Overview of the Federal Reserve's Payment System Risk Policy on Intraday Credit

Updated to reflect policy revisions effective March 24, 2011

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http://www.federalreserve.gov/paymentsystems/files/psr_2011_overview.pdf.

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PREFACE

The purpose of this document, the Overview, is to help institutions comply with the Federal Reserve Policy on Payment System Risk (PSR policy), issued by the Board of Governors of the Federal Reserve System (the Board). The PSR policy contains two parts. Part I addresses risk management in payment and securities settlement systems. Part II addresses the risks to the Federal Reserve Banks in extending intraday credit to depository institutions. This Overview addresses compliance with part II of the PSR policy. The appendix contains a glossary of PSR terminology.

Depository institutions that use small amounts of Federal Reserve intraday credit should use the Overview to help determine the requirements for compliance with the Federal Reserve's policy on intraday credit (part II of the PSR policy). Institutions that use Federal Reserve intraday credit regularly or in substantial amounts, foreign banking organizations, and those that may be considered "special situations" because of their legal structure or payment activity should refer to the *Guide to the Federal Reserve's Payment System Risk Policy on Intraday Credit* for a more-comprehensive description of the requirements of the Board's intraday credit policy.[1]

Information contained in the Overview is based on the PSR policy in effect as of the effective date of this document. If the Board finds it necessary to modify the PSR policy, future policy statements will supersede information in the Overview until it can be updated accordingly.[2]

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[1] The *Guide to the Federal Reserve's Payment System Risk Policy on Intraday Credit* is available at http://www.federalreserve.gov/paymentsystems/psr_guide.htm.

[2] The current version of the PSR policy is available at http://www.federalreserve.gov/paymentsystems/psr_policy.htm.

I. BACKGROUND

An integral component of the PSR policy is a program to govern institutions' use of Federal Reserve intraday credit, also referred to as "daylight overdrafts." A daylight overdraft occurs when funds in an institution's Federal Reserve account are insufficient to cover outgoing transactions, for example, Fedwire® funds transfers, incoming Fedwire securities transfers, or other payment activity processed by a Reserve Bank, such as check or automated clearinghouse (ACH) transactions.[3,4]

A. Brief History of the Federal Reserve's Intraday Credit Policy

In 1985, the Board published a policy on risks in large-dollar wire transfer systems.[5] The policy required institutions incurring daylight overdrafts in their Federal Reserve accounts as a result of Fedwire funds transfers to establish a maximum limit, or net debit cap, on those overdrafts. In subsequent years, the Board expanded the original PSR policy by addressing the control of risks in other payment activities such as ACH transactions, Fedwire securities transfers, offshore dollar clearing and netting, and certain private-sector securities clearing and settlement systems.[6] In addition, the Board has made a number of modifications to the original policy, such as reductions in net debit cap levels, the creation of an exempt status for institutions that incur only small amounts of daylight overdrafts, and the implementation of daylight overdraft fees.

In 1992, the Board modified the policy to charge institutions fees for their use of Federal Reserve intraday credit, beginning in April 1994.[7] The Board also modified how it measures daylight overdrafts in institutions' Federal Reserve accounts to incorporate specific account posting times for different types of transactions.

In 2001, the Board revised the PSR policy to permit certain institutions to obtain collateralized daylight overdraft capacity above their net debit caps and to modify the net debit cap calculation for U.S. branches and agencies of foreign banks.[8] In addition, the Board rescinded its interaffiliate transfer and Fedwire third-party access policies because the risks presented by these arrangements are adequately addressed through the supervisory process.

In 2004, the Board announced two policy revisions pertaining to government-sponsored enterprises (GSEs) and certain international organizations.[9] These revisions, affecting the

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[3] Fedwire is a registered service mark of the Federal Reserve Banks.
[4] For a broader discussion and guidance on management of risks associated with retail payment systems and related banking activities that institutions may find helpful, see the *FFIEC IT Examination Handbook*, "Retail Payment Systems Booklet" at http://www.ffiec.gov/ffiecinfobase/html_pages/retail_book_frame.htm.
[5] See 50 FR 21120, May 22, 1985.
[6] See 52 FR 29255, August 6, 1987.
[7] See 57 FR 47084, October 14, 1992.
[8] See 66 FR 64419, December 13, 2001.
[9] See 69 FR 57917, September 28, 2004.

interest and redemption payments and the general corporate payment activity of these entities, became effective in July 2006.

Also in 2004, the Board approved changes to the PSR policy addressing risk management in payment and securities settlement systems.[10] The action also modified the introduction to the policy, reordered the first two sections of the policy, and deleted the third section of the policy containing guidance on rollovers and continuing contracts. The Board determined that institutions have the appropriate incentives to incorporate the guidance into their daylight credit procedures and that specific guidance was no longer necessary.

In 2008, the Board adopted major revisions to the PSR policy that are designed to improve intraday liquidity management and payment flows for the banking system, while also helping to mitigate the credit exposures to the Federal Reserve Banks from daylight overdrafts.[11] The changes include a new approach that explicitly recognizes the role of the central bank in providing intraday balances and credit to healthy depository institutions, a zero fee for collateralized daylight overdrafts, a 50 basis point (annual rate) charge for uncollateralized daylight overdrafts, and a biweekly daylight overdraft fee waiver of $150. In addition, the Board adopted changes to other elements of the PSR policy dealing with daylight overdrafts, including adjusting net debit caps, eliminating the current deductible for daylight overdraft fees, and increasing the penalty daylight overdraft fee to 150 basis points (annual rate). The changes are effective March 24, 2010.[12]

B. Primary Risk Controls Included in the Intraday Credit Policy

Like depository institutions that offer payment services to customers, Federal Reserve Banks may be exposed to risk of loss when they process payments for institutions that hold accounts with them. Depository institutions use intraday credit primarily to cover outgoing Fedwire transfers, incoming book-entry securities transfers, checks, and ACH transactions. Reserve Banks provide settlement finality for transactions over the Fedwire Funds Service, Fedwire Securities Service, National Settlement Service, and on ACH credit originations. Once the Reserve Banks provide final settlement for these transactions, they face direct risk of loss should depository institutions be unable to settle their daylight overdrafts before the end of the day. The Federal Reserve's exposure in such instances can be significant. Aggregate daylight overdraft data are available at http://www.federalreserve.gov/paymentsystems/psr_data.htm.

The PSR policy enables Reserve Banks to control their exposure to credit risk in four ways. First, institutions that access intraday credit must satisfy safety and soundness requirements. Second, the policy establishes limits on the amount of Federal Reserve's intraday credit that an institution may use. These limits are sufficiently flexible to reflect the overall financial condition and operational capacity of each institution using Federal Reserve payment services. Third, the policy also permits Reserve Banks to protect themselves from the risk of loss through such measures as restricting account activity, imposing collateral or balance requirements, or prohibiting an institution from using Federal Reserve intraday credit.

[10] See 69 FR 69926, December 1, 2004.
[11] See 73 FR 79109, December 24, 2008.
[12] See 75 FR 60749, October 1, 2010.

Finally, the policy provides incentives for institutions to pledge collateral voluntarily to secure daylight overdrafts. Institutions that secure their use of intraday credit with collateral are not charged for these daylight overdrafts, while institutions that incur uncollateralized daylight overdrafts will be charged a fee. The Board has also provided a fee waiver of $150 to reduce the administrative burden on institutions that incur small amounts of uncollateralized daylight overdrafts.

