

Minutes of actions taken by the Board of Governors of the Federal Reserve System on Friday, September 16, 1955. The Board met in the Board Room at 10:00 a.m.

PRESENT: Mr. Balderston, Vice Chairman
Mr. Szymczak
Mr. Vardaman
Mr. Mills
Mr. Robertson
Mr. Shepardson

Mr. Sherman, Assistant Secretary
Mr. Kenyon, Assistant Secretary
Mr. Fauver, Assistant Secretary
Mr. Vest, General Counsel
Mr. Sloan, Director, Division of Examinations
Mr. Sprecher, Assistant Director, Division of Personnel Administration
Mr. Hackley, Assistant General Counsel

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:

Memorandum dated September 1, 1955, from Mr. Young, Director, Division of Research and Statistics, recommending the appointment of Catherine S. Corry as Clerk in that Division with basic salary at the rate of \$3,260 per annum, effective as of the date on which she enters upon the performance of her duties.

Approved unanimously.

Memorandum dated September 1, 1955, from Mr. Bethea, Director, Division of Administrative Services, recommending an increase in the basic salary of Joseph J. Yilek from \$3,685 to \$3,840 per annum, effective September 25, 1955, incident to his transfer from the position of Supply Clerk to the position of Clerk in that Division.

Approved unanimously.

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Memorandum dated September 2, 1955, from Mr. Bethea, Director, Division of Administrative Services, recommending that Bishop Hart, Messenger in the Board Members' Offices, be transferred to the Division of Administrative Services as Supply Clerk, with an increase in his basic salary from \$3,385 to \$3,515 per annum, effective September 25, 1955.

Approved unanimously.

Letter to the Board of Directors, Union Trust Company of Ellsworth, Ellsworth, Maine, reading as follows:

The Board of Governors approves the establishment of a branch by the Union Trust Company of Ellsworth, Ellsworth, Maine, in the Town of Milbridge, Washington County, Maine, provided the branch is established within one year from the date of this letter.

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

There were presented telegrams to the Federal Reserve Banks listed below approving the establishment without change, on the dates indicated, of the rates of discount and purchase in their existing schedules:

St. Louis	September 12
New York	September 15
Philadelphia	September 15

Approved unanimously.

Pursuant to arrangements made in accordance with the Board's request at the meeting on September 9, 1955, a meeting attended by members of the Board's staff and representatives of the Boston, New York, Philadelphia, and Richmond Reserve Banks was held yesterday for the purpose of discussing business development corporations and particularly member bank participation in such corporations. The views expressed by the Reserve

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Bank representatives were summarized in a memorandum prepared by Mr. Fauver under date of September 16, copies of which were sent to the members of the Board prior to this meeting. In general, it was the opinion of the Reserve Banks that the organization of business development corporations should be encouraged, it being felt that they were desirable from an economic and social point of view and also because they utilize existing banking facilities and avoid resorting to direct use of State or Federal funds for industrial financing. It was thought that as long as the corporations functioned on the presently contemplated basis and the present limitations with respect to individual bank participation were continued, there was little cause for concern from the bank supervisory standpoint, especially if a member bank belonged to only one such corporation. Consideration also was given by the Federal Reserve Bank representatives to the draft of letter to Senator Scott, of North Carolina, which was tentatively agreed upon by the Board at the meeting on September 14, and the view was expressed that such a letter might have the inadvertent effect of discouraging bank participation in business development corporations, including those now existing and those which might be organized in the future. Some rewording of the draft therefore was considered desirable.

Governor Vardaman said he was in agreement with the view of the Reserve Bank representatives that in principle the development corporations were desirable, his reservations being based on the delegation of

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lending authority embraced in the requirement that banks becoming members of such corporations may not withdraw for a stated period and during that period are obligated to make loans to the corporations on call up to a specified percentage of their capital and surplus. He thought that the latest draft of letter to Senator Scott was well stated and that it should be sent with no more than minor modifications.

