

STATE TREASURER:
STATE DEPOSITORIES:
BANKS:
INTEREST:
NOTICE:

The state depository contract provides for time deposits, open account for which the state is paid interest on an escalating scale. Banks cannot return deposits unless the banks terminate the contract on 30 days written notice. The 30 days begin to run when the notice is received by the State Treasurer.

December 21, 1965

OPINION NO. 471

Honorable M. E. Morris
Treasurer for the State of Missouri
Jefferson City, Missouri



Dear Mr. Morris:

This opinion is in response to your request for advice arising from certain state depositories' contention that they have the right to return their state deposits to the state treasurer placed with them under contracts on "time deposits, open accounts" without payment of interest at the advanced rate of interest prescribed recently by the Federal Reserve Board.

In the interests of better understanding, a brief explanation of the banking systems so far as it is pertinent to these issues is required. There are two parallel systems of banking practices, each operating under separate federal rules and regulations. There is the Federal Reserve system composed of "member banks" that operate under rules and regulations promulgated by the Board of Governors of the Federal Reserve Board. The other group are "nonmember" banks operating under rules and regulations promulgated by the Federal Deposit Insurance Corporation, for example, state banks insured by the Federal Deposit Insurance Corporation. There is a third type of banks which are state banks and are not members of Federal Deposit Insurance Corporation.

A brief review of the pertinent facts for the record is also desirable. Pursuant to Section 15, Article IV, Constitution of Missouri 1945, and Chapter 30, RSMo as amended, the state treasurer has entered into contracts with certain banks for the safe-keeping of state funds. Some of the money has been placed on "time deposits, open account" drawing interest as provided in Section 30.260 (3) RSMo 1959, for the benefit of the state which provides as follows:

"The rate of interest payable by all banking institutions on time deposits of state moneys shall be the maximum rate of interest which by federal law or regulation a bank which is a member of the Federal Reserve System may from time to time pay on a time deposit that is payable upon written notice of less than ninety days, and the method of computing interest on time deposits of state moneys shall be uniform among

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all depositaries. All time deposits of state moneys shall be subject to withdrawal by the state treasurer upon the expiration of notice given by him not less than thirty days in advance of withdrawal."

Deposits are made pursuant to a written contract which is attached hereto. Prior to December 6, 1965, the maximum rate of interest payable on time deposits open account by Federal Reserve member banks (or "nonmember" banks that were under the Federal Deposit Insurance Corporation regulations) was 4 percent. This was because of the provisions of Federal Reserve regulation Section 217.6 of Regulation Q, effective December 6, 1965, for Federal Reserve member banks, the rates were increased to 5½ percent pursuant to an amendment to Section 217.6 (supra). On December 7, 1965, the Federal Deposit Insurance Corporation increased the maximum interest rate payable by their banks to 5½ percent pursuant to an amendment to Section 329, Federal Deposit Insurance Corporation rules and regulations.

On November 24, 1965, the State Treasurer gave notice to the depository banks that the State would withdraw 25 percent of the respective balances on deposit with such banks effective January 1, 1966.

After the increase of maximum interest rate pursuant to the change in the Federal Reserve Regulation and the operation of the provisions of Section 30.260 RSMo 1959 the banks have tendered to the State Treasurer the amounts of the state deposits with accrued interest payable at the rate of 4 percent until December 6, 1965, and 5½ percent from December 6, 1965 to date of tender stating they are not "cancelling" the depository contract but they are returning the money. As to those sums to be withdrawn under notice given by the State on November 24, 1965, the banks are offering only 4 percent interest until payment contending such sums are not time deposits covered by the amendment on interest rates stating that the maturity date is December 31, which is less than 30 days from December 6, 1965, and therefore cannot be classified as "a time deposit, open account."