II. DAYLIGHT OVERDRAFT CAPACITY

Under the Federal Reserve's PSR policy, each institution that maintains a Federal Reserve account is assigned or may establish a net debit cap, which limits the amount of daylight overdrafts that the institution may incur in its Federal Reserve account. An institution must be financially healthy and have regular access to the discount window to adopt a positive net debit cap. This section discusses the types of cap categories and the methods for establishing a cap category.

A. Net Debit Caps

An institution's net debit cap is the maximum dollar amount of daylight overdrafts it may incur in its Federal Reserve account. An institution's cap category and its capital measure determine the dollar amount of its net debit cap.[13] An institution's net debit cap is calculated as its cap multiple times its capital measure:

Net debit cap =

cap multiple x capital measure.

Because an institution's net debit cap is a function of its capital measure, the dollar amount of the cap will vary over time as the institution's capital measure changes. An institution's cap category is normally set for one year, but the Reserve Banks will monitor the condition of all accountholders throughout the year to ensure that they remain eligible for their respective caps.

The policy defines six cap categories, described in more detail below: zero, exempt-from-filing, de minimis, and three cap categories referred to as "self-assessed": average, above average, and high. Cap categories and their associated cap levels, set as multiples of capital, are listed in the following table.

[13] The capital measure for domestically chartered institutions is equivalent to supervisory capital, as described in the capital adequacy guidelines of the federal financial regulatory agencies. See section 6 of this document for a discussion of the capital measure used for U.S. branches and agencies of foreign banks.

Net Debit Cap Multiples

Cap Categories	Cap Multiples
Zero	0.0
Exempt-from-filing*	$10 million/0.20
De minimis	0.40
Average	1.125
Above average	1.875
High	2.25
*The net debit cap for the exempt-from-filing category is equal to the lesser of $10 million or 0.2 multiplied by a capital measure.	

1. Zero

Generally, the Reserve Bank assigns zero caps to institutions that pose special risks to the Reserve Bank, such as those in weak financial condition, those without regular access to the discount window, or those incurring daylight overdrafts in violation of the PSR policy.[14] The Reserve Bank may also assign a zero cap to recently chartered institutions. Institutions that are financially healthy may adopt a zero cap voluntarily.

An institution with a zero net debit cap may not incur daylight overdrafts in its Federal Reserve account. If an institution with a zero cap incurs a daylight overdraft, the Reserve Bank will counsel the institution and may monitor the institution's activity in real time and reject or delay certain transactions that would cause an overdraft. The institution will also be required to prefund its ACH credit originations when the Reserve Bank processes the items. If the institution has adopted the zero cap voluntarily and qualifies for a positive cap, the Reserve Bank may suggest that the institution adopt an exempt-from-filing cap or file for a higher cap if the institution believes that it will continue to incur daylight overdrafts.

2. Exempt-from-Filing

The exempt-from-filing cap permits institutions to incur daylight overdrafts in amounts up to the lesser of $10 million or 20 percent of their capital. The majority of institutions that maintain Federal Reserve accounts have an exempt-from-filing net debit cap. If a Reserve Bank determines that an institution is eligible for the exempt-from-filing status, it will assign this cap category without requiring any additional documentation. Unlike higher cap categories, institutions in this category are not required to renew their caps annually. As a result, the exempt-from-filing cap category substantially reduces the administrative burden associated with obtaining a net debit cap.

To be eligible for an exempt-from-filing cap, an institution must be in healthy financial condition and should use only minimal amounts of the Federal Reserve intraday credit: up to the lesser of $10 million or 20 percent of its capital. The PSR policy offers some flexibility for

[14] An institution may be assigned a zero cap if the condition of its holding company or one or more affiliates is deemed to be marginal or unsatisfactory by the primary regulator. See Appendix A to the *Guide to the Federal Reserve's Payment System Risk Policy on Intraday Credit* at http://www.federalreserve.gov/paymentsystems/psr_guide.htm for further information.

exempt-from-filing institutions to accommodate higher payment volumes; the Reserve Bank allows an exempt-from-filing institution to exceed its cap up to two times in two consecutive two-week reserve-maintenance periods. If overdrafts over the cap limit are more frequent, the Reserve Bank will counsel the institution and may require the institution to file for a higher cap.

3. De Minimis

Institutions that incur daylight overdrafts up to 40 percent of their capital may qualify for a de minimis net debit cap. To ease the burden of performing a self-assessment for these institutions, the PSR policy allows a financially healthy institution to incur daylight overdrafts up to 40 percent of its capital if the institution submits a board of directors' resolution.[15] An institution with a de minimis cap must submit to its Reserve Bank at least once in each twelve-month period a copy of its board of directors' resolution (or a resolution by its holding company's board) approving the institution's use of daylight credit up to the de minimis level. Generally, if an institution with a de minimis cap exceeds its cap during a two-week reserve maintenance period, the Reserve Bank may counsel the institution and decide whether the de minimis cap should be maintained or whether the institution will be required to perform a self-assessment for a higher cap.

4. Self-Assessed

Financially healthy institutions that regularly incur daylight overdrafts in excess of 40 percent of their capital must assess their creditworthiness, intraday funds management and control, customer credit policies and controls, and operating controls and contingency procedures to obtain cap levels that accommodate their normal use of intraday credit.[16] An institution's board of directors must review and approve the results of the self-assessment, and the institution must communicate its directors' approval to the Reserve Bank by submitting a board of directors' resolution. This process should occur at least once in each twelve-month period. The Reserve Bank, in conjunction with the institution's primary regulator, will review the appropriateness of the cap. Should the Reserve Bank determine that the cap resolution is not appropriate, it may require a new self-assessment and resolution, or it may determine and assign the appropriate cap. Additional information on the self-assessment process is provided in the *Guide to the Federal Reserve's Payment System Risk Policy on Daylight Credit.*[17]

B. Maximum Daylight Overdraft Capacity

Although net debit caps provide sufficient liquidity to most institutions, some institutions may still experience intraday liquidity pressures. To relieve these pressures, certain institutions with self-assessed net debit caps may pledge collateral to their Reserve Banks to secure daylight overdraft capacity in excess of their net debit caps, subject to Reserve Bank approval. The net

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[15] Sample resolutions are provided in the *Guide to the Federal Reserve's Payment System Risk Policy on Daylight Credit* at http://www.federalreserve.gov/paymentsystems/psr_guide.htm.
[16] An institution is not eligible for a self-assessed or any other positive cap, if the condition of one or more affiliates is deemed to be marginal or unsatisfactory by the primary regulator. See Appendix A to the *Guide to the Federal Reserve's Payment System Risk Policy on Intraday Credit* for further information.
[17] See http://www.federalreserve.gov/paymentsystems/psr_guide.htm.

debit cap plus the additional capacity is referred to as the "maximum daylight overdraft capacity" or "max cap." Collateral pledged to support a max cap offsets daylight overdraft fees.

An institution with a self-assessed net debit cap that wishes to expand its daylight overdraft capacity by pledging collateral should consult its Reserve Bank. The Reserve Bank will work with an institution that requests additional daylight overdraft capacity to determine the appropriate max cap level. The institution must submit its associated board of directors' resolution at least once in each twelve-month period.

