# Federal Reserve Notes

**FEDERAL RESERVE BANK OF SAN FRANCISCO • JUNE 1976**

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## REDLINING REGULATION ISSUED BY BOARD

The new "redlining" regulation to implement the Home Mortgage Disclosure Act of 1975 has been approved by the Federal Reserve Board of Governors. This Regulation C requires institutions active in the mortgage lending field to start disclosing the areas where they make their mortgage loans.

The Home Mortgage Disclosure Act, which takes effect on June 28, represents an attempt to eliminate "redlining"—the practice of refusing to lend mortgage money on property because it is in a certain geographic area. Generally redlining has affected older inner-city neighborhoods. The act and the regulation specify that nothing in them is meant to encourage unsound lending practices or the allocation of credit.

An estimated 4,400 commercial banks, along with 3,000 savings and loan associations, 470 mutual savings banks and 600 credit unions, are covered by the act. The Fed was responsible for writing the regulation, but enforcement lies in the hands of the appropriate Federal regulatory agencies.

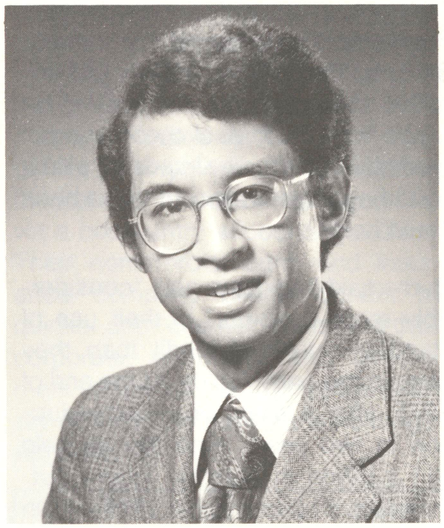
Regulation C affects federally insured or regulated institutions with $10 million or more in assets, which have offices in Standard Metropolitan Statistical Areas (SMSAs) and which make first mortgage loans on one-to-four family residences. The regulation requires institutions subject to the act to disclose publicly where their mortgage loans are made—by zip code, in initial disclosure statements for fiscal years ending before July 1, and by Census tracts thereafter.

The regulation requires breakdown of the disclosed mortgage-loan information into two main categories. The first covers loans made originally by an institution. The second covers loans originated by another, but purchased by the institution. Within each of these categories, loan data are further divided according to whether the loans are on property located within SMSAs where the lenders' headquarters or branches are located, or outside of those SMSAs.

In the case of loans on one-to-four family residences, the data must be broken down into: loans insured or guaranteed by the Federal Housing Administration, the Veterans Administration and the Farmers Home Administration; conventional mortgage loans; home improvement loans. Loans on multifamily dwellings are to be reported separately.

The final regulation differed in several respects from the proposed regulation. First, the final regulation extended the compliance date for reporting from August 30 to September 30. It also required lenders to take affirmative action in notifying depositors of the date of availability of mortgage-loan disclosure, and of the name and address of each institution's Federal enforcement agency. Another change narrowed the definition of a mortgage loan to exclude junior liens (except for home improvement loans), as well as first mortgages taken as additional collateral for business purposes.

Copies of Regulation C have been mailed to all commercial banks in the Twelfth District. Additional copies of the Regulation are available at your nearest Fed office.



**K.A. Grant**

## GRANT NAMED DIRECTOR OF COMPUTER SYSTEMS

Kenneth A. Grant has been named Director of Computer Systems with the Computer Services Group of the Federal Reserve Bank of San Francisco.

In this senior officer capacity, he is responsible for the development of the bank's computerized information systems. These systems support all of the bank's operations—including check processing, electronic funds transfer and economic research.

Grant joined the San Francisco Fed's Research Department in 1968 and was subsequently promoted to Assistant Vice President in 1971. He has been actively involved in the Fed's electronic funds transfer efforts for many years and serves on several System committees.

A graduate of the University of California at Berkeley, he received a B.S. degree in computer sciences.

## BURNS OPPOSES STRICT CREDIT LETTER LAW

Legislation that would severely limit the use of standby letters of credit, ineligible acceptances and related instruments has been opposed by Federal Reserve Chairman Arthur Burns, on the grounds that it might hurt the competitive position of American business.

Chairman Burns outlined his position in correspondence to Senator William Proxmire, Chairman of the Senate Banking Committee, and in subsequent committee testimony. The bill would limit the use of these various credit instruments by imposing a limit on the aggregate amount that a bank could hold.

Burns said banks are now "considerably more cautious" in their use of standby letters of credit than they were in the early 1970s. At the end of 1975, after a sharp one-third reduction in two years' time, banks held $11.3 billion in standby letters outstanding. Of this amount $675 million represented guarantees for documented discount notes, which are bank letters of credit that businesses use to support their own notes sold in the market.

Standby letters of credit came to national attention when they figured prominently in the failure of United States National Bank of San Diego. As a result, Federal agencies tightened regulations by requiring that outstanding standby letters of credit and related instruments be subject to individual customer loan limits and disclosed in footnotes to bank financial statements.