Section 30.250, RSMo 1959, in pertinent parts, reads as follows:

"1. The state treasurer shall enter into a written contract in quintuplicate with each depository setting forth the conditions and terms upon which the moneys of the state are deposited therewith and containing among its provisions and conditions the following:

- (1) The amount of the moneys of the state to be entrusted to each depository;
- (2) With respect to demand deposits, the time such contract shall continue with

the right reserved to each the state treasurer and the depository to terminate the contract at any time upon giving thirty days' notice to the other party of his or its intention to do so;

- (3) With respect to time deposits, the conditions as to time and notice which need be given in regard to withdrawals and the rate of interest which the depository shall be obligated to pay;
- (4) Provisions requiring that the depository shall (a) safely keep said deposits, (b) pay demand deposits on the state treasurer's written demand therefor, and (c) pay time deposits only in accordance with the contract with the depository."

The terms and conditions of this statute are a part of the contract between the State and the bank.

The "State Depository Contract" referred to in the statute is in standard form with the banks and the State Treasurer is the First Party and the Bank is the Second Party. The 3rd paragraph of the contract contains the following language:

"It is hereby agreed that First Party will deposit with Second Party such sums of the state moneys of the State of Missouri as may be designated by the State Treasurer, not to exceed a total of \$_____. Moneys so deposited with Second Party shall be held by Second Party as a time deposit, open account, and shall be subject to withdrawal by First Party upon the expiration of the period of notice of intention to withdraw which shall be given by First Party to Second Party in writing not less than thirty (30) days in advance of withdrawal."

A "time deposit, open account," as used in the Federal Reserve System is defined by Section 217.1 (d), Regulation Q of the Federal Reserve Board as follows:

"The term 'time deposit, open account' means a deposit, other than a 'time certificate of deposit' or a 'savings deposit', with respect to which there is in force a written contract with the depositor that neither the whole nor any part of such deposit may be withdrawn, by check or otherwise, prior to the date of maturity, which shall be not less than 30 days after the date of the deposit, or prior to

the expiration of the period of notice which must be given by the depositor in writing not less than 30 days in advance of withdrawal."

A "time deposit, open account" as defined for use of non-member banks that are under Federal Deposit Insurance Corporation regulations is found in Section 329.1 (d) Title 12, C.F.R. p 247 and is substantially identical to that employed for members of the Federal Reserve System.

Pursuant to Section 30.260 (3), RSMo 1959, the Contract contains an escalation clause respecting the interest rate that such state deposits shall bear as follows:

"Second Party agrees to pay to First Party interest on moneys so deposited with Second Party at the maximum rate which, by federal law or regulation, a bank which is a member of the Federal Reserve System is permitted, from time to time, to pay on such time deposits."

A comment at this time on the validity of a contract provision providing for escalation of interest rates appears appropriate. The general rule covering escalating interest rates in a contract is aptly stated in 47 CJS "Interest" Section 33(b), p. 44, as follows:

"The parties may enter into a contract by which the rate of interest to be paid shall change whenever the legal rate changes."

See also 30 Am Jur "Interests" Section 28, p. 25; Wychoff v. Wychoff (NJ 1888) 13 at 662; Bankers Bond Co. v. Buckingham (Ky. 1936) 97 S.W.2d 596.

The fact that there was an effective change of interest rate on December 6, 1965, for Federal Reserve banks does not change the nature of the deposit or the obligations of the parties in our opinion. It does not constitute a novation as there has been no consent by the state (Hutcheson & Co. v. Providence-Washington Insurance Company, 341 S.W.2d 142, 146).

The contract contains the following provision respecting termination:

"Each party reserves the right to terminate this contract at any time on giving thirty (30) days' written notice to the other party of its intention to do so; and this contract shall continue in effect until so terminated."

Considering the principles set out above, we believe the obligations of the parties were fully spelled out in the contract, with the change of interest rates increasing the sum payable by the debtor banks for use of state money. Simply put, we believe the banks agreed to accept a sum certain under the contract for the duration of the contract or until terminated on 30 days written notice as provided by the contract. They agreed to pay therefor an interest rate on an escalating scale according to the maximum legal rate set by the Federal Reserve Board.