U.S. branches and agencies of foreign banks with a self-assessed net debit cap and either a financial holding company designation or a SOSA 1 rating may pursue a streamlined procedure for obtaining a max cap. The streamlined max cap provides overdraft capacity of up to 100 percent of worldwide capital times the self-assessed cap multiple. Additional information on the max cap procedures and a max cap example are provided in the Guide to the Federal Reserve's Payment System Risk Policy on Daylight Credit.[18]

An institution's maximum daylight overdraft capacity is defined as follows:

Maximum daylight overdraft capacity = net debit cap + collateralized capacity.

Institutions with exempt-from-filing and de minimis net debit caps are not eligible for a max cap. These institutions, as well as institutions that have adopted a zero cap voluntarily, must first file for a self-assessed cap to obtain the additional capacity. An institution with a Reserve Bank-assigned zero net debit cap is not eligible for a max cap.

C. Confidentiality of Net Debit Caps

The Federal Reserve regards cap categories and net debit caps as confidential information and will share this information only with an institution's primary supervisor (5 U.S.C § 552(b)).[19] Institutions are also expected to treat their cap as confidential and should not disclose this information for marketing purposes. If an institution believes it must disclose its cap under securities law, the Federal Reserve does not prohibit such disclosure.

[18] See http://www.federalreserve.gov/paymentsystems/psr_guide.htm.

[19] For more information on the Freedom of Information Act, see http://www.federalreserve.gov/generalinfo/foia/foiastat.cfm.

III. COLLATERAL

An institution may pledge collateral to its Reserve Bank for a number of reasons such as to secure a loan from the discount window, or for PSR purposes.[20] Under the PSR policy, institutions with regular access to the discount window may pledge collateral voluntarily to secure daylight overdrafts at a zero fee.[21,22] Additionally, a Reserve Bank may require an institution to pledge collateral in certain circumstances, such as when an institution incurs an impermissible daylight overdraft.

Collateral an institution pledges to its Reserve Bank for PSR or discount window purposes is placed in a single Federal Reserve "FR collateral" account.[23] The Federal Reserve's Collateral Management System (CMS) records and maintains information on the collateral pledged to the FR collateral account, including tracking intraday pledges and withdrawals, and providing collateral valuation.

FR collateral that is not already encumbered may be applied in calculating an institution's charges for daylight overdrafts. An institution's "collateral available for daylight overdraft purposes" is calculated on a minute-by-minute basis by subtracting any collateral encumbrances, such as outstanding discount window loans, from the value of the FR collateral. In assessing charges for use of intraday credit, the Federal Reserve will compare an institution's end-of-minute daylight overdraft balance with the institution's end-of-minute balance of collateral available for daylight overdraft purposes. An institution's collateralized daylight overdrafts will be charged a zero fee. Uncollateralized daylight overdrafts will be assessed a fee of 50 basis points per annum. For further information about daylight overdraft pricing, see section V (Fees).

A. Eligibility, Valuation, and Margins

Generally, collateral that is acceptable to the Reserve Bank for discount window lending is also acceptable for PSR purposes. [24] The Federal Reserve provides a detailed list of acceptability

[20] Collateral pledged for PSR purposes serves to secure daylight overdrafts at a zero fee, to support an approved max cap, and to qualify for fully collateralized cap breach waivers.
[21] See section V (Daylight Overdraft Fees) of this Overview for further information on how the Federal Reserve determines collateral available for daylight overdraft purposes and calculates the charges.
[22] Self-assessed institutions may also pledge collateral to support an approved max cap. In addition, self-assessed and de minimis institutions may pledge collateral to qualify for fully collateralized cap breach waivers. Institutions without a regular access to the discount window, such as bankers' banks that are not subject to reserve requirements, do not benefit from the zero price for collateralized overdrafts.
[23] Institutions may also pledge collateral for Treasury purposes, which is held in the "TT&L collateral" account.
[24] In addition to the collateral that is eligible for discount window lending, the Reserve Banks may accept securities in transit for PSR purposes. In-transit securities refer to book-entry securities transferred over the Fedwire Securities Service that have been purchased by a depository institution but not yet paid for and owned by the institution's customers.

criteria on the discount window and PSR website.[25] This listing provides information on acceptance criteria applicable for all securities and loans, as well as specific acceptance criteria applicable by collateral type.

The Reserve Banks value and margin all pledged collateral. Generally, the Federal Reserve seeks to value all pledged collateral at fair market value. When possible, the Federal Reserve values securities using prices supplied by external vendors. It uses internal valuation models for loans and other securities. The Federal Reserve then applies its own margin, or haircut, to the fair market value estimates to determine lendable value of collateral for the institution. The Federal Reserve publishes its collateral margins table and provides a summary of the Federal Reserve's approach to valuing and margining collateral on the discount window and PSR website.[26]

B. Pledging and Withdrawing Collateral

The requirements for pledging collateral under the PSR policy are the same as those for pledging to the discount window. Institutions interested in pledging collateral for discount window or PSR purposes must complete certain legal documents (authorizing resolutions and agreements) with their Reserve Bank, specifically, Operating Circular No. 10 documents.[27] All collateral pledged to a Reserve Bank must be free of other claims, liens, security interests, or restrictions upon transfer or pledge to the Reserve Bank.

1. Types of pledging arrangements

Depending on what type of collateral is pledged, institutions may need to establish one or more pledging arrangements. Collateral may reside in Fedwire Securities Service (FSS), at Depository Trust Corporation (DTC), at a custodian, at the pledging institution via a borrower-in-custody (BIC) arrangement, at a foreign depository, or at the Reserve Bank.

- **FSS** is the Fedwire book-entry securities system that consists of safekeeping, transfer, and settlement functions for securities maintained on the books of the Reserve Banks. Institutions can initiate a pledge of securities held in FSS online using Fedline or offline by contacting Reserve Bank Wholesale Operations staff by phone. [28]
- **DTC** is a limited-purpose trust company that acts as the central securities depository for most publicly traded equity securities and many fixed-income securities in the U.S. market. An institution may directly pledge such securities (if it is a DTC participant) or may pledge DTC-held securities through a correspondent that is a DTC participant.

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[25] See the Discount Window and Payment System Risk Acceptance Criteria for Commonly Pledged Asset Types table that is available on the discount window and PSR website at http://www.frbdiscountwindow.org.
[26] The margins table is located at http://www.frbdiscountwindow.org/discountmargins.xls.
[27] Operating Circular No. 10 documents, including instructions, are available at http://frbdiscountwindow.org.
[28] A Reserve Bank may also accept in-transit securities as collateral for PSR purposes, including daylight overdraft pricing. In-transit securities are defined as book-entry securities transferred over FSS that have been purchased by a depository institution but not yet paid for and owned by the institution's customers.

- Institution approved by the Reserve Bank to maintain physical control of the loans on the premises of a custodian may designate a **third-party custodian** to provide collateral custody services. A third-party custodian must not be affiliated with the pledging institution and must be approved by the Reserve Bank prior to any pledge of collateral.[29] Custodians that are affiliated with the pledging institution will be considered under the borrower-in-custody pledging arrangement.
- **BIC arrangements** may be used by institutions approved by their Reserve Bank to maintain physical control of the loans either on its own premises or held on the premises of a custodian. Under this arrangement, institutions or custodians may retain custody of collateral while pledging it to a Reserve Bank, and the collateral must be designated as being pledged to the Reserve Bank.
- If an institution's Reserve Bank has entered into a custodian arrangement with **foreign depositories** - Clearstream and Euroclear – and the institution has been approved by its Reserve Bank, it may pledge foreign-issued or foreign-denominated securities.
- **Reserve Bank custody** may be used for pledging tangible assets, such as promissory notes evidencing commercial/consumer loans. The Reserve Bank may request financial information and other details about the institution's customers in order to evaluate the credit quality of the obligations.

