Reserve Requirements and Interest on Deposits

Summary: This bulletin transmits revised Examination Handbook Sections 561, Reserve Requirements (Regulation D), and 1420, Interest on Deposits. The revisions incorporate changes to the examination procedures as a result of amendments to Regulation D and OTS Regulation 12 CFR Part 561 that create a uniform six-transfer limit for savings accounts. This bulletin rescinds RB 37-33 dated March 26, 2009.

For Further Information Contact: Your Office of Thrift Supervision (OTS) Regional Office or Suzanne McQueen in the Compliance and Consumer Protection Division of OTS, Washington D.C. at (202) 906-6459. You may access this bulletin and the Examination Handbook at our web site: www.ots.treas.gov.

SUMMARY OF CHANGES

The Office of Thrift Supervision is issuing revised Examination Handbook Sections 561, Reserve Requirements, and 1420, Interest on Deposits. Change bars in the margins of the handbook sections indicate revisions. OTS is amending its definition of “Money Market Deposit Account” (MMDA) in 12 C.F.R. § 561.28 to create a uniform limit of six transfers a month for savings accounts, whether the transfers have been made by check, debit card transfer, or similar order payable to third parties. This amendment brings OTS regulations into conformity with the Federal Reserve Board (FRB) amendments to Regulation D (Reserve Requirements of Depository Institutions)1 and the Federal Deposit Insurance Corporation’s amended definition of “demand deposits.”2 The OTS amendment is effective immediately.

Prior to the FRB amendment, Regulation D treated transfers to third parties made by check, debit card, or similar order differently than pre-authorized or automatic transfers. There was, and still is, an overall limit of six transfers a month, but the FRB found that the three transfer limit was no longer logical in light of technological advances. OTS agrees. In addition, the FRB issued its annual indexing and low reserve tranche changes in October 2009.3 Consistent with these regulatory amendments, we revised Examination Handbook Sections 561 and 1420.

—Thomas A. Barnes
Deputy Director
Examinations, Supervision, and Consumer Protection

1 74 Fed. Register 25629 (May 29, 2009).
3 74 Fed. Register 52873 (Oct. 15, 2009)
Reserve Requirements (Regulation D)

Under the Depository Institutions Deregulation and Monetary Control Act of 1980, every depository institution that has transaction accounts or nonpersonal time deposits must maintain reserves on those deposits as prescribed by the Federal Reserve Board (the FRB). The FRB’s Regulation D, Reserve Requirements of Depository Institutions (12 CFR § 204), sets forth the rules related to reporting deposits and maintaining reserve balances. Depository institutions, whether members of the Federal Reserve System or not, must file a periodic report of deposits with the Federal Reserve Bank in its local Federal Reserve District.

The Federal Reserve uses the reports of deposits to accomplish the following goals:

- Define more precisely the components of the money supply.
- Set reserve requirements.
- In aggregate, help formulate monetary policy.

Errors in reporting or in maintaining proper reserve balances may adversely affect the conduct of monetary policy by the Federal Reserve and result in the following for institutions:

- Higher reserve requirements and a reduction in potential earnings.
- The assessment of reserve deficiency charges.
- A more frequent reporting requirement.

Regulation D is a highly complex regulation that requires careful study to master. We suggest that all regulators and institution management read the regulation. In addition, the comprehensive instructions for preparation of required reports contain information helpful in providing a good understanding of the regulation. See the Federal Reserve Board’s website for the forms and instructions: www.federalreserve.gov/boarddocs/reportforms/.

This Handbook Section only touches on the highlights of the regulation and focuses on frequently misunderstood areas.
Reserve Requirements

All depository institutions must hold a percentage of certain types of deposits as reserves in the form of vault cash, as a deposit in a Federal Reserve Bank, or as a deposit in a pass-through account at a correspondent institution. Reserve requirements currently are assessed on the depository institution’s net transaction accounts (mostly checking accounts).

Regulation D (12 CFR § 204.9) specifies the reserve requirement ratios for all depository institutions as shown in Table 1.