The first question for consideration is the contention of the several banks that a depository bank may return the amount of deposit to the state at the election of the bank.

With the permission of the author, we quote from a letter dated December 9, 1965, written by the General Counsel for the Federal Reserve Bank at St. Louis, Missouri, which reads as follows:

'A bank's obligations under the Federal banking laws with regard to payment of time deposits are governed, for banks which are members of the Federal Reserve System, by 12 U.S.C.A. §371 (b) which provides:

'The Board of Governors of the Federal Reserve System shall from time to time limit by regulation the rate of interest which may be paid by member banks on time and savings deposits . . . No member bank shall pay any time deposit before its maturity except upon such conditions and in accordance with such rules and regulations as may be prescribed by the said Board . . .'

"(Similar provisions with regard to Federally insured banks which do not belong to the Federal Reserve System may be found at 12 U.S.C.A. §1828 (g).)

"By authority of 12 U.S.C.A. §461, the Board of Governors of the Federal Reserve System is empowered to define (among other terms) 'time deposit,' and it has done so in Section 217.1 (b) of Regulation Q as including a 'time deposit, open account.' The latter term is further defined in Section 217.1 (d) of the Regulation as ' . . . a deposit, . . . with respect to which there is in force a written contract with the depositor that neither the whole nor any part of such deposit may be withdrawn . . . prior to the expiration of the period of notice which must be

given by the depositor in writing not less than 30 days in advance of withdrawal.' The terms of the State Depository Contract make it clear that these deposits must be classified by a member bank as a 'time deposit, open account.'

"The possibility of the repayment of a 'time deposit, open account' before maturity is governed by Sections 217.4 (c) and (d) which provide:

'(c) . . . No member bank shall pay any time deposit, with respect to which notice is required to be given a certain specified period before any withdrawal is made, until such required notice has been given and the specified period thereafter has expired, except as provided in paragraph (d) of this section.

'(d) . . . In an emergency where it is necessary to prevent great hardship to the depositor, a member bank may pay before maturity a time deposit or the portion thereof necessary to meet such emergency, Provided, That before making such payment the depositor shall sign an application describing fully the circumstances constituting the emergency which is deemed to justify the payment of the deposit before maturity, which application shall be approved by an officer of the bank who shall certify that, to the best of his knowledge and belief, the statements in the application are true. Such application there shall be retained in the bank's files and made available to the examiners authorized to examine the bank. Where a time deposit is paid before maturity the depositor shall forfeit accrued and unpaid interest for a period of not less than three months on the amount withdrawn if an amount equal to the amount withdrawn has been on deposit three months or longer, and shall forfeit all accrued and unpaid interest on the amount withdrawn if an amount equal to the amount withdrawn has been on deposit less than three months'

"The foregoing makes provision for payment of a time deposit prior to maturity only upon the application of the depositor. However, it cannot be presumed that the absence of any counterpart provision for prepayment at the initiative of the bank is accidental. On the contrary, such absence may well reflect a conclusion that if the best interests of the bank and other depositors are to be protected, it is necessary to remove any possibility that a bank could waive the requirements of

notice and repay before maturity. Otherwise, for example, a bank might be subject to considerable pressures from an important customer to acquiesce in an early repayment.

"In any event, however, there is no provision under Regulation Q for advance payment of a time deposit upon the initiative of the depository bank, and, accordingly, it would be my opinion that a member bank which does so violates the Regulation and 12 U.S.C.A. §371 (b)."

Section 329.4 Title 12 C.F.R. p. 250-251 (which is applicable to "nonmember" state banks under Federal Deposit Insurance Corporation rules) reads as follows:

"(a) Time deposits payable on a specified date. No insured nonmember bank shall pay any time deposit, which is payable on a specified date, before such specified date, except as provided in paragraph (d) of this section.