2. *Withdrawing collateral*

An institution's collateral that is not securing an outstanding extension of credit at the discount window, and is not pledged as a PSR collateral requirement (see below), is considered unencumbered and available for withdrawal. The procedures and processing times to withdraw collateral depends on the pledging arrangement.[30]

C. Reserve Bank PSR Collateral Requirement

Under the PSR policy, a Reserve Bank may require an institution to pledge collateral in certain circumstances. A Reserve Bank may impose a PSR collateral requirement on an institution incurring impermissible daylight overdrafts or on an institution in weak financial condition. For institutions with regular access to the discount window, PSR collateral requirements contribute to offsetting fees and assessing fully collateralized cap breach waivers.[31]

[29] An institution should contact its Reserve Bank to obtain approval of its proposed custodian and must execute appropriate agreements to qualify for a third-party custody pledging arrangement.
[30] For more information, visit the Federal Reserve System Guide to Discount Window and PSR Collateral available at http://www.frbdiscountwindow.org.
[31] At the Reserve Bank's discretion, an institution with a self assessed or de minimis net debit cap may exceed its net debit cap without violating the policy if the institution has fully collateralized all cap breaches on a given day. Under the waiver, institutions may fully collateralize up to two cap breaches in two consecutive reserve-maintenance periods (four weeks).

D. Collateral Monitoring and Inquiry Capabilities

CMS serves as the system of record and valuation for all collateral pledged to the Reserve Banks. As institutions pledge and withdraw collateral, and receive or repay discount window loans, the amount of collateral available for daylight overdraft purposes also changes. CMS updates collateral balances in near-real-time throughout the day and sends this information to the Account Management Information (AMI) system and Account Balance Monitoring System (ABMS), two Reserve Bank applications that serve as information sources and as balance monitoring and management tools for institutions.[32]

1. Intraday monitoring

The AMI application provides institutions with near-real-time collateral holdings information. Institutions may view and download aggregate and CUSIP-level collateral information on an intraday basis. Institutions may view and download their intraday increases (including deposits and revaluations) and decreases (including withdrawals and revaluations) to their collateral positions rolled up by asset type (securities or loans). Institutions are also able to view and download their collateral activity chronologically, from the beginning of the day to the close of business. Institutions may view the value of their collateral available for daylight overdraft purposes (the value of holdings in their FR collateral account less outstanding discount window advances) during the day through AMI or ABMS.[33]

2. Ex post monitoring

In addition to monitoring their collateral balances intraday, institutions may also view information about their collateral holdings and transactions ex post. CMS creates a statement of collateral holdings at the CUSIP level and a report summarizing an institution's collateral transactions grouped by type, such as deposits, withdrawals, and revaluations, which are available to institutions in AMI.[34]

In addition to the reports available through AMI, CMS also generates periodic reports for each institution that has elected to receive statements of its collateral holdings via e-mail.[35]

[32] AMI is a web-based application that provides institutions with real-time access to their intraday account and collateral balances, detailed transaction information, a variety of reports, and inquiry capabilities. ABMS receives updated collateral information, including an institution's value of collateral available for daylight overdraft purposes, from CMS on a near-real-time basis. ABMS will use the collateral available for daylight overdraft purposes to calculate the institution's collateralized and uncollateralized daylight overdraft balances, which will also be updated on a near-real-time basis. Institutions can obtain information on ABMS and AMI in the *Account Management Guide* at http://www.frbservices.org/files/regulations/pdf/amg.pdf.
[33] AMI and ABMS do not provide institutions with information on extensions of credit.
[34] Because collateral-related activities occur throughout the day and past the close of business, CMS creates two sets of collateral reports each day: a preliminary holding statement after 5:30 p.m. ET that day and the final version next morning. Institutions also have access to previous days' final reports, which are also available through AMI.
[35] Institutions that do not have access to AMI may elect to receive holdings statements via e-mail from CMS.

IV. Daylight Overdraft Monitoring

The information in this section is intended to assist institutions in monitoring their Federal Reserve account balances for daylight overdraft purposes. The Federal Reserve expects institutions that maintain Federal Reserve accounts to monitor their account balances on an intraday basis in order to comply with the PSR policy. Institutions should be aware of the payments made from their accounts each day and know how those payments are funded. Institutions are expected to use their own systems and procedures, as well as the Federal Reserve's systems, to monitor their Federal Reserve account balance and payment activity.

A. Daylight Overdraft Measurement

The Federal Reserve uses a schedule of rules (referred to as "daylight overdraft posting rules") to determine whether a daylight overdraft has occurred in an institution's account. The daylight overdraft posting rules define the time of day that debits and credits for transactions processed by the Federal Reserve will post to an institution's account.[36] For example, Fedwire funds transfers, Fedwire securities transfers, and National Settlement Service (NSS) transactions are posted to accounts as they occur throughout the day, while all other transactions have fixed posting times. Although the posting rules affect the calculation of an institution's account balance for daylight overdraft monitoring and pricing purposes, the posting rules do not affect the finality or irrevocability of the entry to the account.

The Federal Reserve uses the Daylight Overdraft Reporting and Pricing System (DORPS) to measure on an ex post basis an institution's overdraft activity, monitor its compliance with the PSR policy, and calculate daylight overdraft charges. At the end of each Fedwire operating day, DORPS captures all debits and credits resulting from an institution's payment activity and calculates end-of-minute account balances using the daylight overdraft posting rules.[37] The daylight overdraft measurement period begins with the standard opening time of the Fedwire Funds Service at 9:00 p.m. eastern time (ET) the preceding calendar day and continues until the standard closing at 6:30 p.m. ET.[38] Although DORPS records positive and negative account balances, a net positive balance from one minute does not offset a net negative balance from another minute for purposes of determining compliance with net debit caps or for

[36] The daylight overdraft posting rules are available in the PSR policy at http://www.federalreserve.gov/paymentsystems/psr_policy.htm.

[37] Examples of daylight overdraft monitoring summary reports can be viewed in the *Account Management Guide* at http://www.frbservices.org/serviceofferings/account/ami.html.

[38] Fedwire transfers occurring after the standard close are recorded as if they were made at the standard closing time. In cases of unscheduled extensions of Fedwire hours, the final closing account balance at the time the Fedwire Funds Service actually closes is recorded as if it were the balance at the standard closing time.

calculating daylight overdraft fees. In addition, DORPS calculates daylight overdrafts on a consolidated basis for U.S. branches and agencies of the same foreign bank family and for accounts involved in a charter-level merger. In these instances, DORPS derives a single account balance by adding together the end-of-minute balances of each account.[39,40]

B. Policy Compliance

Reserve Banks generally monitor institutions' compliance with the PSR policy over each two-week reserve maintenance period. At the end of each two-week reserve maintenance period, DORPS generates several reports that provide both Reserve Banks and institutions with information for monitoring daylight overdrafts, including the largest (or peak) daylight overdraft for each day during the period and daylight overdrafts in excess of an institution's approved daylight overdraft capacity (cap breach).

