

Minutes of actions taken by the Board of Governors of the Federal Reserve System on Thursday, July 21, 1955. The Board met in the Board Room at 9:30 a.m.

PRESENT: Mr. Martin, Chairman
 Mr. Balderston, Vice Chairman
 Mr. Szymczak
 Mr. Vardaman
 Mr. Shepardson

Mr. Carpenter, Secretary
 Mr. Sherman, Assistant Secretary
 Mr. Kenyon, Assistant Secretary
 Mr. Thurston, Assistant to the Board
 Mr. Riefler, Assistant to the Chairman
 Mr. Leonard, Director, Division of Bank Operations
 Mr. Sloan, Director, Division of Examinations
 Mr. Solomon, Assistant General Counsel
 Mr. Koch, Assistant Director, Division of Research and Statistics
 Mr. Horbett, Assistant Director, Division of Bank Operations

The following matters, which had been circulated to the members of the Board, were presented for consideration and the action taken in each instance was as indicated:

Letter to Mr. Crosse, Assistant Vice President, Federal Reserve Bank of New York, reading as follows:

Reference is made to your letter of July 12, 1955, regarding the request of the Marine Midland Trust Company of Central New York, Syracuse, New York, for an extension of time within which it may establish a branch in the Northern Lights Shopping Center at a site approximately 400 feet east of the junction of State Route 11 and County Road 208, Town of Salina, Onondaga County, New York.

It is noted that several problems have arisen in connection with the completion of the shopping center, which

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will delay its opening until December 1, 1955, and the bank's management feels that conditions will not be satisfactory for the opening of the branch until January 1956.

After consideration of the information submitted, the Board concurs in your recommendation and extends to January 3, 1956, the time within which the Marine Midland Trust Company of Central New York, Syracuse, New York, may establish the above described branch.

Approved unanimously.

Letter to Mr. Jesse W. Tapp, Chairman, Board of Directors, Bank of America, New York, New York, reading as follows:

Reference is made to Mr. Ferroggiaro's letter of May 18, 1955, regarding the report of examination of Bank of America made as of December 3, 1954, by examiners for the Board of Governors of the Federal Reserve System.

The Board is pleased to note that the examiner's miscellaneous recommendations and suggestions (pages 18-19) are now being followed, that your bank will comply with the recommendation regarding purpose statements on loans (page 15), and that dealings in platinum and palladium have been discontinued (page 17).

The comments regarding the examiner's remarks about large concentrations of credit, particularly large accommodations to clients in Brazil and Colombia, have been carefully noted, as well as the reductions which have been effected in such outstandings as of May 11, 1955.

The matter of audit and control has been the subject of critical comment in each report of examination of your Bank. The examiner has again recommended that an audit or control officer of official rank--without operating duties or responsibilities--be appointed and stationed full time at the Home Office in New York with appropriate authority and direct reporting responsibilities to the Board of Directors (page 17).

With regard to Mr. Ferroggiaro's remarks regarding the audit and control system used by Bank of America NT&SA, it is felt that Bank of America, New York, has now reached such

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size that a resident control officer with appropriate authority and responsibilities should be appointed.

It is the view of the Board of Governors that reports of inspection of the Home Office and branches of Bank of America should be presented and considered by the Board of Directors and that appropriate notation thereof should be made in the minutes.

With reference to the Transferable Sterling Account maintained with Bank of America NT&SA in the name of Mr. Max Roesti, Pelikanstrasse 19, Zurich, Switzerland, when, in fact, the account is actually that of Bank of America, New York, the Board of Governors would be disposed to regard this arrangement as objectionable unless the British exchange control authority is informed regarding the beneficial owner of the deposit account.

With regard to the various deposit, loan, and acceptance accounts which were regarded by the examiner as apparent violations of section 25(a) of the Federal Reserve Act and/or Regulation K issued thereunder, Mr. Ferroggiaro's comments have been noted. The Board will defer further action thereon pending consideration of the proposed revision of Regulation K which has been prepared in implementation of the recommendation of the Special Committee on Foreign Operations of American Banks. This Committee, as you will recall, has been considering, among other things, activities that are appropriate and inappropriate for Edge Banks. A copy of the proposed revised regulation was submitted to your bank for review and comment on July 13.

Approved unanimously, with
copies to the Federal Reserve
Banks of New York and San Francisco.