"(b) Time deposits payable after a specified period. No insured nonmember bank shall pay any time deposit, which is payable at the expiration of a specified period, before such period has expired, except as provided in paragraph (d) of this section.

"(c) Time deposits payable after a specified notice. No insured nonmember bank shall pay any time deposit, with respect to which notice is required to be given a specified period before any withdrawal is made, until such required notice has been given and the specified period thereafter has expired, except as provided in paragraph (d) of this section."

Section 1828 (g) Title 12 U.S.C.A. p. 382 reads as follows:

". . . Such regulations shall prohibit any insured nonmember bank from paying any time deposit before its maturity except upon such conditions and in accordance with such rules and regulations as may be prescribed by the Board of Directors, and from waiving any requirement of notice before payment of any savings deposit except as to all savings deposits having the same requirement . . ."

Based on the above authorities we conclude that a bank (whether a member bank of the Federal Reserve System or nonmember bank under Federal Deposit Insurance Corporation) may not lawfully make an advance payment of a time deposit upon the initiative of the depository bank (absent termination of the contract on 30 days written notice as provided in the contract).

The next question for determination is the amount of interest that the depository banks are required to pay after December 6, 1965, on those sums of monies for which notice of withdrawal has been given by the state treasurer to the depository banks on November 24, 1965.

As to that portion of the deposits on which notice has been given, we quote subparagraph Section 217.3 (e) of Regulation Q of the Federal Reserve Regulations:

"A deposit which was a time deposit at the date of deposit continues to be such until maturity although it has become payable within 30 days, and interest at a rate not exceeding that prescribed pursuant to the provisions of paragraph (a) of this section may be paid until maturity upon such deposit. A time deposit or a savings deposit with respect to which notice of withdrawal has been given continues to be such until the expiration of the period of such notice, and interest may be paid upon such deposit until the expiration of the period of such notice at a rate not exceeding that prescribed pursuant to the provisions of paragraph (a) of this section." (Emphasis Added)

Section 329.3 (d) Title 12, C.F.R. applicable to nonmember state banks under Federal Deposit Insurance Corporation regulations reads as follows:

"(d) Continuance of time deposit status. A deposit which was a time deposit at the date of deposit continues to be such until maturity, although it has become payable within thirty (30) days, and interest at a rate not exceeding that prescribed pursuant to the provisions of paragraph (a) of this section may be paid until maturity upon such deposit. A time deposit or a savings deposit, with respect to which notice of withdrawal has been given, continues to be such until the expiration of the period of such notice, and interest may be paid upon such deposit until the expiration of the period of such notice, at a rate not exceeding that prescribed pursuant to the provisions of paragraph (a) of this section. Interest at a rate not exceeding

that prescribed pursuant to the provisions of paragraph (a) of this section. Interest at a rate not exceeding that prescribed pursuant to the provisions of paragraph (a) of this section may be paid upon savings deposits with respect to which notice of intended withdrawal has not actually been required or given. No interest shall be paid by an insured nonmember bank on any amount which by the terms of any certificate or other contract or agreement, or otherwise, the bank may be required to pay within thirty (30) days from the date on which such amount is deposited in such bank, except as to savings deposits with respect to which the bank consistently continues to adhere to a practice existing prior to January 23, 1936, of requiring notice of at least fifteen (15) days before permitting withdrawal."

These regulations provide that the bank may continue to pay interest on the time deposit at the applicable rate until the expiration of the period provided in the notice of withdrawal.

We conclude therefore that the depository member and "non-member" banks are required to pay on all moneys on deposit at the rate of 4 percent interest until December 6, 1965, and thereafter at the rate of 5 1/2 percent until such moneys in the time deposit, open account have been withdrawn from the depository member banks by the state.

The next question is one of notice, i.e., does the 30 day period of written notice to terminate start to run under the contract when it is mailed (if so) or when such notice is received by the state treasurer?

