawn on MMDAs; but that is a regulatory directive, not a statutory one.

System could suffer a competitive disadvantage if the FRB continues to impose limits on such transfers. It would also be possible under the Alternative Rule for banks to reduce the reserved-notice period for nondemand checking accounts to a very small interval--e.g., one day--in order to maintain technical compliance with the prohibition against paying interest on demand deposits. This procedure may be considered to be an evasion of the rule. Such an "evasion" is arguably more a matter of form than of substance. Even under current rules, banks do not have to invoke the reserved-notice period, and as a rule they do not do so.[12]

One additional effect of the Alternative Rule could be to shrink the class of "demand deposits" somewhat. Banks may subtract 1/6 of their "demand deposits"--as that term is defined in Part 329--from their assessment base. Id. § 327.03. The Alternative Rule could increase assessments for some banks.

REQUEST FOR COMMENT: The FDIC is proposing to adopt either the Revision or the Alternative Rule. Accordingly, the FDIC specifically asks for full comment on each one. The FDIC specifically seeks comment on which would be preferable to adopt, and the reasons for the choice. The FDIC also seeks comment on any other approaches that might be feasible.

OTHER MATTERS

Regulatory Flexibility Act statement. Both the Revision and the Alternative Rule merely simplify Part 329 and relax regulatory constraints. Accordingly, neither the Revision nor the Alternative Rule will have a significant economic impact on a substantial number of small entities. The provisions of the Regulatory Flexibility Act relating to an initial and final regulatory flexibility analysis (5 U.S.C. §§ 603, 604) are not applicable.

Paperwork Reduction Act statement. Neither the Revision nor the Alternative Rule will affect the record-keeping or reporting requirements imposed on insured banks, or affect any bank's competitive status. A cost/benefit analysis (including a small-bank impact statement) is not required.

Regulation Review Program. The FDIC has established a program for reviewing each of its regulations at least once every five years for the purpose of determining whether the regulation should be continued, revised, or terminated. See "Development and Review of FDIC Rules and Regulations," 1 FED. DEPOSIT INS. CORP. 5057 (1979). The FDIC has selected Part 329 for review under the FDIC's Regulation Review Program. See 50 Fed. Reg. 14247 (1985).

[12] The FDI Act now provides that, if a bank waives the reserved-notice period for one depositor, the bank must do so for all depositors. Id. § 1828(g)(2). This requirement is removed from the FDI Act on March 31, 1986.

The factors the FDIC must consider in making the determination are (a) the continuing need for the regulation; (b) alternative methods of accomplishing the purpose of the regulation; (c) the type and number of complaints or suggestions received; (d) the need to minimize the burden imposed on those affected by the regulation, especially small banks; (e) possible simplification or clarification of the regulation; (f) the need to eliminate overlapping and duplicative regulations or supervisory procedures; and (g) the length of time since the regulation was last evaluated and the extent to which technology, economic, and other factors have changed in the area affected by the regulation. See 1 FED. DEPOSIT INS. CORP. at 5059. These factors were all taken into consideration during the development of each alternative presented in the proposed rule (i.e., the Revision and the Alternative Rule).

LIST OF SUBJECTS IN 12 C.F.R. Part 329: Advertising; Banks, banking; Federal Deposit Insurance Corporation; Interest rates.

1. For the reasons set out in the preamble, the Board of Directors of the Federal Deposit Insurance Corporation proposes to revise Part 329 of title 12 of the Code of Federal Regulations to read as follows:

PART 329--INTEREST ON DEPOSITS

Sec.
§ 329.0 Scope.
§ 329.1 Definitions.
§ 329.2 Payment of interest.
§ 329.3 Advertising.
§ 329.101 Applicability of § 329.2(b).

AUTHORITY: Secs. 9 and 18, Pub. L. No. 797, 64 Stat. 881, 891 (12 U.S.C. 1819 and 1828); secs. 302(b) and 303, Pub. L. No. 96-221, 94 Stat. 146 (12 U.S.C. 1828(g) and 1832(a)).

§ 329.0 Scope.

This part applies to any deposit which is payable within the States of the United States or the District of Columbia, or which is directly or indirectly accessible by check, draft, or order payable within the States of the United States or the District of Columbia, which check, draft or order is drawn on an account maintained at a bank office located within the States of the United States or the District of Columbia. An "international banking facility time deposit," as defined by the Board of Governors of the Federal Reserve System, 12 C.F.R. § 204.8(a)(2), is not a "deposit" within the meaning of this part.

