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**Date:** August 1, 2000

**One Way Sweep Arrangement**

A federal savings association may offer its commercial deposit customers a "one way" sweep arrangement that would automatically transfer funds from the customer's checking account into its money market deposit account at the association. The association would not automatically transfer funds in the other direction.

**P-2000-10**

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**Office of Thrift Supervision**  
Department of the Treasury

**P-2000-10**

*Chief Counsel*

1700 G Street, N.W., Washington, DC 20552 • (202) 906-6251

August 1, 2000

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**Re: One Way Sweep Arrangement**

Dear [ ]:

This responds to your inquiry whether [ ] (the "Association") may offer its commercial deposit customers a "one way" sweep arrangement. The arrangement would automatically transfer funds above a preset level from a demand deposit checking account ("checking account") into a money market deposit account ("MMDA") at the Association. The Association would not, however, automatically transfer funds in the other direction. In brief, we conclude that the proposed activity is permissible.

**I. Background**

You describe a one way sweep deposit product the Association has developed and wishes to offer its commercial customers. You represent that the one way sweep will operate as follows. Each customer who uses this product will establish two separate deposit accounts at the Association, one a demand deposit checking account and the other an MMDA. The checking account will not pay interest. It will offer the depositor the ability to make unlimited transfers to third parties by check or electronic transfer.<sup>1</sup>

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<sup>1</sup> You specifically have not requested any opinion from OTS, and OTS does not express any opinion on the status of any deposits under Regulation D, 12 C.F.R. Part 204 (2000). You state that you will consult with the Federal Reserve Board staff on this issue.

The MMDA will pay interest at money market rates that may vary based on the amount of funds in the MMDA.<sup>2</sup> The depositor will choose the initial balance in the MMDA. The Association will reserve the right to require seven days' advance written notice of any withdrawal from the MMDA. The Association will limit the depositor to six withdrawals from its MMDA per month, and only three of those withdrawals can be by check, draft, debit card, or similar order payable to third parties. The depositor may also transfer funds out of the MMDA into the checking account but, depending on the transfer method, may be limited to six such transfers per month. Regardless of the six withdrawals limit, the depositor may make an unlimited number of transfers in any month from the MMDA to the checking account if the depositor (and not the Association) makes such transfers by mail, automated teller machine, in person, or by messenger. Telephone and online transfers from the MMDA to the checking account will count towards the limit of six monthly withdrawals, regardless of who makes them.

The Association will give the depositor the option of linking the MMDA and checking account as follows. The depositor will establish a maximum balance for its checking account.<sup>3</sup> If, at the end of any business day, funds in the checking account exceed the maximum balance that the depositor established, the Association will automatically transfer, or "sweep," that excess out of the checking account and into the depositor's linked MMDA.

You represent that the Association will never automatically transfer funds out of the MMDA into the checking account (hence the "one way" sweep), but the depositor will be able to make such transfers, subject to the limits described above. If a check or other charge is presented against the checking account when that account has insufficient funds to cover the charge, MMDA funds will not be available to cover the charge unless the depositor transfers MMDA funds into the checking account. In other words, the Association will not transfer funds out of the MMDA to cover the check or charge against the checking account. Rather, if the checking account is fully depleted and the depositor fails to move funds into the account, subsequent checks or debits will be subject to return for insufficient funds or to overdraft fees and interest, even if the MMDA has sufficient funds to cover the deficiency. In any event, the depositor's transfers will be subject to the limits on number and type described above.

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<sup>2</sup> The balance in the depositor's checking account will not affect the interest rates on the MMDA.

<sup>3</sup> You represent that the customer, in its sole discretion and based on its expectations regarding the flow of funds into and out of the checking account as account payables come due and as receivables are paid into the account, would establish a threshold, or maximum balance, amount for the checking account.

## II. Discussion

Federal law prohibits depository institutions from paying interest on demand accounts, such as checking accounts.<sup>4</sup> Depository institutions may pay interest or dividends on non-commercial deposits against which depositors may make withdrawals by negotiable or transferable instruments,<sup>5</sup> but that authority does not extend to commercial checking accounts. The differing legal treatment for different types of deposits gives rise to questions about the permissibility of transferring, or sweeping, funds from one type of deposit account to another.

In 1998, OTS opined that sweep arrangements are within the incidental powers of federal savings associations, although they are subject to certain legal restrictions.<sup>6</sup> In the 1998 Opinion, OTS reaffirmed that sweep arrangements, *i.e.*, sweeping excess funds out of non-interest bearing commercial checking accounts, using government securities repurchase agreements are permissible.<sup>7</sup> In the 1998 Opinion, OTS also opined that sweeps to a third party which then invests the swept funds in mutual funds are permissible.<sup>8</sup> OTS also discussed, but did not opine on, linked account sweeps, that is, arrangements that involve transfers of funds between two deposit accounts at one depository institution.<sup>9</sup> The Association's one way sweep is a type of linked account sweep.