There is a zero percent reserve requirement on the first $10.7 million of the depository institution’s transaction accounts subject to the low reserve tranche ($55.2 million). The regulation requires the application of a three percent reserve requirement on the remainder of the low reserve tranche. Transaction accounts above the low reserve tranche have a ten percent reserve requirement.

The FRB establishes before the beginning of each year the amount of transaction accounts subject to the three percent ratio requirement. The FRB describes this adjustment as the low reserve tranche adjustment. The FRB also establishes on an annual basis the amount of reservable liabilities of each depository institution that is subject to a reserve requirement of zero percent. The FRB describes this adjustment as the reservable liability exemption. Reservable liabilities include transaction accounts, nonpersonal time deposits, and Eurocurrency liabilities as defined in § 19(b)(5) of the Federal Reserve Act. The reserve ratio on nonpersonal time deposits and Eurocurrency liabilities is zero percent.

The FRB uses deposit cutoff levels in conjunction with the reservable liability exemption to determine the frequency of deposit reporting. Nonexempt institutions are those with total reservable liabilities exceeding the amount exempted from reserve requirements. Exempt institutions are those with total reservable liabilities not exceeding the amount exempted from reserve requirements.

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<tr>
<td>Nonpersonal Time Deposits</td>
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<td>Eurocurrency Liabilities</td>
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¹ See 12 CFR § 204.3(a)(3) for a technical explanation of the allocation of exemption from reserve requirements.
TRANSACTION ACCOUNTS

Regulation 12 CFR § 204.2(e) defines transaction accounts with great specificity. Such accounts include the following:

- Demand deposits.

- Certain accounts on which the depository institution reserves the right to require at least seven days written notice before withdrawal or transfer of any funds. These accounts exclude those meeting the definition of savings accounts but include other accounts:
  - Subject to check, draft, negotiable order of withdrawal, or other similar item.
  - Subject to automatic withdrawal.
  - That permit a depositor to make more than six withdrawals per month or statement cycle.

- Deposits or accounts maintained with an agreement that permits the depositor to obtain credit directly or indirectly through the drawing of a negotiable or nonnegotiable check or similar device.

- Certain other accounts that the FRB determines by rule or order, to be transaction accounts.

Regulation 12 CFR § 204.2(f) defines Nonpersonal time deposits. Regulation D does not require the holding of reserves against these deposits.

Regulation 12 CFR § 204.2(h) defines Eurocurrency liabilities. Regulation D does not require the holding of reserves against these liabilities.

The computation of transaction accounts does not permit, with one exception, the netting of overdrafts in demand accounts and other transaction accounts [12 CFR § 204.3(e)].

Specific Rules for Certain Types of Savings Deposit Accounts

The definition of transaction accounts excludes savings deposits; however, savings deposits must meet detailed requirements to qualify for exclusion. Regulation D places restrictions on transfers and withdrawals from savings deposits such as passbook and statement savings accounts and money market deposit accounts (MMDAs).

Regulation D and Regulation 12 CFR § 561.28(a)(2) authorize only six transfers and withdrawals, or a combination of such, to another account of the depositor at the same depository institution or to a third party, during one of these time periods:
• Calendar month.

• Statement cycle of at least four weeks.

Institutions should report MMDAs and other savings deposits separately where called for according to reporting instructions for the specific reports.

Regulation D requires depository institutions to implement procedures either to prevent transfers in excess of the limitations or to monitor accounts on a periodic basis and contact customers who exceed these limits. Further, proper disclosure to customers of these limitations may serve to ensure compliance.

If the depositor exceeds account limitations the depository institution must take one of the following actions:

• Close the account and place the funds in another account that the depositor is eligible to maintain.

• Remove the transfer and draft capacities of the account.

**Frequency of Reporting**

Depository institutions must regularly submit reports of their deposits and other reservable liabilities. The Board screens depository institutions each year and assigns them to one of four deposit reporting panels (weekly reporters, quarterly reporters, annual reporters, or nonreporters). The panel assignment for annual reporters is effective in June of the screening year; the panel assignment for weekly and quarterly reporters is effective in September of the screening year.

In order to ease reporting burden, the FRB permits smaller depository institutions to submit deposit reports less frequently than larger depository institutions.