In commenting on legislation that would further restrict these instruments, Chairman Burns said that the Fed agrees with the basic thrust of the committee bill. But he said that the proposed legislation is not necessary because of the effectiveness of existing regulations, as well as the ability of regulators to take further steps to control these instruments.

Burns said, "The aggregate amount outstanding of standby letters of credit relative to documented discount notes is significant, since it underscores the fact that standby letters of credit are used for a variety of purposes, and that not all such instruments are inherently risky." He added that it is a standard bank practice for a foreign corporation or bank to require a standby letter of credit before conducting business with an unknown United States corporation.

"Upon reviewing the usage of such standby letters of credit, the Board is of the view that a regulation or statute that would limit such instruments in a blanket fashion might place U.S. businesses at an unnecessary competitive disadvantage in foreign markets," he said. Furthermore, he added, a restriction on such instruments might also jeopardize the ability of banks to service their domestic customers.

## QUESTIONS & ANSWERS ON MARGIN ACCOUNTS

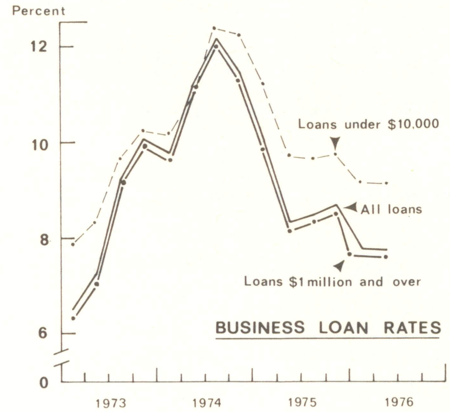
A newly revised "Questions and Answers" publication on Regulation U is now available from the Federal Reserve Bank of San Francisco.

Regulation U covers credit by banks for the purpose of purchasing or carrying margin accounts. "Questions and Answers" is useful to prospective borrowers who may be subject to the regulation, but the publication is intended mainly for the use of banks.

The 24-page publication covers nine general subject areas. Among them are the general features of Reg U, the nature of credit restrictions and other limitations, exempt credit, transactions by a bank as trustee, exempt transactions with and for broker-dealers, and general prohibitions against credit to broker-dealers by nonmember banks.

As the publication points out, "Questions and Answers" should be regarded only as a general aid to better understanding of the principal features of margin stock credit, rather than as an exhaustive explanation of the application of the regulation. Each given case must be considered in the light of the specific circumstances involved. Nevertheless, the publication brings Reg U into perspective, and serves as a primer for bankers who want to know more about margin accounts.

## BUSINESS LOAN RATES DECLINE IN MAY




Business-loan rates declined at Western banks between February and May, according to the latest quarterly survey of the Federal Reserve Bank of San Francisco. The survey failed to pick up the recent two-step rise in the prime rate to 7.25 percent from 6.75 percent, which occurred after the May survey period. But while lower average interest costs were reported on all loan-size categories, the reductions were relatively small compared to the declines reported in the February survey.

The average rate on regular short-term business loans reached 7.75 percent in May—a drop of only 2 basis points over the last three months, compared to the 90-point decline in the November-February period. (One hundred basis points equal one percentage point.) The average rate on revolving-credit loans fell to 7.15 percent—a 17-basis point decline compared to an 83-point decline observed in the February survey.

In the recent survey period, the thirteen West Coast banks in the sample reported 1,824 short-term and revolving-credit loans, totaling $603 million dollars. Both the number and total amount were down from three months ago, and substantially below year-ago levels, reflecting the continued weakness of business-loan demand nationwide.

## FED CLARIFIES EQUAL CREDIT RULES

The Federal Reserve Board of Governors has issued a clarification of Regulation B to aid consumer borrowers, and also to reduce reporting burdens for businesses in complying with the Equal Credit Opportunity Act.

As originally written, the Regulation could be interpreted to require credit reporting agencies to maintain two separate files for married couples sharing a credit account. The regulation could also be construed to require reporting credit information twice—once in the name of the husband and again in the name of the wife. The proposed amendment would eliminate this possible interpretation.

The Equal Credit Opportunity Act forbids creditors from discriminating against anyone on the basis of sex or marital status in any respect of a credit transaction. Regulation B deals with the furnishing of credit information by creditors to consumer reporting agencies.

The regulation was designed to remove an obstacle that many women have encountered in attempting to obtain credit, namely, the lack of a credit history. Creditors traditionally have reported information relating to the accounts of married couples in the husband's name only. Because of this, only the husband accumulated a credit history. If a divorced or widowed woman ever needed to obtain credit on her own, she would lack the necessary credit documentation.

Regulation B, as written, says that a creditor should report information concerning the account to a consumer reporting agency "in a manner which will enable the agencies to provide access to information about the account in the name of each spouse." But in the Board's view, the separate files that would be established for married women under the existing regulation could be incomplete.

When credit information about a shared account is reported under the wife's name, it would be placed in her separate file, but the wife's separate file would not contain undesignated information about the couple's prior credit experience. All existing information currently is undesignated. But consumer reporting agencies argue that duplication of credit information would result in an increase in the cost of credit to the consumer.