§ 329.1 Definitions.

As used in this Part 329--

(a) The term "bank" includes:

(1) any State bank, as defined in section 3(a) of the Federal Deposit Insurance Act, 12 U.S.C. § 1813(a), the deposits in which are insured by the Corporation, and which is not a member of the Federal Reserve System;

(2) any State branch of a foreign bank, the deposit obligations in which branch are insured by the Corporation; and

(3) any noninsured bank in a State if the total amount of time and savings deposits held in all such banks in the State, plus the total amount of deposits, shares, and withdrawable accounts held in all building and loan, savings and loan, and homestead associations (including cooperative banks) in the State which are not members of a Federal home loan bank, is more than 20 per centum of the total amount of such deposits, shares, and withdrawable accounts held in all banks and building and loan, savings and loan, and homestead associations (including cooperative banks) in the State.[1]

(b) The term "demand deposit" includes any deposit that:

(1) has an original maturity or required notice period of less than seven days;

(2) represents funds regarding which the bank does not reserve the right to require at least seven days' written notice prior to withdrawal or transfer of any funds in the account; or

(3) represents funds regarding which the bank has reserved the right to require at least seven days' notice prior to withdrawal or transfer of any funds in the account, and from which, under the terms of the deposit contract or by practice of the depository institution, the depositor is permitted or authorized to make more than six transfers per month or statement cycle (or similar period) of at least four weeks to another account of the depositor at the same institution, to the institution itself, or to a third party by means of preauthorized, automatic or telephonic or data transmission agreement, order or instruction and no more than three of the six such transfers may be by check, draft or similar order (including debit card or transfer at an automatic teller machine or remote service unit) drawn by the depositor: Provided, that such a deposit shall not be deemed to be a "demand deposit" if the entire beneficial interest of the deposit is held by a party that is eligible to hold a NOW account as prescribed by 12 U.S.C. § 1832(a).

(c) The term "interest" means any payment to or for the account of any depositor as compensation for the use of funds constituting a deposit. A bank's absorption of expenses incident to providing a normal banking function or its forbearance from charging a fee in connection with such a service is not deemed the payment of "interest."

The following State satisfies this criterion: Massachusetts.

(d) The term "NOW account" means an account authorized by 12 U.S.C. § 1832(a) on which the bank has reserved the right to require at least seven days' notice prior to withdrawal or transfer of any funds in the account but only if the account consists of funds in which the entire beneficial interest is held by a party eligible to have such an account as prescribed by 12 U.S.C. § 1832(a).

(e) The term "ATS account" means a deposit subject to automatic withdrawals or transfers authorized by 12 U.S.C. § 1828(g)(2), and on which the bank has reserved the right to require at least seven days' notice prior to withdrawal or transfer of any funds in the account. Under that paragraph, a bank may permit withdrawals to be made automatically from a deposit that consists only of funds in which the entire beneficial interest is held by one or more individuals through payment to the bank itself or through transfer of credit to a demand deposit or other account pursuant to written authorization from the depositor to make such payments or transfers in connection with checks or drafts drawn on the bank.

§ 329.2 Payment of interest.

(a) Except as provided in subsections (b) and (c), no bank shall, directly or indirectly, by any device whatsoever, pay interest on any demand deposit.

(b) The prohibition expressed in subsection (a) does not apply to:
(1) any NOW account; or
(2) any account on which the bank has reserved the right to require at least seven days' notice prior to withdrawal or transfer of any funds in the account but which is subject to withdrawals by telephonic or data transmission order or instruction and which consists of funds the entire beneficial interest of which is held by a party eligible to hold a NOW account.

(c) The prohibition expressed in subsection (a) does not apply to any ATS account.

§ 329.3 Advertising

Every advertisement shall be governed by the following rules:

(a) Annual rate of simple interest. Interest rates shall be stated in terms of annual rates of simple interest. In no case shall a rate be advertised which is in excess of the applicable maximum rate for the particular deposit.

(b) Percentage yields based on 1 year. Where a percentage yield achieved by compounding interest during 1 year is advertised, the annual rate of simple interest shall be stated with equal prominence, together with a reference to the basis of compounding.