The Federal Reserve considers all cap breaches to be violations of the PSR policy except in the following limited circumstances. First, the policy allows institutions in the exempt-from-filing cap category to incur up to two cap breaches in two consecutive two-week reserve-maintenance periods. Second, certain cap breaches incurred by institutions in the administrative counseling flexibility program are not considered policy violations.[41] Third, the policy allows de minimis, self-assessed cap, and max cap institutions to fully collateralize up to two cap breaches in two consecutive reserve-maintenance periods without violating the policy. Finally, a Reserve Bank has discretion to waive counseling for a violation in limited circumstances, such as an operational problem at a Reserve Bank.

C. Consequences of Policy Violations

Generally, a policy violation will initiate a series of Reserve Bank actions aimed at deterring an institution from exceeding its allowed capacity for intraday credit. These actions depend on the institution's history of daylight overdrafts and its financial condition. Initial actions taken by the Reserve Bank may include assessing the causes of the overdrafts, sending a counseling letter to the institution, and reviewing the institution's account-management practices. In addition, the

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[39] For institutions with accounts in more than one Federal Reserve District, an administrative Reserve Bank (ARB) is designated. The ARB coordinates the Federal Reserve's daylight overdraft monitoring activities for the consolidated accounts.

[40] In early 2012, the Federal Reserve will no longer consolidate FBO accounts across Reserve Banks for the purpose of assessing compliance with the PSR policy. State ring-fencing laws may diminish the ability of a Reserve Bank to perfect collateral pledged with another Reserve Bank, thus reducing the protection provided by the collateral against an intraday credit exposure. FBOs will have two options through which to make these changes: (1) function all activity through a single master account or (2) manage daylight overdrafts and collateral separately for each branch or agency. Reserve Banks will contact FBOs with more details prior to the change.

[41] The Federal Reserve's administrative counseling flexibility program is designed to assist relatively small institutions that frequently exceed their net debit caps as a result of transactions other than Fedwire funds transfers, NSS transactions, and ACH credit originations. Under administrative counseling flexibility, the Reserve Banks work with affected institutions to identify alternatives that would avoid or reduce daylight overdrafts caused by such transactions, but the Banks generally do not subject these institutions to escalated levels of counseling, require collateral, or assign a zero cap.

Reserve Bank may require an institution to submit documentation specifying actions it will take to address the overdraft problems. If policy violations continue to occur, the Reserve Bank may take additional actions. For example, if a financially healthy institution in the zero, exempt-from-filing, or de minimis cap category continues to breach its cap, the Reserve Bank may strongly recommend that the institution file a cap resolution or perform a self-assessment to obtain a higher net debit cap.

In situations in which an institution continues to violate the PSR policy and counseling and other Reserve Bank actions have been ineffective, the Reserve Bank may assign the institution a zero cap. In addition, the Reserve Bank may impose other account controls that it deems prudent, such as requiring the institution to pledge collateral; imposing balance requirements; rejecting Fedwire funds transfers or NSS transactions that would cause or increase an institution's daylight overdraft; or requiring the institution to prefund ACH credit originations. Reserve Banks also keep institutions' primary regulators apprised of any recurring overdraft problems.

D. Real-Time Monitoring and ABMS

The Reserve Banks use ABMS to monitor in real time the payment activity of institutions that may expose the Federal Reserve and other payment system participants to risk of loss. ABMS serves as both an information source and an account-monitoring and account-management tool. It allows institutions to obtain intraday balance and collateral information for purposes of managing their use of intraday credit, avoiding overnight overdrafts and monitoring in real time their collateralized and uncollateralized daylight overdraft balance. All institutions that have an electronic connection to the Reserve Banks' Fedwire Funds Service are able to access their intraday Federal Reserve account position in ABMS or in the AMI system.[42] While ABMS is not a substitute for institutions' own internal tracking and monitoring systems, it does provide real-time account information based on Fedwire funds and securities transfers and NSS transactions. Additionally, ABMS captures debits and credits resulting from other payment activity as those transactions are processed in the Reserve Bank's accounting system.[43]

ABMS also provides authorized Reserve Bank personnel with a mechanism to monitor and control account activity for selected institutions. The Reserve Banks may use ABMS to intercept or reject certain transactions from posting to an institution's account, a capability known as "real-time monitoring." Real-time monitoring allows the Reserve Banks to prevent an institution from transferring funds from an account that lacks sufficient funds to cover the

[42] AMI is a web-based application that provides institutions with real-time access to their intraday account and collateral balances, detailed transaction information, a variety of reports, and inquiry capabilities. Institutions can obtain more information on ABMS and AMI in the *Account Management Guide* at http://www.frbservices.org/serviceofferings/account/ami.html.

[43] ABMS receives transaction information from the Fedwire Funds Service, the Fedwire Securities Service, and the National Settlement Service in real time; information on cash, check, and Treasury Investment Program transactions at 5-minute intervals; and information on prefunded ACH credit originations every 15 minutes. ABMS receives updated collateral information, including an institution's value of collateral available for daylight overdraft purposes, from the Federal Reserve's Collateral Management System on a near-real-time basis. ABMS will use the collateral available for daylight overdraft purposes to calculate the institution's collateralized and uncollateralized daylight overdraft balances, which will also be updated on a near-real-time basis.

payment(s). If an institution's account is monitored in "reject" mode in ABMS, any outgoing Fedwire funds transfers or NSS transactions that exceed its available funds will be rejected. The institution will also be required to prefund its ACH credit originations when the Reserve Bank processes the items.[44] The Reserve Banks generally notify institutions before monitoring their accounts in real time.

ABMS calculates balances three ways so that institutions and Reserve Bank staff can take into account the effect of the daylight overdraft posting rules on an institution's payment activity. Generally, the daylight overdraft (DLOD) balance in ABMS reflects the balance in the account according to the transaction posting rules described in the PSR policy and is usually equivalent to the balance measured by DORPS.[45] A second balance calculated by ABMS, the account (ACCT) balance, reflects the sum of all transactions posted to ABMS regardless of the daylight overdraft posting rules. A third balance, the available funds (AVL FNDS) balance, shows funds available to an institution that include its daylight overdraft capacity.[46]

In addition, institutions can monitor their collateral balances, and collateralized and uncollateralized daylight overdraft positions in near-real-time in ABMS or in real-time in AMI. For more information on collateral under the PSR policy, see section III (Collateral).

[44] If the total amount of all ACH credit item originations exceeds the institution's account balance, none of the items will be processed. For further information on ACH prefunding, see Operating Circular 4: http://www.frbservices.org/regulations/operating_circulars.html.

[45] The schedule of posting rules is located in part II of the PSR policy, available at http://www.federalreserve.gov/paymentsystems/psr_policy.htm#daylightdef.

[46] For further information, see the *Account Management Guide* at http://www.frbservices.org/files/regulations/pdf/amg.pdf.

V. DAYLIGHT OVERDRAFT FEES

Regardless of its net debit cap level, an institution incurs daylight overdraft fees for any uncollateralized daylight overdrafts, subject to the fee-waiver provisions discussed below. Collateralized daylight overdrafts are assessed a zero fee. This section describes how daylight overdraft fees are calculated and assessed.