The FRB permits depository institutions with net transaction accounts above the reserve requirement exemption amount but with a sum of total transaction accounts, savings deposits, and small time deposits below a specified level (the “nonexempt deposit cutoff”) to report deposit data quarterly. The FRB requires certain large depository institutions to report weekly regardless of the level of their net transaction accounts if the sum of total transaction accounts, savings deposits, and small time deposits exceeds a specified level (the “reduced reporting limit”). The FRB adjusts the nonexempt deposit cutoff level and the reduced reporting limit annually, by an amount equal to 80 percent of the increase, if any, in the sum of total transaction accounts, savings deposits, and small time deposits of all depository institutions over the one-year period that ends on the June 30 prior to the adjustment.
From June 30, 2008 to June 30, 2009, the total transaction accounts, savings deposits, and small time deposits at all depository institutions increased 10 percent (from $6,461 billion to $7,126 billion). Accordingly, the FRB is increasing the nonexempt deposit cutoff level to $243.1 million for 2010. The FRB is also increasing the reduced reporting limit to $1.362 million for 2010.²

See the Reserve Maintenance Manual at [http://www.reportingandreserves.org](http://www.reportingandreserves.org) for current deposit reporting categories and deposit reporting categories. The Reserve Maintenance Manual also has information fundamental to understanding the reserve calculations and account maintenance for depository institutions that file the FR 2900.

**Reserve Balances**

Each depository institution can satisfy its reserve requirements with a combination of vault cash and balances held at a Federal Reserve Bank. Depository institutions may deposit their required reserve balances directly with a Federal Reserve Bank. Depository institutions that are not members of the Federal Reserve alternatively may elect to pass through their required reserve balances to the Federal Reserve through a correspondent. The correspondent may be the District Federal Home Loan Bank. The correspondent will pass through this required reserve balance dollar for dollar to the Federal Reserve Bank located in the depository institution’s Federal Reserve District. However, the FRB requires every depository institution that maintains transaction accounts or nonpersonal time deposits to file its report of deposits directly with the Federal Reserve Bank in its district. This requirement applies regardless of the manner the depository institution chooses to maintain required reserve balances.

The Federal Reserve Bank that receives the reports must notify the reporting depository institution of its reserve requirements. If a pass-through arrangement exists, the Federal Reserve Bank also will notify the correspondent that passes reserve balances through to the Federal Reserve of the depository institution’s required reserve balance.

**Reserve Deficiency Charges**

Deficiencies in a depository institution’s required reserve balance are subject to reserve deficiency charges. Regulation D authorizes Federal Reserve Banks to assess charges for deficiencies in required reserves.

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² Consistent with FRB practice, the nonexempt deposit cutoff level has been rounded to the nearest $0.1 million and the reduced reporting limit has been rounded to the nearest $1 million.
The charge for deficiencies is one percent per year above the primary credit rate in effect for borrowings from the Federal Reserve Bank. The rate used for borrowings is the rate on the first day of the calendar month when the deficiencies occurred. The Federal Reserve Banks assess charges using daily average deficiencies during each maintenance period.

A Federal Reserve Bank may, after consideration of the circumstances, permit an institution to eliminate a reserve deficiency and any charges accruing by maintaining additional reserves during subsequent reserve maintenance periods.

REFERENCES

**United States Code (12 USC)**

*Subchapter XIV - Bank Reserves*

§ 461 (19(a) - (c)) Reserve Requirements

**Code of Federal Regulations (12 CFR)**

*Chapter II - Federal Reserve System*

Part 204 Reserve Requirements of Depository Institutions (Regulation D) and Interpretations

*Chapter V - Office of Thrift Supervision*

Part 557 Deposits

§561.9 Certificate Account

§561.16 Demand Accounts

§561.28 Money Market Deposit Accounts

§561.29 Negotiable Order of Withdrawal Accounts

§561.42 Savings Account
Federal Reserve Board Amendments, Reporting Guidance, and Forms

74 FR 52873, October 15, 2009, Reserve Requirements of Depository Institutions

74 FR 25629, May 29, 2009 – Reserve Requirements of Depository Institutions

67 FR 67787, November 7, 2002 – Reserve Requirements of Depository Institutions


The following report forms and instructions are available online at the Federal Reserve Board’s website: http://www.federalreserve.gov/boarddocs/reportforms/

- Report of Transaction Accounts, Other Deposits and Vault Cash (Reporting Form FR 2900)
- Annual Report of Total Deposits and Reservable Liabilities (FR 2910a)
Reserve Requirements (Regulation D) Program

**EXAMINATION OBJECTIVES**

To determine that the savings association has procedures in place to comply with Regulation D.