Letter to Mr. Hill, Vice President, Federal Reserve Bank of Philadelphia, reading as follows:

Reference is made to your letter of July 12, 1955, and enclosures with respect to the retirement by the Camden Trust Company, Camden, New Jersey, of \$50,000 par value preferred stock on August 1, 1955.

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After considering the information submitted and your favorable recommendation, the Board of Governors gives its prior consent to the proposed retirement of \$50,000 preferred stock by the Trust Company.

It is understood that Counsel for the Reserve Bank will review and satisfy himself as to the legality of all steps taken in effecting the retirement.

Approved unanimously.

Letters to Mr. Armistead, Vice President, Federal Reserve Bank of Richmond, reading as follows:

In view of the information submitted with your letter of July 11, 1955, and the Reserve Bank's favorable recommendation, the Board of Governors extends until December 31, 1955, the time within which The Liberty Trust Company, Cumberland, Maryland, may establish a branch on U. S. Highway 40, about four and one-half miles west of its main office in an area known as the LaVale section, Allegany County, Maryland.

In view of the information submitted with your letter of July 11, 1955, and the Reserve Bank's favorable recommendation, the Board of Governors further extends until November 1, 1955, the time within which Randallstown Bank, Randallstown, Maryland, may establish a branch in a shopping center at Woodmoor on the south side of Liberty Road in Baltimore County, Maryland, under the authorization contained in its letters of April 19 and July 19, 1954.

Approved unanimously.

Letter to Mr. Diercks, Vice President, Federal Reserve Bank of Chicago, reading as follows:

Reference is made to your letter of July 11, 1955, regarding the request of the Security Bank, Lincoln Park, Michigan, for an extension of time within which to establish a branch on Dix Road between Euclid and Russell Streets in Lincoln Park, Michigan.

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After consideration of the information submitted, the Board concurs in your recommendation and extends to December 31, 1955, the time within which the Security Bank may establish the above-described branch, as originally approved in the Board's letter of October 6, 1954.

Approved unanimously.

Letter to Mr. Johns, President, Federal Reserve Bank of St. Louis, reading as follows:

This refers to your letter of July 8 regarding the propriety of furnishing credit information to the Small Business Administration concerning an applicant to whom your Bank had some years ago issued a commitment under Section 13b to commercial bank lenders.

The general statement of policy adopted by the Presidents at their June 21-22, 1954, Conference, and concurred in by the Board, included a provision that a Federal Reserve Bank may furnish credit information to appropriate parties where the information relates to borrowers in cases in which a Federal Reserve Bank is the sole lending institution involved in the extension of credit. Accordingly, it would seem that where a Reserve Bank had issued a 13b loan commitment to a commercial bank any request for credit information concerning the borrower should be referred to the financing institution.

However, since in this instance the Small Business Administration was aware of the fact that its applicant had previously been a 13b borrower and has asked merely for a statement of your experience with the loan, the Board agrees with you that there is no reason why the information should not be furnished.

Approved unanimously.

Letter to Mr. Pondrom, Vice President, Federal Reserve Bank of Dallas, reading as follows:

The Board of Governors of the Federal Reserve System has considered the recommendation of your Bank, contained in your letter of July 1, 1955, and, pursuant to the provisions of Section 19 of the Federal Reserve Act, grants permission to First State Bank of Green's Bayou, now located outside the

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city limits of Houston, Texas, to maintain the same reserves against deposits as are required to be maintained by banks outside of central reserve and reserve cities, effective as of the date the subject bank moves to its new location within the city limits of Houston.

Please advise the bank of the Board's action in this matter, calling its attention to the fact that such permission is subject to revocation by the Board of Governors of the Federal Reserve System.

Approved unanimously.

Letter to the Board of Directors, California Bank, Los Angeles, California, reading as follows:

Pursuant to your request submitted through the Federal Reserve Bank of San Francisco, the Board of Governors approves the establishment of branches by California Bank at 175 East Badillo Street, Covina, and at 1144 East Garvey Boulevard, West Covina, California, provided (a) a merger with The Covina National Bank is effected substantially in accordance with the terms of the proposed merger agreement submitted with your application, and (b) the branches are established within six months from the date of this letter.

Approved unanimously,
for transmittal through the
Federal Reserve Bank of San
Francisco.

Letter to the Comptroller of the Currency, Treasury Department, Washington, D. C., (Attention: Mr. W. M. Taylor, Deputy Comptroller of the Currency), reading as follows:

Reference is made to a letter from your office dated May 19, 1955, enclosing photostatic copies of an application to organize a national bank at Waynesboro, Virginia, and requesting a recommendation as to whether or not the application should be approved.