A. Calculation of Charges

In order to assess charges on uncollateralized daylight overdrafts, the Federal Reserve, through its automated applications, maintains minute-by-minute information on account holders' daylight overdraft and collateral balances.[47]

An institution's daily daylight overdraft charge is equal to the effective daily rate multiplied by the average uncollateralized daylight overdraft for the day. The Reserve Banks calculate and assess charges on the basis of two-week reserve maintenance periods. The charges are equal to the sum of daily uncollateralized daylight overdraft charges incurred minus the fee waiver for the maintenance period.[48]

[47] DORPS records each institution's end-of-minute daylight overdraft. CMS records information on each institution's end-of-minute value of FR collateral, less extensions of credit from the discount window. CMS sends this value to DORPS, which determines the amount of uncollateralized daylight overdrafts and performs the pricing calculations.

[48] Institutions incurring fees for a two-week reserve maintenance period over $150 will have their gross fees reduced by a flat $150 fee waiver. The fee waiver is not available for institutions that do not have regular access to the discount window.

Example of daylight overdraft charge calculation[49]

Calculate an institution's daily charge
A. Find the average daily uncollateralized daylight overdraft *Sum of end-of-minute uncollateralized overdrafts for one day* = $1,800,000,000 = $1,394,268 *official Fedwire day = 21.5 hours (or 1,291 minutes)* 1,291 B. Find the daily daylight overdraft charge *average daily uncollateralized overdraft =* $1,394,268 *multiplied by effective daily rate*[50] *= .0050 x (21.5/24) x (1/360) =* x .0000124 $17.29
Calculate an institution's reserve maintenance period charge and apply the fee waiver
A. Find the gross overdraft charge *Sum of daily overdraft charges* = $17.29 x *10 days per reserve maintenance period* = $172.90 B. Subtract the waiver from the gross overdraft charge for the period gross overdraft charge $172.90 *less* $150 fee waiver − $150.00 $22.90

Institutions without regular access to the discount window are not eligible for daylight overdrafts, zero price for collateralized daylight overdrafts, or the fee waiver. Such institutions are charged a penalty fee for any daylight overdrafts they incur. The daylight overdraft penalty rate is equal to the regular Federal Reserve daylight overdraft fee plus 100 basis points, or 150 basis points. Institutions without regular access are also subject to a minimum charge of $25.

B. Billing and Adjustments

At the end of each reserve maintenance period, the Reserve Bank provides a report of daylight overdraft charges to each institution that was assessed fees in that period. Eligible institutions whose period charges were under $150 will receive a report of their use of uncollateralized

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[49] The example assumes that the institution incurred $1.8 billion in uncollateralized daylight overdrafts, as measured by the sum of end-of-minute daylight overdraft amounts. For simplicity's sake, the example also assumes that the institution had identical activity for each day of a ten-day reserve maintenance period. Finally, the example assumes that the institution has regular access to the discount window.

[50] The effective daily daylight-overdraft rate is truncated to .0000124.

daylight overdrafts, but their assessed fees will be waived. The Federal Reserve makes an assessment of final charges to the institution's Federal Reserve account at the end of the period following the reserve maintenance period in which charges were assessed. Institutions may not use earnings credits to offset daylight overdraft charges.[51]

Adjustments to daylight overdraft charges may be appropriate in limited circumstances, such as extended technical or operational difficulties at a Reserve Bank.

[51] For further information on earnings credits, see Reserve Maintenance Manual at www.frbservices.org/files/regulations/pdf/rmm.pdf.

VI. Special Situations

Certain institutions are considered "special situations" because of their legal structure or payment activity. These institutions are subject to special rules and procedures, which are not detailed in this document. Institutions that fall into any of the categories discussed below should refer to the *Guide to the Federal Reserve's Payment System Risk Policy on Daylight Credit* for more information on compliance with the PSR policy.[52]

A. U.S. Branches and Agencies of Foreign Banks

For U.S. branches and agencies of foreign banks, the PSR policy includes separate procedures for determining the U.S. capital equivalency measure used in calculating net debit caps, and for eligible FBOs, a streamlined procedure for obtaining a max cap. The U.S. capital equivalency measure for these institutions is generally based on the foreign banking organization's capital and its strength of support assessment (SOSA) ranking or financial holding company status. The Federal Reserve regards capital information provided in connection with an FBO's daylight overdraft cap as confidential and will share this information only with the FBO's primary regulator and home country supervisor (5 U.S.C. § 552(b)).[53]

Each foreign bank "family"— consisting of all the U.S. branches and agencies of a particular foreign bank —has a single daylight overdraft cap that may be allocated among its U.S. offices. For purposes of measuring daylight overdrafts, the intraday account balances of all the branches and agencies in the family are consolidated, as described in section VI (Special Situations) of the *Guide to the Federal Reserve's Payment System Risk Policy on Daylight Credit*.[54] In addition, an administrative Reserve Bank is designated to coordinate the Federal Reserve's daylight overdraft monitoring activities for the foreign family.

B. Industrial Banks and Industrial Loan Companies Subject to the Bank Holding Company Act (BHCA) Exception

Industrial banks and industrial loan companies subject to the BHCA exception may not incur daylight overdrafts on behalf of affiliates, except under very limited circumstances.[55] An

[52] The Guide is available at http://www.federalreserve.gov/paymentsystems/psr_guide.htm.
[53] For more information on the Freedom of Information Act, see http://www.federalreserve.gov/generalinfo/foia/foiastat.cfm.
[54] In early 2012, the Federal Reserve will no longer consolidate FBO accounts across Reserve Banks for the purpose of assessing compliance with the PSR policy. State ring-fencing laws may diminish the ability of a Reserve Bank to perfect collateral pledged with another Reserve Bank, thus reducing the protection provided by the collateral against intraday exposure. FBOs will have two options for managing their accounts (1) function all activity through a single master account or (2) manage daylight overdrafts and collateral separately for each branch or agency. Reserve Banks will contact FBOs with more details prior to the change.
[55] See section VI of the *Guide to the Federal Reserve's Payment System Risk Policy on Daylight Credit* at http://www.federalreserve.gov/paymentsystems/psr_guide.htm for further information.

industrial bank or industrial loan company may lose its BHCA exception if it incurs prohibited overdrafts. In enforcing these restrictions, the Federal Reserve uses a separate formula for calculating intraday account position for these institutions.

C. Other Special Situations

Special rules and procedures also apply to bankers' banks that have not waived their exemption from the reserve requirement, limited-purpose trust companies, Edge and agreement corporations, and GSEs and international organizations.[56] These institutions do not have regular access to the discount window and therefore are not permitted to incur daylight overdrafts in their Federal Reserve accounts.[57] These entities are assigned a zero net debit cap. See section VI (Special Situations) of the Guide to the Federal Reserve's Payment System Risk Policy on Daylight Credit for further information.

[56] Bankers' banks, including corporate credit unions, are defined as depository institutions not required to maintain reserves under the Board's Regulation D (12 CFR 204) because they are organized and chartered solely to do business with other financial institutions and are owned primarily by the financial institutions they service.
[57] A bankers' bank that waives its exemption from reserve requirements may be eligible for a positive net debit cap.

GLOSSARY OF TERMS

Above-average cap - The cap category that permits an institution to incur daylight overdrafts on a single day up to 1.875 times its capital measure.

Account Balance Monitoring System (ABMS) - The Reserve Bank application that provides institutions that have an electronic connection to Fedwire with access to real-time account balance and collateral information. ABMS also allows Reserve Banks to monitor institutions' account balances and payment activity on a real-time basis and reject or intercept certain transactions. Also see real-time monitoring.