Governor Robertson stated that he agreed substantially with the views expressed by Governor Vardaman. He did not believe that the letter would have the effect contemplated by the Reserve Bank representatives, and he felt that the Board was under obligation to point out what it considered to be a defect in the scheme of bank participation and to express the hope that this defect would be corrected in the future. Governor Robertson then suggested certain minor amendments to the letter, particularly to emphasize the Board's understanding that an individual bank would be a member of only one business development corporation, and there was agreement with these suggestions.

Governor Shepardson said that although he recognized the principle involved in the point to which members of the Board objected, that is, the obligation of banks becoming members of a development corporation to make loans to the corporation at the call of its directors, he felt that there had been some tendency to magnify the dangers which might be involved in such a plan. After discussing the provisions made for bank participation in the administration of existing business development corporations and the

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proposed North Carolina corporation, he said that the very strength of this kind of organization rests in a commitment that members of the organization will extend financial assistance over a stated period and can not withdraw at their pleasure. For these reasons, he felt that the language of the draft of letter to Senator Scott should be modified by softening the portion thereof which referred to this "potentially unsound" feature.

Governor Mills stated that he was inclined to share the view expressed by Governor Shepardson. He then pointed out that according to statements made at the staff meeting yesterday, the development corporations seem to be rather enthusiastically supported by the Reserve Banks in whose districts such corporations are now in existence. He suggested that for the Board to express a measure of dissent might create the appearance of a difference of opinion within the Federal Reserve System. It was his thought that the letter to Senator Scott might be phrased in somewhat milder terms and express the Board's reservations in terms of questions rather than opinion, and that it would be sufficient if the letter were to indicate that the Board intended to continue to study the matter. A milder communication, he thought, would have the effect desired by the Board and would give support to commercial banks endeavoring to have the development corporations organized and operated in a manner consistent with sound banking practices.

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Language was suggested which would represent a compromise of the views expressed by members of the Board and after various modifications were made Governors Vardaman and Robertson indicated that they would agree to the revised wording, although somewhat reluctantly, if it reflected the views of the majority of the Board. Governor Shepardson stated that he also would agree with the revised language, although he remained of the opinion that in a cooperative type of organization the obligation of members to support it financially over a period of time is a feature essential to its success.

It was reported that the Chairman of the Presidents' Conference had placed the subject of business development corporations on the agenda for discussion at the next meeting of the Conference so that the views of the Presidents might be stated at the joint meeting of the Presidents and the Board of Governors.

Thereupon, unanimous approval was given to a letter for the signature of Vice Chairman Balderston to the Honorable W. Kerr Scott, United States Senate, Washington, D. C., in the following form, with the understanding that copies would be sent to the Presidents of all Federal Reserve Banks:

This refers to your letter of June 24, 1955, with its enclosures, regarding the question whether member banks of the Federal Reserve System may purchase stock in the Business Development Corporation of North Carolina, which it is understood is being organized pursuant to a special statute of the State of North Carolina approved May 20, 1955, and also whether a member bank of the Federal Reserve System could become a "member" of such Corporation.

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Under section 5136 of the U. S. Revised Statutes and section 9 of the Federal Reserve Act, national banks and State banks which are members of the Federal Reserve System are prohibited from purchasing corporate stocks with certain limited exceptions not here applicable. Consequently, such banks could not legally purchase stock in the proposed Corporation. There is no provision of Federal law, however, which would forbid a State bank which is a member of the Federal Reserve System from becoming a "member" of the proposed Corporation.

The Board is in complete sympathy with the objective of the Business Development Corporation of North Carolina and corporations of this kind which have been organized in other States. As you may know, however, the North Carolina statute makes it obligatory upon banks which are members of the Corporation to make loans up to specified amounts to the Corporation as and when called upon to do so, on terms and conditions approved by the directors of the Corporation; and a member institution may not withdraw from membership in the Corporation except after advance notice of five years. The Board questions the wisdom and propriety of a commercial bank, operating as it does largely with depositors' funds, entering into a long-term commitment of this kind to make loans, even in a small amount, irrespective of what may be the nature of the loan or the condition of the borrower at the time the loan will be made. It is hoped that, as similar corporations are created in other States in the future, this feature can be corrected without impairing the effectiveness of bank participation in such programs.