Information contained in a report of investigation of the application, made by an examiner for the Federal Reserve Bank of Richmond, discloses generally favorable findings with respect to the proposed capital structure of the bank, its ability

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to obtain a sufficient volume of business to be able to operate profitably within a reasonable length of time, and the character of its management. However, it is reported that the two existing banks in Waynesboro are rendering adequate service in the area, and there is no evidence that the public needs another bank. After considering the information available, the Board of Governors does not feel justified in recommending approval of the application.

The Board's Division of Examinations will be glad to discuss any aspects of this case with representatives of your office, if you so desire.

Approved unanimously.

There had been circulated to the members of the Board a draft of letter to the Chairman of the House Committee on the Judiciary commenting on bill H. R. 6121, which would amend section 610 of title 18 of the United States Code. Whereas section 610 now prohibits a national bank or corporation organized by authority of any law of Congress from making a contribution or expenditure in connection with any election to a political office, H. R. 6121 would broaden the prohibition to include contributions or expenditures in connection with any election, including one in which any issue is submitted for approval or disapproval by the voters. The draft would state that the Board had no objection to the proposed legislation.

Following a discussion during which reference was made to the broad scope of the bill, unanimous approval was given to the following letter for the signature of Chairman Martin to the Honorable Rowland R. Hughes, Director of the Bureau of the Budget:

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In compliance with the request received from the House Committee on the Judiciary, the Board has prepared the enclosed report on the bill H. R. 6121, "To amend section 610 of title 18 of the United States Code so as to broaden the coverage of its provisions prohibiting election expenditures by national banks and corporations organized under Federal law."

Before transmitting this report, the Board will appreciate advice as to the relationship of the proposed legislation to the program of the President.

At the meeting of the Board on June 22, 1955, it was understood that a letter would be sent to the Federal Reserve Banks setting forth the Board's views regarding the absorption of banks through a procedure involving the acquisition of shares of stock. Accordingly, the following letter to the Presidents of all Federal Reserve Banks had been drafted and had been circulated to the members of the Board:

Occasionally, during recent years, a bank has absorbed another bank through a procedure that involves, as one step in the absorption, the temporary acquisition (directly or through an agent) of all or most of the stock of the latter. It is understood that the chief reason for proceeding in that manner, rather than through direct acquisition of the assets and assumption of the liabilities of the liquidating bank, has been to avoid corporate income taxes that otherwise would be payable by the liquidating bank on capital gains realized from the sale of its appreciated assets, such as the bank building and investment securities.

In the supervision of member State banks, the described practice causes difficulty because of the possible conflict with Federal statutes (R.S. § 5136; Fed. Res. Act § 9) which prohibit national banks and member State banks from purchasing for their own account "any shares of stock of any corporation", with specified exceptions.

The statutory prohibition, it is believed, was aimed principally at investment of bank funds in corporate stock, because

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Congress considered corporate stocks, generally speaking, to involve speculative risks and dangers of wide fluctuations in price which made them inappropriate as bank investments. Accordingly, the statutory prohibition against purchase of corporate stocks might justifiably be regarded as not applying to a temporary acquisition in the course of an absorption, when such acquisition is followed promptly by a take-over of assets and assumption of liabilities. However, the Board of Governors wishes to avoid, as far as possible, what might appear to be approval of even momentary, insignificant, and "technical" violations of law. As indicated in the attachment hereto, the Internal Revenue Code of 1954 apparently eliminated the tax disadvantage of the ordinary purchase-and-assumption arrangement, so that the tax-avoidance reason for absorbing another bank via acquisition of its stock no longer exists.

Accordingly, when a member bank proposes to absorb another bank and may intend to do so through the stock-acquisition procedure, it should be informed that the Board of Governors looks with disfavor upon that practice, except where unusual circumstances are present that clearly justify its use. In the event the parties are under the impression that a substantial additional tax will be payable unless the stock-acquisition technique is followed, their attention should be directed to the information in the attachment. Needless to say, neither the Board of Governors nor the Reserve Banks are in a position to make authoritative tax rulings, but it may be sufficient in these cases to point out that the 1954 Internal Revenue Code made significant changes in this respect, so that the banks and their tax advisers may study the matter further or submit the question to the Internal Revenue Service for a specific ruling.

Approved unanimously.