Under the Board's amended regulation, creditors will be required to mail or deliver an explanatory notice to their customers between November 1, 1976 and February 1, 1977. The notice, which is entitled "Credit History for Married Persons," discusses the traditional practice of reporting credit information in the husband's name only. It also explains that if a customer wishes to create a credit history for both spouses, he or she may sign the detachable request form and return it to the creditor. A married woman who is credit-worthy will also be able to establish her own separate file by opening her own individual accounts.

## BANKING TRENDS IN THE EAST

New York state banking authorities this month for the first time permitted mutual savings banks to offer demand-deposit accounts. This follows the authorization in January of statewide commercial-bank branching, as well as several years of exposure to the NOW accounts offered in neighboring New England.

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Many Eastern banks, having tried low- or no-cost checking accounts in recent years, comment that they are trending back toward service charges on demand accounts. What's the reason? Most people questioned cite increased activity without corresponding increase in balances, greater incidence of overdrafts, and declining sales of money orders and cashiers checks.

* * *

Bankers from institutions ranging in total assets size from $100 million through $400 million appear to have the most "Back room" trouble with movement of cash, checks and due to/due from accounts. Lost items and erroneous entries seem to occur among this group with greater frequency than at smaller institutions (which purchase many operational services from their city correspondents) or at the larger city banks.

* * *

"Limited Purpose Trust" companies have grown in number since the admission of Depository Trust Company, Manhattan, to membership in the Federal Reserve System in 1973. There are currently four such companies in New York City, facilitating the transfer of customers' securities via a book-entry accounting system. Their commercial bank and insurance company clients benefit by quicker and "cleaner" transfer of their corporate, municipal, and government securities, since physical delivery of these instruments is no longer required.

"The need for a strong monetary authority to discipline the inflationary tendency inherent in modern economies is evident from the historical experience of the nations around the world. Among the major industrial countries, West Germany and the United States appear to have achieved the greatest success—albeit woefully insufficient success—in resisting inflationary pressures in the period since World War II. It is no accident that both countries have strong central banks. In some other countries, where the monetary authority is dominated by the executive or the legislature, inflationary financial policies have brought economic chaos and even extinguished political freedom.

"It is, of course, essential that the monetary authority observe the spirit as well as the letter of our laws. In our democratic society the independence of a governmental agency can never be absolute. The Federal Reserve System is thus subject not only to the provisions of the Federal Reserve Act, but also to the Employment Act and numerous other statutes."

Arthur F. Burns
*The Independence of the Federal Reserve System*
May 22, 1976

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## TENTH YEAR FOR COST DATA

The Federal Reserve Bank of San Francisco has completed its 1975 Functional Cost Analysis Program, marking the end of the first decade that this free service has been available to Twelfth District member banks. Originally the program was designed for small banks, but large banks have also found FCA increasingly useful.

Participating banks are grouped in one of three deposit-size categories—up to $50 million, $50-$200 million, and over $200 million. Participants furnish deposit-structure and other characteristics, which permit grouping of institutions of like size to facilitate comparisons.

The annual *Average Banks* publication includes cost ratios which help participants to compare their own results with those of other District member banks as well as member banks nationwide. These ratios provide an important bank-management tool for use in forming policy and operating decisions and implementing cost controls.

The FCA program is continually being revised, and suggestions regarding further revisions are solicited from member banks to keep the program relevant to today's banking community. In essence, the program belongs to members, with the Fed acting as a coordinator.

Any individual interested in receiving a free copy of the 1975 *Average Banks* report should write to:

Functional Cost Analyst
Bank and Public Relations
Federal Reserve Bank
of San Francisco
P.O. Box 7702
San Francisco, CA 94120

## MURPHY NAMED VISITING SCHOLAR

Professor Neil B. Murphy of the University of Maine has been appointed to serve a seven-month term as a Visiting Scholar at the Federal Reserve Bank of San Francisco.

The Visiting Scholar position was inaugurated at the San Francisco Fed in 1974 to encourage the interchange of ideas between academic and Fed economists. Scholars from Stanford, Ohio State, the University of Chicago and the University of Oregon have recently held such appointments with the bank.

Dr. Murphy is Maine Bankers Association Professor of Finance at the University of Maine. In 1975 he was Visiting Professor of Finance and Economics at the Amos Tuck School of Business Administration at Dartmouth College.

Dr. Murphy has lectured widely at a number of universities—Howard, Maryland, Illinois, George Washington, Georgetown, and Bucknell. Prior to his academic career, he served as an economist with the Federal Reserve Bank of Boston, Leasco Systems and Research Corporation, and the Federal Deposit Insurance Corporation, where he was Chief of the Economic Research Unit. In 1971 he served as Staff Economist on the President's Commission on Financial Structure and Regulation, known as the Hunt Commission.

Dr. Murphy was an Associate Editor of the *Journal of Finance* and is currently a member of the Editorial Advisory Board of the *Journal of Bank Research*. He is in the process of writing two textbooks entitled *Bank Credit Cards*, and *Money and Financial Institutions*.