(c) Percentage yields based on periods in excess of 1 year. No advertisement shall include any indication of a total percentage yield, compounded or simple,

based on a period in excess of a year, or an average annual percentage yield achieved by compounding during a period in excess of a year.

(d) Time or amount requirements. If an advertised rate is payable only on deposits that meet time or amount requirements, such requirements shall be clearly and conspicuously stated. Where the time requirement for an advertised rate is in excess of a year, the required number of years for the rate shall be stated with equal prominence, together with an indication of any lower rate or rates that will apply if the deposit is withdrawn at an earlier maturity.

(e) Profit. The term "profit" shall not be used in referring to interest paid on deposits.

(f) Accuracy of advertising. No insured nonmember bank shall make any advertisement relating to the interest paid on deposits which is inaccurate or misleading or which misrepresents its deposit contracts.

(g) Solicitation of deposits for banks. Any person or organization which solicits deposits for a bank shall be bound by the rules contained in this section with respect to any advertisement relating to such deposits. No such person or organization shall advertise a percentage yield on any deposit it solicits for a bank which is not authorized to be paid and advertised by such bank.

(h) Withdrawal penalties. Any advertisement relating to the interest paid on any deposit regarding which the bank imposes a penalty for withdrawal prior to the deposit's maturity shall include a clear and conspicuous statement that in the event the depositor is allowed to withdraw all or part of his deposit before maturity, a "substantial penalty" will be imposed.

§ 329.101 Applicability of § 329.2(b).

(a) Any organization that is not organized for profit and that is described in paragraphs 501(c)(3) through (13) and (19) and section 528 of the Internal Revenue Code of 1954 (26 U.S.C. 501(c)(3)-(13) & (19), & 528) is eligible to hold a NOW account. Actual Internal Revenue Service documentation of tax-exempt status is not required to meet eligibility requirements; it is merely an aid in making eligibility determinations.

(b) It is impracticable to distinguish between NOW accounts that are used for personal purposes and NOW accounts that are used for business purposes (*e.g.*, by sole proprietorships). The rule set forth in § 329.2(b) applies to all NOW accounts--including NOW accounts that are used for business purposes.

(c) The rule set forth in § 329.2(b) applies to NOW accounts that represent funds held in a fiduciary capacity (whether the fiduciary is a natural person or otherwise) if all the beneficiaries are natural persons.
(d) Subsections (a), (b), and (c) also apply to any account described in § 329.2(b)(2).

2. In the alternative, for the reasons set out in the preamble, the Board of Directors of the Federal Deposit Insurance Corporation proposes to revise Part 329 of title 12 of the Code of Federal Regulations to read as follows:

PART 329--INTEREST ON DEPOSITS

Sec.
§ 329.0 Scope.
§ 329.1 Definitions.
§ 329.2 Payment of interest.
§ 329.3 Advertising.
§ 329.101 Eligibility to hold a "nonbusiness deposit."

AUTHORITY: Secs. 9 and 18, Pub. L. No. 797, 64 Stat. 881, 891 (12 U.S.C. 1819 and 1828); secs. 302(b) and 303, Pub. L. No. 96-221, 94 Stat. 146 (12 U.S.C. 1828(g) and 1832(a)).

§ 329.0 Scope.

This part applies to any deposit which is payable within the States of the United States or the District of Columbia, or which is directly or indirectly accessible by check, draft, or order payable within the States of the United States or the District of Columbia, which check, draft or order is drawn on an account maintained at a bank office located within the States of the United States or the District of Columbia. An "international banking facility time deposit," as defined by the Board of Governors of the Federal Reserve System, 12 C.F.R. § 204.8(a)(2), is not a "deposit" within the meaning of this part.

§ 329.1 Definitions.

As used in this Part 329--

(a) The term "bank" includes:
(1) any State bank, as defined in section 3(a) of the Federal Deposit Insurance Act, 12 U.S.C. § 1813(a), the deposits in which are insured by the Corporation, and which is not a member of the Federal Reserve System;
(2) any State branch of a foreign bank, the deposit obligations in which branch are insured by the Corporation; and
(3) any noninsured bank in a State if the total amount of time and savings deposits held in all such banks in the State, plus the total amount of deposits, shares, and withdrawable accounts held in all building and loan, savings and loan, and homestead associations (including cooperative banks) in the State which are not members of a Federal home loan bank, is more than 20 per centum of the total amount of such deposits, shares, and withdrawable accounts held in all banks and building and loan, savings and loan, and homestead associations (including cooperative banks) in the State.[1]

[1] The following State satisfies this criterion: Massachusetts.