To determine that the savings association complies with the reporting and reserve balance requirements of the regulation.

**EXAMINATION PROCEDURES**

**LEVEL I**

1. Identify whether the savings association prepares a report of deposits and submits it to the Federal Reserve Bank in its district.

2. Determine whether the association has operating procedures in existence and a system of internal controls to ensure compliance with the reporting requirements.

3. Obtain the association’s records detailing charges assessed by its Federal Reserve Bank. Also, review forms returned by the Federal Reserve Bank due to improper preparation and failure to comply with Regulation D. Determine whether the association makes corrections upon identification of problem areas.

4. Determine whether the association’s internal audit program provides adequate coverage to assure monitoring on a regular basis of the Regulation D reporting requirements. If the association does not have an internal audit function, a program of management reviews or self audits should include the reporting requirements.

5. Identify whether the association has procedures in place to identify and monitor the monthly transaction limitations on the following accounts to ensure that they do not exceed regulatory limits:
Reserve Requirements (Regulation D)

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- Regular passbook accounts.
- Statement savings accounts.
- Money market accounts.

6. Review Level II procedures and perform those necessary to test, support, and present conclusions derived from performance of Level I procedures.

LEVEL II

7. Review the two most recent reports of deposits to determine whether the items listed are accurate and properly classified.

8. Perform a limited review of all line items on the report of deposits.

9. Perform a review and evaluation of the savings association’s internal controls for Regulation D reporting compliance. Typical internal controls include independent review and verification of forms for accuracy before submission and the maintenance of proper supporting documentation.

10. Ensure that your review meets the Objectives of this Handbook Section. State your findings and conclusions, and appropriate recommendations for any necessary corrective measures, on the appropriate work papers and report pages.
LEVEL III

11. If you note substantive exceptions in Level I examination procedures 1-5, perform a detailed review of all line items on the report of deposits. Reconcile the form line items with the general ledger accounts for the specific period under review.

EXAMINER’S SUMMARY, RECOMMENDATIONS, AND COMMENTS
Compliance Laws and Regulations

Interest on Deposits

In 1993, the OTS made numerous changes to its regulations pursuant to the adoption of Regulation DD implementing the Truth in Savings Act, and the actions taken under the Regulatory Review Program. To reduce regulatory burden, the OTS reviewed its regulations to identify those provisions which were unnecessary and onerous. Sections pertaining to premiums, give-aways, advertising, and disclosures on fixed term accounts have either been removed or amended, as reflected in the revised narrative and examination procedures for this section of the handbook.

The effective annual yield formula previously used to determine the amount of interest paid on deposits has been replaced by the Annual Percentage Yield calculation contained in Regulation DD. In addition, Regulation DD restricts the method by which institutions determine the account balance for interest calculation purposes. Refer to section 1365 of this handbook for discussion on Regulation DD.

While many of the deposit restrictions, such as mandatory early withdrawal penalties, are not included in the OTS’s regulations, it should be noted that associations under the OTS’s jurisdiction are subject to the FRB reserve requirements set forth in Regulation D. In this regard for example, the presence and amount of early withdrawal penalties will affect the classification of deposits for reserve purposes.

Note: Compliance with Regulation D is currently covered during safety and soundness examinations. For examination procedures, see Examination Handbook, Section 561.