It is noted the contract does not specify the means or manner in which the notice shall be communicated other than require that it be "30 days written notice". The court, in *Schott v. Continental Auto Ins. Underwriters*, 31 S.W.2d 7, 13, made these general observations about notice, which we feel are pertinent here and we set them out:

"According to a general rule, where notice is required to be given by statute, or contract, and the manner of serving the notice is not prescribed, personal service is intended. There is also an auxiliary rule, likewise general in application, that has the support of authority: 'In the absence of custom, statute, estoppel, or express contract stipulation, when a notice, affecting a right, is sought to be served by mail, the service is not effected until

the notice comes into the hands of the one to be served, and he acquires knowledge of its contents.' 46 C. J. 559. If the language of the applicable provision of the policy alone be considered, it must be held, in consonance with the rules just mentioned, either that personal service of notice of loss on the insurer at its home office in Springfield, Ill., is required, or, if the general rule may be sufficiently relaxed to admit of service by mail, that such service is not effected until the notice is actually received and read by a duly authorized agent of the insurer at its home office.

[7,8] But the rules just referred to are merely rules of construction--at least when applied to contracts. They are not controlling, therefore, where it is manifest from the instrument as a whole that the intention of the parties would be thwarted, rather than given effect, by their application. A more important rule in the construction of contracts is that the interpretation must be upon the entire instrument, and not merely upon disjointed or particular parts of it. 'The whole context is to be considered in ascertaining the intention of the parties, even though the immediate object of inquiry is the meaning of an isolated clause.' 6 R.C.L. 837, §227."

Applying these general rules to this contract, it is intended that service of notice must be had upon the state treasurer, or his office if the depository banks desire to terminate the contract. Thus, if notice were mailed to the state treasurer, the 30 day period for termination of the contract would begin to run from the date such notice of termination was, in fact, delivered to the office of the state treasurer. We conclude therefore that the 30 day written notice by depository banks to terminate the contract begins to run when such notice is delivered to the office of the state treasurer in Jefferson City, Missouri, or is personally served on him elsewhere as the case may be.

The State Treasurer does not have authority to settle or adjust the claims of the banks except as provided for by the depository contract pursuant to the law made and provided for. A waiver or acceptance of oral notice to terminate is unauthorized. As long as the contract is in effect the banks have agreed to accept an amount up to a sum certain and to pay thereon, interest at the rate specified under the terms of the contract, nothing less can be accepted.

CONCLUSION

It is the opinion of this office that:

1. Depository banks under their contracts with the state may not return deposits of the state at their election while the contract

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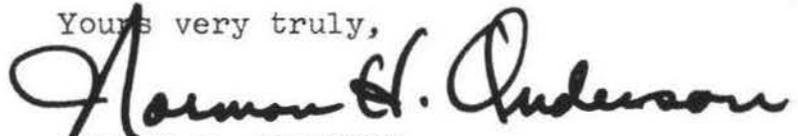
is in force, provided such deposits do not exceed the total amount of deposit stipulated in the contract.

2. Moneys on deposit for which notices of withdrawal have been given to the depository banks retain their character as "time deposits, open account" drawing the same rate of interest as the balance of the moneys on deposit as provided by the contract, i.e., at the maximum rate which, by federal law or regulation, a bank which is a member of the Federal Reserve System is **permitted**, from time to time, to pay on such time deposits even though the rate of interest may escalate subsequent to the notice of withdrawal.

3. The 30 day written notice of termination of the State Depository Contract commences to run upon delivery to the State Treasurer of such notice.

The foregoing opinion, which I hereby approve, was prepared by my assistant, Mr. Richard C. Ashby.

Yours very truly,

A handwritten signature in cursive script, reading "Norman H. Anderson". The signature is written in black ink and is positioned above the typed name and title.

NORMAN H. ANDERSON
Attorney General