Account Management Information (AMI) - A web-based application that provides institutions with real-time access to their intraday account and collateral balances, detailed transaction information, reporting and inquiry capabilities as a priced service offered by the Reserve Banks. For further information refer to http://www.frbservices.org/serviceofferings/account/ami.html.

ACH - Automated Clearing House. An electronic batch-processing service used to disburse or collect funds.

Administrative Reserve Bank (ARB) - The Reserve Bank responsible for the administration of Federal Reserve credit, reserves, and risk-management policies for a given depository institution or other legal entity.

Affiliate - Any company that controls, is controlled by, or is under common control with, a bank or nonbank bank (according to Federal Reserve Regulation Y).

Agreement corporation - A corporate subsidiary of a federally chartered or state-chartered bank having an agreement or undertaking with the Board of Governors, under section 25 of the Federal Reserve Act, to engage in international banking and investments.

Average cap - The cap category that permits an institution to incur daylight overdrafts on a single day up to 1.125 times its capital measure.

Average daily daylight overdraft - The amount resulting from the division of the sum of an institution's negative Federal Reserve account balances at the end of each minute of the scheduled Fedwire operating day (with positive balances set to zero) by the total number of minutes in the scheduled Fedwire operating day.

Bank holding company (BHC) - Any company that has direct or indirect control over a bank. The Bank Holding Company Act provides a federal framework for the supervision and regulation of companies that own or control a bank. See pub. L. No. 100-86, 101 Stat. 552, available at http://www.fdic.gov/regulations/laws/rules/6000-100.html.

Bankers' bank - An institution organized and chartered solely to do business with other banks and primarily owned by the financial institutions that it services. The term includes corporate credit unions. A bankers' bank is a depository institution that is not required to maintain reserves under the Board's Regulation D (12 CFR 204). Bankers' banks do not take deposits or make loans to the public and are not eligible for discount window access unless they waive their exemption from reserve requirements.

Board of directors' resolution - A statement of intention to follow a course of action that is approved by a majority vote of a quorum of the board of directors of a corporation. In the context of the PSR policy, a board of directors' resolution would be adopted to convey approval to a Reserve Bank of a net debit cap category or max cap.

Board of Governors (Board) - The Board of Governors of the Federal Reserve System.

Book-entry securities transfer - Generally, an electronic transfer of Fedwire-eligible securities (such as securities issued by the U.S. Treasury, a government agency, or a GSE) over the Fedwire Securities Service.

Borrower-in-Custody (BIC) Arrangement **-** An agreement under which the pledging institution retains possession of assets being pledged as collateral but must designate the BIC collateral as being pledged to the Reserve Bank.

Cap - See *Net debit cap.*

Cap breach - An event in which the negative end-of-minute balance in an institution's Federal Reserve account on any day exceeds its net debit cap.

Cap category - An institution's category or class for purposes of determining its daylight overdraft limit, or net debit cap. There are six cap categories: zero, exempt-from-filing, de minimis, average, above average, and high. The average, above-average, and high cap categories are referred to as the self-assessed net debit caps. DIs with self-assessed caps may be eligible to apply for maximum daylight overdraft capacity (max cap).

Cap multiple - The factor associated with each cap category that is applied to capital for the purposes of calculating the net debit cap.

Capital measure - For institutions chartered in the United States, net debit caps are multiples of "qualifying" or similar capital measures that consist of those capital instruments that can be used to satisfy risk-based capital standards, as set forth in the capital adequacy guidelines of the federal financial regulatory agencies. The U.S. capital equivalency measures for branches and agencies of foreign banks are based on their strength of support assessment ranking and financial holding company status.

Collateral available for daylight overdraft purposes - An institution's value of collateral pledged to the Reserve Bank less the value of collateral used to secure any outstanding loan advances.

When assessing fees, the Federal Reserve compares, ex post, an institution's end-of-minute value of collateral available for daylight overdraft purposes with the institution's end-of-minute daylight overdraft to determine whether and how much of that minute's overdraft was collateralized. Institutions with access to ABMS or to AMI may view their collateral available for daylight overdraft purposes in near-real-time intraday.

Collateral Management System **-** The Federal Reserve's collateral inventory tracking and transaction-processing application that is used to record collateral pledged for discount window, payment system risk, and Treasury programs.

Collateral value **-** The amount of credit that the Federal Reserve will extend against the pledged asset. Collateral value is calculated by multiplying a pledged asset's observed market price or estimated fair value by the margin assigned to the asset by the Federal Reserve.

Collateralized capacity - The additional daylight overdraft capacity available to an institution with an approved max cap through the pledge of collateral. The collateralized capacity available to such an institution is calculated as the difference between the approved max cap and the institution's net debit cap. An institution with an approved max cap may, at any time, pledge collateral to use the collateralized capacity in part or in full.

Collateralized daylight overdraft - An institution's end-of-minute daylight overdraft if the institution's end-of-minute value of collateral available for daylight overdraft purposes meets or exceeds the value of its daylight overdraft for that minute. See collateral available for daylight overdraft purposes.

Competitive Equality Banking Act (CEBA) - A federal law enacted August 10, 1987, that, among other things, prohibits industrial banks and industrial loan companies from incurring daylight overdrafts in their Federal Reserve accounts on behalf of affiliates.

Corporate credit union **–** See *bankers' bank.*

Daylight overdraft - A negative balance in an institution's Federal Reserve account at any time during the Fedwire operating day.

Daylight Overdraft Reporting and Pricing System (DORPS) - The Reserve Bank application that measures, calculates, and assesses fees to institutions for their use of daylight overdrafts in their Federal Reserve accounts.

Depository Trust Company (DTC) **-** A limited-purpose trust company that acts as the central securities depository for most publicly traded equity securities and many fixed-income securities in the U.S. market. Each Reserve Bank has established a pledge account with DTC through which institutions may pledge securities for discount window and PSR purposes.

De minimis cap - The cap category that permits an institution to incur daylight overdrafts up to 40 percent of its capital measure.

Edge Act corporation - A corporate subsidiary of a domestic or foreign bank, established under section 25(a) of the Federal Reserve Act to engage in international banking and investments.

Effective daily rate - The annual rate charged for daylight overdrafts divided by 360 days, adjusted for the portion of the day during which the Fedwire funds transfer system normally operates.

End-of-minute balance - The balance in an institution's Federal Reserve account at the end of each minute as measured by DORPS for purposes of daylight overdraft reporting and pricing.

Exempt-from-filing cap - The cap category that permits an institution to incur daylight overdrafts up to the lesser of $10 million or 20 percent of its capital measure.

Fedwire - The Federal Reserve funds and book-entry government securities transfer system.

Fedwire Securities Service (FSS) - A system that provides safekeeping, transfer, and delivery-versus-payment settlement services for securities maintained on the books of the Reserve Banks. FSS maintains in electronic form all marketable U.S. Treasury securities, as well as many federal government agency, government-sponsored enterprise (GSE), and certain international organizations securities. Institutions may pledge eligible FSS securities to their Reserve Bank for discount window and PSR purposes.

Fee waiver - Institutions that incur fees for a two-week reserve maintenance period under $150 will not be assessed any fees, and institutions incurring fees for a two-week reserve maintenance period over $150 will have their gross fees reduced by $150. The fee waiver is not available for institutions that do not have regular access to the discount window.