There was presented for consideration a memorandum from Mr. Carpenter dated July 11, 1955, listing the various members of the Board's staff having assignments as associates of subcommittees of the Presidents' Conference. The memorandum, which had been circulated to the members of the Board, was prepared in view of letters from the chairmen of two Conference committees

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requesting that the members of the Board's staff currently serving as subcommittee associates be permitted to continue to serve during the year beginning July 1, 1955.

Unanimous approval was given to letters as follows, with the understanding that if the chairmen of other Presidents' Conference committees should inquire about the service of Board staff members as associates of various subcommittees, similar letters would be prepared and submitted to the Board:

To Mr. Earhart, Chairman, Presidents' Conference Committee on Miscellaneous Operations

It is entirely agreeable to the Board for Messrs. Myrick and Bethea to continue to serve as associates of the subcommittees of the Presidents' Conference on Miscellaneous Operations, referred to in your letter of June 28, 1955.

To Mr. Leach, Chairman, Presidents' Conference Committee on Fiscal Agency Operations

It is entirely agreeable to the Board for Messrs. Vest and Myrick to continue to serve as associates of the respective subcommittees of the Committee on Fiscal Agency Operations of the Conference of Presidents specified in your letter of June 28, 1955.

Reference was made to a memorandum dated July 15, 1955, from Mr. Young, Director, Division of Research and Statistics, recommending that the Board authorize publishing in pamphlet form the reports of the five consultant groups organized by the Board at the request of the Congressional Joint Subcommittee on Economic Statistics (the "Talle Subcommittee") to evaluate available statistics in the fields of consumer expectations,

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savings, inventories, business plant and equipment expenditure expectations, and general business expectations. The memorandum, which had been circulated to the members of the Board and which was submitted as the result of preliminary discussion at the meeting on June 23, 1955, stated that according to a letter from the Chairman of the Subcommittee publication of the reports by the Board would contribute to the usefulness of the reports, both at the time of the Subcommittee hearings and later. The memorandum also stated that the cost of 1,000 copies of each of the five pamphlets was estimated at about \$8,400.

The recommendation contained in Mr. Young's memorandum was approved unanimously.

Consideration was given to (1) the application of Quincy Trust Company, Quincy, Massachusetts, for permission to establish a branch in South Weymouth, Massachusetts, and (2) the application of Granite Trust Company, Quincy, Massachusetts, for permission to establish a branch in North Weymouth. The application of Quincy Trust Company had been considered by the Board previously and was the subject of a meeting with representatives of the trust company on June 23, 1955. Originally, both the Federal Reserve Bank of Boston and the Board's Division of Examinations recommended unfavorably. However, in the light of developments, including the application of Granite Trust Company for a branch in North Weymouth, the Division of Examinations now recommended that the application be granted. The Division also recommended favorably with respect to the

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Granite Trust Company application. The files on both of the matters had been circulated to the members of the Board prior to this meeting.

Mr. Sloan said the Boston Reserve Bank felt at first that if Quincy Trust Company wished to establish a branch in the Town of Weymouth, a location in the northern part of the town would be preferable, but that in view of Granite Trust Company's application to establish a branch in that section of the town, the Boston Bank was now agreeable to favorable action on Quincy Trust Company's application. This conclusion, he said, had also been reached by the Division of Examinations. He pointed out that approval of Granite Trust Company's application would give that institution four branches in the Town of Weymouth, that these would be the only commercial banking facilities in Weymouth unless the Quincy Trust Company's application was approved, and that neither trust company was understood to desire any additional offices in Weymouth.

In a discussion which followed, Mr. Sloan stated, in response to a question by Chairman Martin, that in his opinion establishment of the two branches would not result in an overbanked condition. In response to a question by Governor Shepardson, he said that Quincy Trust Company did not care to establish a branch in North Weymouth, since it felt that the area could be served from its head office and that South Weymouth offered a greater potential for branch operations.

It was noted that Governor Robertson had initialed the files relating to the two applications, and the matter was then discussed further

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in the light of the action taken by the Board on July 14, 1955, concerning the application of California Bank, Los Angeles, California, to establish a branch in Fullerton, California.

At the conclusion of the discussion, unanimous approval was given to letters as follows, for transmittal through the Federal Reserve Bank of Boston:

Letter to the Board of Directors, Quincy Trust Company, Quincy, Massachusetts

Pursuant to your request submitted through the Federal Reserve Bank of Boston, the Board of Governors approves the establishment of a branch at 106 Pleasant Street, South Weymouth, a section of the Town of Weymouth, Massachusetts, by the Quincy Trust Company, Quincy, Massachusetts, provided the branch is established within six months from the date of this letter.