(b) The term "demand deposit" means any deposit from which the depositor may, as a matter of legal right, withdraw the funds from the bank upon demand: Provided, that the term "demand deposit" does not include a nonbusiness deposit.

(c) The term "interest" means any payment to or for the account of any depositor as compensation for the use of funds constituting a deposit. A bank's absorption of expenses incident to providing a normal banking function or its forbearance from charging a fee in connection with such a service is not deemed the payment of "interest."

(d) The term "nonbusiness deposit" means an account that consists of funds in which the entire beneficial interest is held by one or more parties specified in 12 U.S.C. § 1832(a)(2).

§ 329.2 Payment of interest.

No bank shall, directly or indirectly, by any device whatsoever, pay interest on any demand deposit.

§ 329.3 Advertising

Every advertisement shall be governed by the following rules:

(a) Annual rate of simple interest. Interest rates shall be stated in terms of annual rates of simple interest. In no case shall a rate be advertised which is in excess of the applicable maximum rate for the particular deposit.

(b) Percentage yields based on 1 year. Where a percentage yield achieved by compounding interest during 1 year is advertised, the annual rate of simple interest shall be stated with equal prominence, together with a reference to the basis of compounding.

(c) Percentage yields based on periods in excess of 1 year. No advertisement shall include any indication of a total percentage yield, compounded or simple, based on a period in excess of a year, or an average annual percentage yield achieved by compounding during a period in excess of a year.

(d) Time or amount requirements. If an advertised rate is payable only on deposits that meet time or amount requirements, such requirements shall be clearly and conspicuously stated. Where the time requirement for an advertised rate is in excess of a year, the required number of years for the rate shall be stated with equal prominence, together with an indication of any lower rate or rates that will apply if the deposit is withdrawn at an earlier maturity.

(e) Profit. The term "profit" shall not be used in referring to interest paid on deposits.

(f) Accuracy of advertising. No insured nonmember bank shall make any advertisement relating to the interest paid on deposits which is inaccurate or misleading or which misrepresents its deposit contracts.

(g) Solicitation of deposits for banks. Any person or organization which solicits deposits for a bank shall be bound by the rules contained in this section with respect to any advertisement relating to such deposits. No such person or organization shall advertise a percentage yield on any deposit it solicits for a bank which is not authorized to be paid and advertised by such bank.

(h) Withdrawal penalties. Any advertisement relating to the interest paid on any deposit regarding which the bank imposes a penalty for withdrawal prior to the deposit's maturity shall include a clear and conspicuous statement that in the event the depositor is allowed to withdraw all or part of his deposit before maturity, a "substantial penalty" will be imposed.

§ 329.101 Eligibility for "nonbusiness deposits."

(a) Any organization that is not organized for profit and that is described in paragraphs 501(c)(3) through (13) and (19) and section 528 of the Internal Revenue Code of 1954 (26 U.S.C. 501(c)(3)-(13) & (19), & 528) is eligible to hold a "nonbusiness deposit." Actual Internal Revenue Service documentation of tax-exempt status is not required to meet eligibility requirements; it is merely an aid in making eligibility determinations.

(b) It is impracticable to distinguish between "nonbusiness deposits" that are used for personal purposes and "nonbusiness deposits" that are used for business purposes (e.g., by sole proprietorships). Accordingly, the term "nonbusiness deposit" includes all deposits that are held by a depositor listed in 12 U.S.C. § 1828(a)(2)--including "nonbusiness deposits" that are used for business purposes.

(c) Funds held in a fiduciary capacity (whether the fiduciary is a natural person or otherwise) may be held in the form of "nonbusiness deposits" if all the beneficiaries are natural persons.

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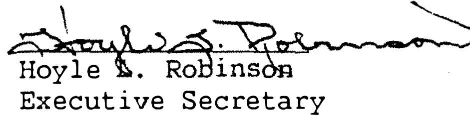
By order of the Board of Directors this __ day of January, 1986.

Federal Deposit Insurance Corporation



Hoyle L. Robinson
Executive Secretary

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