

Payment of Interest on Demand Deposits

Summary Conclusion: Providing certain rewards to customers of savings associations who use Visa U.S.A. Inc. debit cards to access demand deposit accounts does not violate the HOLA § 5(b)(1)(B)(i) prohibition against payment of interest on demand deposits.

Date: May 29, 2003

Subjects: Home Owners' Loan Act/Savings Association Powers

P-2003-4



Office of Thrift Supervision
Department of the Treasury

1700 G Street, N.W., Washington, DC 20552 • (202) 906-6000

May 29, 2003

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Re: Payment of Interest on Demand Deposits

Dear Mr. Ballen:

This responds to your recent letter concerning whether providing certain rewards to customers of savings associations who use Visa U.S.A. Inc. ("Company") debit cards to access demand deposit accounts would violate the prohibition against payment of interest on demand deposits in section 5(b)(1)(B)(i) of the Home Owners' Loan Act ("HOLA"). We conclude that it would not.

Background

Under the arrangement the Company contemplates, its financial institution members could offer to some or all of their consumer and business cardholders the opportunity to participate in the rewards program. Under the program, cardholders could earn points for using their credit cards and debit cards in eligible transactions. The points could be redeemed for merchandise, gift or travel certificates, or other rewards. The points could not be redeemed for cash. The member financial institution would pay for the reward and arrange for it to be provided to the cardholder.

Eligible transactions for which points could be earned would generally be limited to signature-based card transactions that do not involve the use of a personal identification number to authorize the transaction. Certain other types of transactions, such as ATM transactions, balance transfers, and cash advances, would generally not be eligible to earn points. The purpose of the program would be to encourage cardholders to pay for eligible transactions with their cards, rather than cash, checks, or other payment devices.

Cardholders would earn points based on the amount spent in eligible transactions. Typically, a cardholder would earn one point for each dollar spent. After reaching a certain level of spending during a 12-month cycle, a particular cardholder might be eligible to earn additional points, such as two points for every dollar spent. A cardholder might also earn points for enrolling in the program or in connection with other special offers. The points would expire after a set period of months or upon card cancellation.

Discussion

HOLA section 5(b)(1)(B)(i) prohibits federal savings associations from paying interest on demand accounts.¹ While savings associations may offer to individuals, certain non-profit entities, and public units Negotiable Order of Withdrawal (“NOW”) accounts that allow these depositors to draw against interest-bearing deposits by negotiable or transferable instruments for the purpose of making transfers to third parties, associations may not offer these accounts to for-profit commercial entities.² OTS regulations define the term “demand accounts” to mean “non-interest-bearing demand deposits which 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.”³ Neither these statutes nor the OTS regulation defines the term “interest.”

The Board of Governors of the Federal Reserve System (“FRB”) and the Federal Deposit Insurance Corporation (“FDIC”), however, have defined the term “interest” for purposes of the statutory prohibitions on the payment of interest on demand deposits applicable to the institutions they regulate.⁴ The definition of interest the FRB and FDIC have promulgated is “any payment to or for the account of any depositor as compensation for the use of funds constituting a deposit.”⁵ These agencies each have also promulgated interpretive rules providing that “premiums, whether in the form of merchandise, credit, or cash, given by [an institution] to a depositor” will not be considered the payment of interest on a demand deposit account under various circumstances, including when the

¹ 12 U.S.C.A. § 1464(b)(1)(B)(i) (West 2001).

² 12 U.S.C.A. § 1832(a) (West 2001).

³ 12 C.F.R. § 561.16 (2003).

⁴ Those statutes are section 19(i) of the Federal Reserve Act, 12 U.S.C.A. § 371a (West 2001), and section 18(g) of the Federal Deposit Insurance Act, 12 U.S.C.A. § 1828(g) (West 2001).

⁵ 12 C.F.R. § 217.2(d) (2003) (FRB); 12 C.F.R. § 329.1(c) (2003) (FDIC).

premium “is not, directly or indirectly related to or dependent on the balance in a demand deposit account and the duration of the account balance.”⁶

OTS has previously indicated that it takes a similar approach to the permissibility of the payment of premiums on demand deposit accounts as the FRB and FDIC. In the preamble to its 1997 rule on Deposits, OTS explained:

[The] FRB and the FDIC recently revised their interpretive guidance to permit regulated institutions to pay any premium that is not, directly or indirectly, related to or dependent on the balance in a demand deposit account and the duration of the account balance. [citations omitted] While OTS has no interpretive rule specifically addressing premiums, OTS agrees that premiums under such circumstances are not interest and will generally follow the FRB and FDIC interpretations on this point.⁷

Both the FRB and the FDIC have recently concluded that the rewards that would be offered under the Company’s program would not constitute the prohibited payment of interest on demand deposits, but rather permissible premiums. The FRB reasoned that the rewards would be based solely on the dollar value of purchases and services in eligible transactions or on participation in special offers that have no relationship to the balance in a demand deposit account or the duration of that account.⁸ Similarly, the FDIC reasoned that the rewards would not be compensation for the use of funds in a deposit account or based on the duration of the account balance but rather, but would be based on the nature and value of the cardholder’s transactions using the Company’s card.⁹

OTS likewise concludes that providing certain rewards to customers who use the Company’s cards to access demand deposit accounts would not violate the prohibition against payment of interest on demand deposits. The rewards would not be directly or indirectly related to or dependent on the balance in a demand deposit account and the duration of the account balance. Rather, the rewards would be based on how much the customer used the Company’s card for eligible transactions.

⁶ 12 C.F.R. § 217.101 (2003) (FRB); 12 C.F.R. § 329.103 (2003) (FDIC).

⁷ 62 Fed. Reg. 54,759, 54,760 (October 22, 1997)

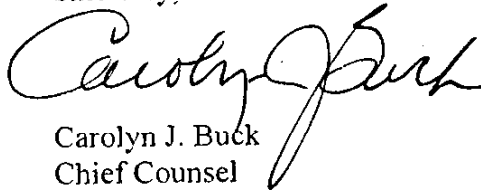
⁸ Letter from Stephanie Martin, Associate General Counsel, FRB (February 27, 2003).

⁹ Letter from Michelle M. Borzillo, Counsel, Supervision and Legislation Section, FDIC (March 28, 2003).

In reaching this conclusion, we have relied on the factual information and materials you submitted to us as described in the Background discussion above. Our conclusions depend upon the accuracy and completeness of that information and those materials. Any material differences in the facts or circumstances from those submitted to us and described in this letter could result in different conclusions.

We trust that this is responsive to your inquiry. If you have further questions, please contact Richard Bennett, Counsel (Banking and Finance), at (202) 906-7409.

Sincerely,

A handwritten signature in black ink, appearing to read "Carolyn J. Buck". The signature is fluid and cursive, with a large, sweeping flourish at the end.

Carolyn J. Buck
Chief Counsel

cc: Regional Directors
Regional Counsel