Letter to the Board of Directors, Granite Trust Company, Quincy, Massachusetts

Pursuant to your request submitted through the Federal Reserve Bank of Boston, the Board of Governors approves the establishment of a branch in that section of the town of Weymouth, Massachusetts, which is commonly known as North Weymouth at a location in or near Bicknell Square by the Granite Trust Company, Quincy, Massachusetts, provided the branch is established within six months from the date of this letter.

There had been sent to the members of the Board copies of a draft of letter to Mr. F. H. Stafford, President, The First National Bank of Dryden, Dryden, New York, reading as follows, along with copies of a memorandum dated July 19, 1955, from the Division of Examinations, commenting on the situation and recommending that the letter be approved:

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This refers to the request contained in your letter of July 11, 1955, submitted through the Federal Reserve Bank of New York, for a determination by the Board of Governors as to the status of Dryden Securities Company, Inc., Dryden, New York, as a holding company affiliate.

From the information supplied, the Board understands that Dryden Securities Company, Inc., was organized for the principal purpose of buying conditional sales contracts covering mobile homes; that such Company is a holding company affiliate of The First National Bank of Dryden, Dryden, New York, because it owns 630 shares of the outstanding preferred A stock of the national bank, which is more than 50 per centum of the number of shares voted for the election of directors of such bank at the preceding election; and that such Company does not, directly or indirectly, own or control any stock of, or manage or control, any banking institution other than The First National Bank of Dryden.

In view of these facts the Board has determined that Dryden Securities Company, Inc., is not engaged, directly or indirectly, as a business in holding the stock of or managing or controlling banks, banking associations, savings banks, or trust companies within the meaning of section 2(c) of the Banking Act of 1933, as amended; and, accordingly, Dryden Securities Company, Inc., is not deemed to be a holding company affiliate except for the purposes of section 23A of the Federal Reserve Act and does not need a voting permit from the Board of Governors in order to vote the bank stock which it owns.

If, however, the facts should at any time differ from those set out above to an extent which would indicate that Dryden Securities Company, Inc., might be deemed to be so engaged, this matter should again be submitted to the Board. The Board reserves the right to rescind this determination and make a further determination of this matter at any time on the basis of the then existing facts.

Following a discussion of the matter by Mr. Sloan, during which he stated that action by the Board at this meeting was desired in view of the fact that the stockholders of the national bank were to meet

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tomorrow, the letter was approved unan-
imously, for transmittal through the Fed-
eral Reserve Bank of New York.

Consideration was given to a memorandum from the Division of Examinations dated July 7, 1955, which had been circulated to the members of the Board and which stated that the Division concurred in the recommendation of the Federal Reserve Bank of Richmond that approval be given to the request of Merchants and Farmers Bank, Portsmouth, Virginia, for permission to establish an in-town branch at the intersection of Air Line Turnpike and Gosport Road. When the file was in circulation, Governor Robertson indicated that he would not favor approving the application because on May 7, 1955, the Comptroller of the Currency approved an application of the American National Bank, also of Portsmouth, to establish a branch approximately one-half block from the site of the proposed branch of the Merchants and Farmers Bank. Governor Szymczak also had indicated on the file that he had a question as to whether the application should be approved.

After discussing various factors, including competitive relationships between the commercial banks in Portsmouth and the nature of the area where the proposed branch would be situated, Mr. Sloan said that the Division of Examinations recommended approving the application because the State member bank already had a substantial amount of deposits in the area, because he felt that the State bank was entitled to representation in the area to maintain its competitive position, and because it appeared that

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both branches could operate successfully. He also referred to a letter dated June 16, 1955, in which Mr. Armistead, Vice President of the Federal Reserve Bank of Richmond, expressed the opinion that although one branch probably could serve the banking needs of the section, both institutions could render better service to their customers through their branches because of downtown traffic and parking problems. Mr. Armistead's letter also stated that prospects were favorable for expansion of commercial activity in the locality where the branches would be situated.

There was a general discussion of the application in the light of the policy which should be followed with regard to the authorization of additional banking facilities and in the light of the circumstances mentioned by Mr. Sloan and the Federal Reserve Bank of Richmond. It was the consensus that in this case the arguments advanced were persuasive.