Other federal banking agencies have considered linked account sweep arrangements. The Federal Deposit Insurance Corporation ("FDIC") considered a linked sweep arrangement between two accounts at one bank, a commercial demand deposit account and an interest bearing account, where automatic transfers would go between the accounts. In concluding that the arrangement would be

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<sup>4</sup> 12 U.S.C.A. § 1464(b)(1)(B)(i) (West Supp. 2000) (applicable to federal savings associations). The same prohibition applies to other depository institutions, although it is in different statutory provisions. See 12 U.S.C.A. § 371a (West 1989) (applicable to Federal Reserve System member banks ("member banks")). Because national banks are required to be member banks, 12 U.S.C.A. 222 (West 1989), national banks as well as state member banks are similarly prohibited from paying interest on commercial checking accounts. Non-member state banks are also similarly prohibited. See 12 U.S.C.A. § 1828(g) (applicable to non-member banks whose accounts are insured by the Federal Deposit Insurance Corporation).

<sup>5</sup> 12 U.S.C.A. § 1832(a)(1) (West 1989).

<sup>6</sup> See OTS Op. Chief Counsel (March 2, 1998) ("1998 Opinion") for a fuller discussion of the authority to engage in sweep arrangements, and relevant statutory and regulatory provisions.

<sup>7</sup> Id. at 5.

<sup>8</sup> Id. at 7 - 9.

<sup>9</sup> Id. at 5 - 7.

permissible only if it allowed no more than six transfers per month from an interest-bearing account into a checking account, the FDIC stated:

[The] bank could arrange for a commercial customer to sweep money out of a demand deposit and into an interest-bearing account whenever it liked. The difficulty comes when the customer wishes to sweep money out of the interest-bearing account. [12 CFR] Part 329 establishes the so-called ‘six-transactions rule.’ The rule says that a deposit will be deemed to be a ‘demand deposit’ – and the bank will not be allowed to pay interest on it – if the customer may withdraw funds from it more than six times per month by means of a standing order[.]<sup>10</sup>

Thereafter, the Federal Reserve Board (“FRB”) staff considered linked account sweep arrangements that automatically transfer funds from a savings account to a checking account but, at the sixth such transfer in one month, automatically transfer all savings account funds into the checking account.<sup>11</sup> Because the arrangements allow only six monthly automatic transfers, they restrict the extent to which savings account funds can be substituted for transaction account balances. The FRB staff concluded that the restriction is sufficient to prevent the savings accounts from becoming transaction accounts subject to reserve requirements.<sup>12</sup>

The Association’s proposed one way sweep arrangement does not allow automatic transfers out of a depositor’s MMDA into the depositor’s checking account. This fact limits the extent to which depositors can substitute MMDA funds for checking account funds. In other words, the one way sweep merely transfers funds *out of* a checking account *into* an MMDA. As the FDIC and FRB letters make clear, it is automatic transfers *out of* an MMDA *into* a checking or transaction account that cause concern about substituting MMDA funds for

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<sup>10</sup> FDIC Interp. Ltr. (December 6, 1993).

<sup>11</sup> FRB Unpublished Letters (February 7, 1995; August 1, 1995; August 30, 1995). While the FRB staff was considering reserve requirements and OTS in this opinion is considering the ban on interest on commercial checking accounts, the issues are similar. The FRB’s Regulation D, 12 C.F.R. Part 204 (2000), imposes reserve requirements on transaction accounts, such as checking accounts, but not on savings accounts, such as MMDAs. Interest payments are prohibited on commercial checking accounts, but are permissible on MMDAs. In both inquiries, an issue is the extent to which sweep arrangements that transfer funds between accounts invoke laws (reserve requirements or the interest ban) that apply to commercial checking accounts.

<sup>12</sup> *Id.*

checking or transaction account funds. The Association's one way sweep does not impermissibly substitute MMDA funds for checking account funds.

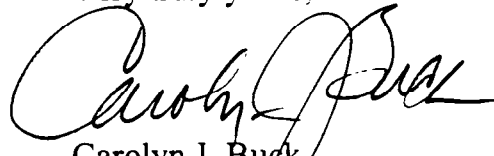
We note that in 1985, OTS's predecessor, the Federal Home Loan Bank Board ("FHLBB"), found impermissible a sweep arrangement that limited a depositor to six monthly automatic transfers from an MMDA to a checking account.<sup>13</sup> Since that time, however, the FDIC and FRB have found permissible linked account sweep arrangements that allow six monthly automatic transfers from an interest bearing account to a checking or transaction account, as discussed above. Given the developments in the banking industry since 1985 and the views of other federal banking agencies, OTS would likely find permissible sweep arrangements that allow no more than six automatic monthly transfers from an MMDA to a linked checking account.

For the reasons discussed herein, we conclude that the Association may provide its one way sweep arrangement to commercial depositors and that such an arrangement does not constitute paying interest on commercial demand deposits.

In reaching the foregoing conclusions, we have relied upon the factual information and representations you have provided to us, as set forth in the background discussion above. Our conclusions depend on the accuracy and completeness of those representations. Any material change in facts from those set forth herein could result in different conclusions.

If you have any questions regarding the foregoing, please contact Christine Harrington, Counsel (Banking and Finance), at (202) 906-7957.

Very truly yours,



Carolyn J. Buck  
Chief Counsel

cc: Regional Directors  
Regional Counsel

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<sup>13</sup> FHLBB Op. Gen. Couns. (October 21, 1985). The sweep arrangement in that opinion was factually distinct from both the Association's proposed one way sweep and the arrangements that the FDIC and FRB found permissible. For example, in the arrangement that the FHLBB reviewed, the linked accounts were marketed and operated as one account, with little or no need for the depositor to conduct any transactions with the MMDA, and any deposits into either the MMDA or checking account always flowed through the checking account.