Requirements

Accounts

Federally chartered savings associations may issue demand deposit accounts and savings accounts for indefinite or fixed terms. Savings associations are also authorized to issue Money Market Deposit Accounts (MMDAs) and negotiable order of withdrawal accounts (NOWs) by 12 U.S.C. 1464(b)(1) and 12 U.S.C. 1832, respectively. There are no interest-rate ceilings on any accounts offered by savings associations and under OTS regulations there are no requirements for early withdrawal penalties. (The OTS believes, however, that early withdrawal penalties are useful in maintaining stability in all classes of Certificate of Deposits (CDs).)

Following is a list of the authorized types of accounts and the requirements associated with each:
1. Regular Savings Account (Passbook Account) – Section 561.42 provides that a savings account is any withdrawable account, except a demand account, a tax and loan account, a note account, a United States Treasury general account, or a United States Treasury time deposit-open account. There are essentially no specific limitations on these accounts imposed by OTS, with the exception that the savings association must reserve the right to require at least seven days' notice prior to withdrawal. These accounts must, however, meet certain requirements to qualify for lower reserve requirements as a savings account under Regulation D.

2. Fixed-term Account (Certificate Account) – Pursuant to §563.7, a certificate account must have a term of at least seven days. (Note: Accounts with fixed terms of less than seven days would be considered a demand deposit.)

An association may prohibit withdrawal of any portion of a certificate account prior to maturity. An association may not, however, restrict withdrawal or impose an early withdrawal penalty under the following circumstances:

- After the death of an account owner, if the withdrawal is requested by any other owner of the account or by the authorized representative of the decedent’s estate; or

- After an account owner is determined by a court or other administrative body of proper jurisdiction to be legally incompetent, if the account was issued before the date of such determination and not extended or renewed after that date.

3. Money Market Deposit Account (MMDA) – These accounts can be made available to any depositor, including individuals, corporations, government entities, and not-for-profit organizations. The association must reserve the right to require seven days' notice prior to withdrawal.

Pursuant to §561.28(a)(2), depositors are restricted to no more than six transfers per calendar month or statement cycle of at least four weeks by means of preauthorized, automatic, telephonic, or data transmission agreement, order, or instruction to another account of the depositor at the same insured association, to the association itself, or to a third party. These six transfers may be by check, draft, debit card, or similar order made by the depositor and payable to third parties. The depositors may, however, make unlimited transfers for the purpose of repaying loans and associated expenses at the association, for interaccount transfers in person or at an ATM from the MMDA account to accounts of the same account holder at the same association, and for cash or check withdrawals made in person, by mail, messenger, ATM, or telephone (via check mailed to the depositor).

In order to ensure that these requirements are met the association must either prevent transfers in excess of the limitations or adopt procedures to monitor transfers after-the-fact. In the second case, the association must take necessary steps to ensure that the excessive transfers do not continue. In the event that a depositor continues to make transfers in excess of the limitations subsequent to...
being contacted by the association in that regard, the association must either restrict access to the account or transfer the funds into another account the depositor is eligible to maintain.

4. Negotiable Order of Withdrawal Account (NOW) – NOW accounts may only be held by one or more individuals, government entities depositing public funds, and not-for-profit organizations operated primarily for religious, philanthropic, charitable, educational, political, or other similar purposes. These eligible “not for profit” organizations are described in §§501(c)(3) through (13), 501(c)(19), or 528 of the Internal Revenue Code. The Internal Revenue Service (IRS) has ruled that a nonprofit housing organization created to aid low and moderate income families may qualify for a tax exemption under §501(c)(3), and pursuant to this ruling the IRS has deemed many public housing authorities eligible for such exemption. Sole proprietorships and unincorporated businesses owned by a husband and wife are considered to be for the benefit of “one or more individuals” for purposes of eligibility for NOW accounts.

The association must reserve the right to require at least seven days’ notice prior to withdrawal or transfer of any funds in the account. A depository institution is authorized by 12 USC 1832 to permit the eligible owner, as described above, to make withdrawals from these accounts by negotiable or transferable instruments for the purpose of making transfers to third parties. Any depository institution which violates §1832 could be subject to a fine of $1,000 for each violation.

5. Checking Accounts (Demand Deposit Accounts) – Federal savings associations are authorized to issue demand deposits accounts by §§545.11 and 545.12, but restricted from paying interest on such deposits by §545.12 (b). They may be issued to any person.