At the conclusion of the discussion, unanimous approval was given to the following letter to the Board of Directors, Merchants and Farmers Bank, Portsmouth, Virginia, for transmittal through the Federal Reserve Bank of Richmond:

Pursuant to your request, submitted through the Federal Reserve Bank of Richmond, the Board of Governors of the Federal Reserve System approves the establishment of a branch at the intersection of Air Line Turnpike and Gosport Road, Portsmouth, Virginia, provided the branch is established within one year of the date of this letter.

Reference then was made to drafts of letters to Mr. Young, President, Federal Reserve Bank of Chicago, and to the United States Attorney

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for the Eastern District of Michigan having to do with a request that Mr. Arthur J. Wiegandt, Assistant Cashier of the Detroit Branch, be given permission to testify before the Grand Jury and in any District Court proceedings that might follow regarding "a scheme to defraud by use of a check kiting system", and that permission also be given for the use of certain records relating to the mailing of checks by the Federal Reserve Bank to the Liberty State Bank of Hamtramck, Michigan.

The draft of letter to the Reserve Bank would take the position that the requested testimony was not clearly of a kind for which the Board's consent was required and that, in any event, the Board would have no objection, while the other draft would state that the matter was being taken up with the Federal Reserve Bank of Chicago. When the file was in circulation, Governor Vardaman expressed doubt that any appearance should be made or record supplied except in response to a subpoena. He raised a question whether the Board would want to make a suggestion to the Reserve Bank along those lines.

In response to a question by Chairman Martin relating to the procedure followed in the past, Mr. Solomon said that he had checked the records, that he had found some cases where testimony was authorized without a subpoena, and that the procedure seemed to depend somewhat on the circumstances. He went on to point out that if the information sought in the matter now before the Board was Federal Reserve Bank information, the

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Board would not be in a position to require the Reserve Bank to follow any particular procedure, although, of course, the Board might suggest in the letter to President Young that the Bank consider requesting the issuance of a subpoena.

Thereupon, unanimous approval was given to letters as follows:

Letter to Mr. Young, President, Federal Reserve Bank of Chicago

The Board is in receipt of a letter dated July 6, 1955, a copy of which is enclosed, from Mr. Fred W. Kaess, United States Attorney, Eastern District of Michigan, requesting that permission be granted for Mr. Arthur J. Wiegandt, Assistant Cashier of the Detroit Branch, to testify before the Grand Jury and in any district court proceedings that may follow regarding "a scheme to defraud by use of a check kiting system", and for the use of certain records of mailing of checks by the Federal Reserve Bank to the Liberty State Bank of Hamtramck, Michigan.

It is not clear that the testimony requested by the United States Attorney in this case is of a kind for which the consent of the Board is required under the Board's regulations on this subject. In any event, however, the Board has no objection to the requested testimony of Mr. Wiegandt as outlined in the letter from the United States Attorney, and it is assumed that you will wish to cooperate with him by making the testimony available. Since it is often desirable as a practical matter that such testimony be preceded by appropriate subpoena, in cooperating with the United States Attorney you may wish to consider suggesting that procedure.

A copy of the Board's letter of this date to Mr. Kaess is enclosed for your information.

Letter to Mr. Fred W. Kaess, United States Attorney, Eastern District of Michigan, Detroit, Michigan (Attention: Mr. Orrin C. Jones, Assistant United States Attorney)

This is in reference to your letter dated July 6, 1955, requesting that permission of the Board be given for the

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testimony of Arthur J. Wiegandt, Assistant Cashier of the Detroit Branch of the Federal Reserve Bank of Chicago, and to use certain records of mailing of checks by the Federal Reserve Bank to the Liberty State Bank of Hamtramck, Michigan, in connection with the possible prosecution of certain persons for use of the mails in a scheme to defraud by use of a check kiting system.

The above matter is being taken up with the Federal Reserve Bank of Chicago, which will doubtless be in touch with you very promptly.

The following drafts of letters, which had been circulated to the members of the Board, were presented for consideration:

Letter for the signature of the Chairman to the Honorable John J. Sparkman,
United States Senate

This is in response to your letter of July 5 on the general subject of availability of mortgage capital to finance residential construction, and in particular on the extent of so-called "warehouse financing" of real estate mortgage loans.

The Board of Governors is entirely in agreement that there should be an adequate flow of mortgage capital for residential construction. Credit and monetary policy has taken account of the importance of maintaining this flow without overcommitment that would adversely affect not only the building industry but the entire economy. It has viewed with some concern, therefore, the overcommitment in mortgages recently and the resulting practice of warehousing mortgages which had been committed for investors in excess of their immediately available funds. Accordingly, the Board has already undertaken to ascertain the dimensions of the problem.