Financial holding company (FHC) - The Gramm-Leach-Bliley Act (Public Law 106-102, 113 Stat. 1338 (1999)) defines a financial holding company as a bank holding company that meets certain eligibility requirements. In order for a bank holding company to become a financial holding company and be eligible to engage in the new activities authorized under the Gramm-Leach-Bliley Act, the act requires that all depository institutions controlled by the bank holding company be well capitalized and well managed (12 U.S.C. 1841(p)). With regard to a foreign bank that operates a branch or agency or owns or controls a commercial lending company in the United States, the act requires the Board to apply comparable capital and management standards that give due regard to the principle of national treatment and equality of competitive opportunity (12 U.S.C. 1843(l)).

Foreign banking organization (FBO) - (1) A foreign bank, as defined in section 1(b)(7) of the International Banking Act of 1978 (12 U.S.C. 3101(7)), that (a) operates a branch, agency, or commercial lending company subsidiary in the United States; (b) controls a bank in the United States; or (c) controls an Edge corporation acquired after March 5, 1987; and (2) any company of which the foreign bank is a subsidiary.

Fully collateralized cap breach waiver – An institution with a self-assessed or de minimis net debit cap may exceed its net debit cap without violating the policy if the institution has fully collateralized all cap breaches on a given day. Under the waiver, institutions may fully collateralize up to two cap breaches in two consecutive reserve maintenance periods (four weeks).

Government-sponsored enterprises (GSEs) - Corporations chartered by Congress to perform certain financial market functions deemed to be in the public interest. These entities include Fannie Mae, the Federal Home Loan Mortgage Corporation (Freddie Mac), entities of the Federal Home Loan Bank System (FHLBS), the Farm Credit System, the Federal Agricultural Mortgage Corporation (Farmer Mac), the Financing Corporation, and the Resolution Funding Corporation.

Gross overdraft charge **-** A daylight overdraft charge calculated, based on average overdrafts, before being reduced by the fee waiver for eligible institutions.

High cap - The cap category that permits an institution to incur daylight overdrafts on a single day up to 2.25 times its capital measure.

Industrial bank **-** An institution as defined in section 2(c)(2)(H) of the Bank Holding Company Act. In general, an industrial bank is a state-chartered finance company that makes loans and raises funds by selling investment certificates or investment shares to the public.

Industrial loan company (ILC) **-** An entity that is not a bank, as defined under the Bank Holding Company Act (BHCA), and that does not accept certain types of demand deposits, has less than $100 million in total assets, or has not undergone any change in control since the enactment of CEBA. An ILC is also excluded from the definition of bank under the BHCA if it does not “engage in any activity in which it was not lawfully engaged” before the enactment of CEBA.

International organizations - The Federal Reserve acts as fiscal agent for certain international organizations, the securities of which are Fedwire-eligible but are not obligations of, or fully guaranteed as to principal and interest by, the United States. The international organizations include the World Bank, the Inter-American Development Bank, the Asian Development Bank, and the African Development Bank.

In-transit securities - Book-entry securities transferred over the Fedwire Securities Service that have been purchased by a depository institution but not yet paid for and owned by the institution’s customers.

Limited-purpose trust company - For purposes of the PSR policy, a limited-purpose trust company is a trust company that is a member of the Federal Reserve System but that does not meet the definition of “depository institution” in section 19(b)(1)(A) of the Federal Reserve Act (12 U.S.C. 461(b)(1)(A)).

Liquidity **-** The ability to make payments as they become due in readily available funds.

Margin - A percentage applied to the observed market price or estimated fair market value of an asset to mitigate the risk that the observed market price or estimated market value of an asset will decline over time. The Federal Reserve's margins are based on risk characteristics of the pledged asset as well as the anticipated volatility of the fair market value of the pledged asset over an estimated liquidation time frame.

Maximum daylight overdraft capacity **-** An institution's net debit cap plus its collateralized capacity. (See *collateralized capacity*.) Only institutions with self-assessed net debit caps are eligible to request maximum daylight overdraft capacity from the Federal Reserve.

Net debit cap **-** The maximum dollar amount of collateralized and uncollateralized daylight overdrafts an institution is permitted to incur in its Federal Reserve account at any point in the day. The net debit cap is generally equal to an institution's capital measure times the cap multiple for its cap category.

Nonbank bank **-** In general, an institution that accepts deposits or makes commercial loans but does not engage in both activities. Any institution that became a bank as a result of the enactment of CEBA and was not controlled by a bank holding company on the day before CEBA was enacted.

Overdraft - See daylight overdraft, overnight overdraft.

Overnight overdraft **-** A negative position in a Federal Reserve account at the Reserve Bank's close of business. Overnight overdrafts are subject to a penalty fee.

Posting rules **-** A schedule used for determining the timing of debits and credits to an institution's Federal Reserve account for various transactions processed by the Reserve Banks.

PSR policy - The Federal Reserve Policy on Payment System Risk. Part II of the policy is relevant for purposes of this Overview. For further information refer to http://www.federalreserve.gov/paymentsystems/psr_policy.htm.

Real-time monitoring **-** The ABMS function used by Reserve Banks to monitor an institution's Federal Reserve account balance as transactions occur throughout the day and to reject or intercept outgoing funds transfers when they would cause an overdraft in an institution's Federal Reserve account.

Reserve maintenance period **-** A two-week period beginning on a Thursday and ending on a Wednesday over which most depository institutions must maintain required reserves and over which daylight overdrafts are monitored and charges may be assessed. Institutions that file a quarterly FR 2900 deposit report have a seven-day reserve maintenance period.

Risk-based capital - The "qualifying" or similar capital measure used to satisfy risk-based capital standards, as set forth in the capital adequacy guidelines of the federal financial regulatory agencies. Generally, for domestic banks the relevant capital measure is

Tier I plus Tier II capital.

Self-assessment **-** A process by which a depository institution assesses its creditworthiness, intraday funds management, operational controls, contingency procedures, and credit policies to determine its appropriate cap category for daylight overdraft purposes.

Self-assessed cap **-** One of three cap categories for which institutions are required to complete a self-assessment. The self-assessment cap categories are average, above average, or high.

Third-Party Custody Pledging Arrangements **-** An institution may designate a third-party custodian to provide collateral custody services. Third-party custody arrangements involve an institution (borrower), another institution that holds the assets to be pledged (custodian), and the Reserve Bank (lender).

Treasury Tax and Loan (TT&L) **-** A program in which institutions collect tax payments or deposits on behalf of Treasury. Institutions must cover the funds with collateral and must pay Treasury interest for use of the funds. Collateral pledged for this program is held in the TT&L account, which is separate from an institution's Federal Reserve account.

Uncollateralized daylight overdraft - An institution's end-of-minute daylight overdraft if the institution's end-of-minute value of collateral available for daylight overdraft purposes is less than the value of its daylight overdraft for that minute. See collateral available for daylight overdraft purposes.

U.S. capital equivalency **-** Capital measure applied to U.S. branches and agencies of foreign banks for purposes of calculating net debit caps and the deductible used to calculate daylight overdraft charges.

Zero cap **-** The cap category for which daylight overdrafts are not permitted. An institution may voluntarily adopt this cap category, or a Reserve Bank may assign a zero cap to certain institutions.