Section 561.16 defines the term “demand accounts” to mean non-interest bearing demand deposits that are subject to check or to withdrawal or transfer on negotiable or transferable order to the savings association and which are permitted to be issued by statute, regulation or otherwise and are payable on demand as provided in §563.6(b).

Finders’ and Brokers’ Fees

As provided in §561.16(b), finders’ and brokers’ fees paid by savings associations for demand deposits will not be considered to be a payment of interest on the account if:

- the fee is a bonus in cash or merchandise to the insured association’s employees for participation in an account drive, contest or other incentive plan where the bonus is based on the total amount of deposits solicited; or

- if the fee is paid to a bona fide broker, which is considered to be one who is principally engaged in the business of brokering deposits, securities, or money market instruments, there is a written agreement between the broker and the association, and an officer of the broker gives written certification that no portion of the fee paid is directly or indirectly passed on to the depositor.
Lotteries

Section 410 of the National Housing Act of 1934, 12 USC 1730c, prohibits SAIF insured institutions from dealing in lottery tickets. The Home Owner’s Loan Act, 12 USC 1463(4)(e), prohibits federal savings associations from dealing in lottery tickets. These statutes define “lottery” to include any arrangement under which three or more persons (participants) advance money or credit to another in exchange for the possibility or expectation that one or more but not all participants (winners) will receive by reason of their advances more than the amounts they have advanced; the identity of the winners is determined by any means which includes a random selection; a game, race or contest. . . . The term “lottery ticket” includes any right, privilege, or possibility . . . of becoming a winner in a lottery.

Advertising

Interest on Deposits

The rules governing the advertising of interest on deposits are set forth in §230.8 of Regulation DD. Refer to section 1365 of this handbook for guidance.

REFERENCES

Laws

12 USC 1463(4)(e)  Home Owner’s Loan Act, Supervision of Savings Associations, Participation by savings associations in lotteries and related activities
12 USC 1464(b)(1)  Home Owner’s Loan Act, Federal Savings Associations Deposits and Related Powers
12 USC 1730c  National Housing Act of 1934, Insurance of Savings and Loan Accounts, Participation by insured institutions in lotteries and related activities
12 USC 1832  Federal Deposit Insurance Act, NOW Accounts: Transfers from Interest Bearing Savings Accounts, Prohibition on certain activities by depository institutions

Regulations

12 CFR 545  Office of Thrift Supervision, Department of the Treasury, Operations Regulation
12 CFR 561  Office of Thrift Supervision, Department of the Treasury, Definitions Regulation
12 CFR 563  Office of Thrift Supervision, Department of the Treasury, Operations Regulation
12 CFR 230  Federal Reserve System, Regulation DD
EXAMINATION OBJECTIVES

To determine whether the savings association is meeting all requirements for different types of accounts.

EXAMINATION PROCEDURES

1. Determine if the savings association is reserving the right to require at least the minimum advance notice on its accounts in its account contracts.

2. Determine through a review of savings association policies, procedures, and practices if any early withdrawal restrictions or penalties imposed by the savings association on certificate accounts are waived under the following circumstances:

   - After the death of an account owner, if the withdrawal is requested by any other owner of the account or by the authorized representative of the decedent’s estate; or
   - After an account owner is determined by a court or other administrative body of proper jurisdiction to be legally incompetent, if the account was issued before the date of such determination and not extended or renewed after that date.

3. Review the savings association’s policies, procedures, and practices to determine if they adequately restrict the number of transactions allowable in MMDA accounts.

4. Determine if the savings association allows only individuals, government entities (public units), or not-for-profit organizations operated primarily for religious, philanthropic, charitable, educational, political, or similar purposes to hold NOW accounts.
Interest on Deposits
Program

5. Determine if the savings association refrains from paying interest on demand deposit accounts.

6. Determine if the payment of finders’ or brokers’ fees on demand deposit accounts meet the limitations in order not to be considered interest payments.

EXAMINER’S SUMMARY, RECOMMENDATIONS, AND COMMENTS