We are planning to make a survey of the extent of various kinds of warehouse financing of real estate loans. It is planned to obtain a special report on this subject from each of the approximately 400 weekly reporting banks located in 94 leading cities. These banks do about two-thirds of the total business of all member banks. A recent pilot survey made by the Federal Reserve Bank of Chicago indicates

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that these banks are likely to account for the great bulk of warehouse financing.

The reports will ask separately for (1) the amount of real estate mortgage loans purchased by the banks from real estate mortgage lending institutions under resale agreement, (2) the amount loaned by the banks to real estate mortgage lending institutions on the security of mortgage loans owned and pledged by the borrowers whether or not also supported by take-out commitments, (3) the amount of similar loans made without security, and (4) the amount of unused portions of firm commitments for warehouse financing. Each category is to be subdivided so as to show transactions with insurance companies, mortgage companies, savings and loan associations, mutual savings banks, and other institutional lenders. Data are to be reported as of a current Wednesday report date and as of a corresponding report date a year ago in order to afford a measure of the growth in warehousing credit.

These categories differ somewhat from those outlined in your letter. They were chosen because they would provide information that would (1) reveal the total volume of warehousing credit currently outstanding, (2) indicate the extent to which additional warehousing credit may be extended on the basis of present commitments, (3) mesh with existing statistical reports from the respondent banks, and (4) be in a form that could be repeated during the coming year if subsequent information on these developments is needed. While we would like this information as of June 30, 1955, it is not feasible to ask for reports of an unusual nature as of a past date. We had planned, consequently, to ask for the information as of a date subsequent to clearance and distribution of the questionnaire.

We would greatly appreciate a prompt response indicating whether the data the Board has been planning to collect would serve the general purposes your Subcommittee has in mind. You will appreciate that whatever information is to be obtained, considerable delay might result if the data are requested from all 14,000 commercial banks rather than from the 400 leading member banks to which we have been planning to send our questionnaire.

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Letter to the Presidents of all Federal Reserve Banks which would be sent, if deemed advisable, after the report form involved had been cleared by the Bureau of the Budget

The recent rise of real estate loans being financed both directly and indirectly by commercial banks is becoming a matter of increasing interest, particularly since the volume of indirect financing through bank loans to mortgage companies, insurance companies, mutual savings banks, savings and loan associations, and similar organizations is not disclosed in current statistics.

The preliminary tabulation made by the Reserve Banks of member bank reports of condition as of April 11, 1955 showed an increase in real estate loans of \$515 million since the year-end and \$1,753 million since the spring call on April 15, 1954. Real estate loans at weekly reporting member banks have increased about \$300 million since the recent spring call date.

It is known that a significant portion of the 1955 increase has resulted from purchases of mortgage loans from one of the large insurance companies under resale agreements. It is assumed that direct purchases of mortgages by banks from insurance companies, mortgage companies, and others under similar types of warehousing arrangements are being reported by the banks as real estate loans in accordance with the Board's telegram of January 12, 1955 to all Reserve Banks.

In the most common type of so-called "warehouse financing," the underlying real estate loans are not sold or assigned to the bank but are merely pledged as collateral against loans made by banks to mortgage companies. These loans would be reported by the banks as commercial and industrial loans, if classified in accordance with the July 2, 1951 letter of the Board's Division of Bank Operations to the Examination and Research Departments at the Reserve Banks. The same thing is true of unsecured loans made to these companies. The volume of such warehouse financing, either on open lines of credit or with pledge of real estate mortgage loans as security, is not known nor is there any accurate indication of increases or decreases therein.

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Even when warehousing loans to mortgage companies are made by one of the sample of weekly reporting banks which classify their increases and decreases in commercial and industrial loans by industry, such loans would appear along with many other types against the item "other types of business." An analysis of the changes in loans to "other types of business" indicates that there may have been some volume of real estate financing included therein in recent months, as the net increase in this category was \$114 million from year-end to June 29, 1955. It is known, however, that at least a portion of this indirect financing in the form of loans to mortgage companies has been incorrectly reported as "other loans" in the weekly reporting member bank series. Information received from various sources indicates that this type of indirect real estate financing may be in the early growth stage.

The call report classification "All other loans," item 9 in Schedule A, which includes direct loans to savings and loan associations and insurance companies, increased \$315 million between April 15, 1954 and April 11, 1955, according to preliminary tabulations. It may be that loans to savings and loan associations and insurance companies increased even more, and that the increase in such loans was offset by decreases in other types of loans also included in the "all other" category.

The Board would like to know the extent to which member banks are engaged in so-called "warehouse financing" of real estate loans, i.e., how much bank credit is now outstanding for the purpose of enabling nonbank institutional lenders and investors and builders to carry real estate mortgage loans on completed properties in their own portfolios or under resale agreements, and what commitments banks have to extend additional warehouse financing. The Board is also interested in ascertaining how the various types of warehouse financing loans are being reported in Schedule A of the call report of condition. Accordingly, it will be appreciated if you will obtain a report, in the form attached, from each weekly reporting member bank in your District as of the second Wednesday following the date of this letter. It is suggested that the reports be obtained in duplicate, that they be reviewed for possible inconsistencies and discrepancies, and that one copy of each report be sent to the

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Board as early as practicable. It will be helpful if the reports are also summarized and analyzed, and if you will submit any comments and suggestions deemed appropriate.

For your information, it is quite possible that, after the reports have been tabulated and the data analyzed, the Board will request that similar information, or a portion thereof, be collected monthly from a smaller group of banks selected from the present weekly reporting series.

Mr. Riefler said that the problem of warehousing of mortgages had been looming larger during recent months, that it appeared desirable to have some facts available regarding the nature and extent of the practice, that he asked Vice President Mitchell, of the Federal Reserve Bank of Chicago, to test the feasibility of obtaining pertinent information, and that the Reserve Bank conducted a pilot survey which demonstrated the feasibility of such a survey but seemed to show that the volume of warehouse financing was not large in the Chicago area. He felt that some confusion might have arisen concerning the amount of mortgages actually warehoused and the amount of commitments for warehouse financing and that, in all the circumstances, it would be advisable to secure data from leading member banks throughout the country.

Mr. Riefler went on to say that at the time the proposed questionnaire was being put into final shape, Senator Sparkman's letter was received, and, while the Senator's letter dealt with the same general problem, it asked for information in somewhat different categories than would be obtained through the questionnaire, Senator Sparkman apparently wanting

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to emphasize the security underlying commitments on the part of mortgage brokers rather than the commitments by commercial banks. In the circumstances, Mr. Riefler said, it was decided to draft a letter to Senator Sparkman inquiring whether the information to be obtained through the questionnaire would be satisfactory for his purposes with the thought that, if the Senator replied in the affirmative, the survey could be made as soon as clearance was obtained from the Budget Bureau.

In the course of a discussion concerning the warehouse financing of mortgage loans, including recent developments with regard to certain types of warehouse financing, Mr. Riefler responded to a question by saying that it would seem well to limit the first survey to the larger banks to obtain general information and then, if necessary, to follow up on that survey by making a more intensive inquiry. He also stated that an effort had been made in developing the survey questionnaire and the letter to the Federal Reserve Banks to avoid any indication that the Board's attitude at this time was unfavorable to the practice.

Governor Vardaman raised for consideration the question whether a representative of the Board should deliver the letter to Senator Sparkman and discuss the matter with him, but it was decided that it would be preferable to send the letter and later make such comments as might be deemed advisable in the light of the Senator's response after he had studied the letter.

Thereupon, the letter to Senator Sparkman and the letter to the Federal

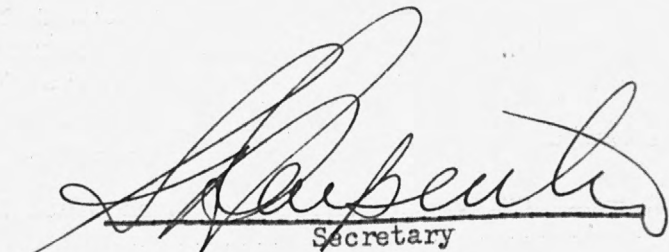
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Reserve Banks were approved unanimously in the form set forth above, with the understanding that the latter would not be sent until after clearance of the report form had been received from the Bureau of the Budget and that technical and clarifying changes might be made in the letter and form before they were transmitted to the Federal Reserve Banks.

Secretary's Note: Certain minor changes of this kind were made in the letter and it was sent to the Federal Reserve Banks on July 29, 1955.

Minutes of actions taken by the Board of Governors of the Federal Reserve System on July 20, 1955, were approved unanimously.

The meeting then adjourned.


Secretary