On the basis of the Board's understanding as to the proposed method of operation of the North Carolina Corporation and on the assumption that a member bank would not become a member of more than one such corporation, the Board is not disposed to express disapproval of bank participation in this plan or in any similar plan which may heretofore have been adopted in other States. It does propose, however, to continue its study of this matter.

In accordance with your request, the enclosures with your letter are returned herewith, together with the copy of the North Carolina statute furnished by Mr. Cochrane of your office.

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Mr. Sloan then withdrew from the meeting and Mr. Leonard, Director, Division of Bank Operations, entered the room.

The following draft of letter to Mr. J. H. Wurts, Chairman, Joint Committee on Check Collection System, c/o Federal Reserve Bank of New York, had been circulated to the members of the Board prior to this meeting and was presented for consideration:

This refers to your letter of August 2 to Governor Mills suggesting the desirability of an expression of the Board's views as to certain specific questions of policy arising from the June 1954 Report of the Joint Committee on Check Collection System.

Before commenting on the questions raised in your letter, the Board wishes to express its appreciation of the excellent work of the Committee in studying the complex question and in preparing such a comprehensive report.

The Presidents' Conference, at its meeting in December 1954, accepted the report of the Joint Committee - with reservations as to the direct return of unpaid items - but took no action to effectuate the recommendations, realizing that it would be premature to consider doing so until the other sponsoring agencies had taken action.

Since then there have been further discussions with representatives of the American Bankers Association and of the Association of Reserve City Bankers, and it is understood that the Associations are expected to give further consideration to the report this fall. In the circumstances, you have suggested that it would be desirable to have an expression of the Board's views regarding the five questions listed in your letter, pointing out that it might be embarrassing if the Associations should act favorably on the report and the Board should later register any objections to portions of the report which you and Mr. Deming have been urging the sponsoring Associations to accept.

The Board believes that there is no occasion for such embarrassment, and its position with respect to each of the questions raised is indicated in the following comments:

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A. Question

"Whether a Federal Reserve Bank should consent to receive from a country member bank (1) items drawn on the Federal Reserve Bank and Government checks and postal money orders, and (2) certain intradistrict deferred credit items payable at par, for credit to a correspondent member bank if the sending member bank and the correspondent member bank so desire. (There is already a precedent for this procedure, in that the Federal Reserve Bank of Minneapolis for some years has followed it on a general basis and other Federal Reserve Banks have made similar arrangements on specific request.)"

Comment

The Board of Governors would welcome the further development of such a practice as a step in the elimination of duplication in check handling and in the expedition of the check collection process.

B. Question

"Whether a Federal Reserve Bank should consent to receive directly from a nonmember bank, when so requested by a member bank and the nonmember bank, (1) items drawn on the Federal Reserve Bank and Government checks and postal money orders, and (2) certain intradistrict deferred credit items payable at par, for credit to the member bank. (The view of the Joint Committee in favoring such a change in policy is stated in section C.3 of Chapter I (at pp. 11-12) of the Joint Committee's report dated June 15, 1954.)"

Comment

For the same reasons, the Board would interpose no objection to the extension of the practice to the acceptance of items directly from nonmember banks for credit to a member bank.

C. Question

"Whether the Federal Reserve System should consider providing facilities for consolidated direct air shipments to important financial centers where there is no Federal Reserve Bank or branch, for the purpose

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of expediting presentation of items drawn on banks in such centers when volume and other circumstances warrant. (This point required no present decision as to whether the facilities should be provided, since the recommendation is merely that the System consider the matter.)"

Comment

The Board will be glad to consider any such plans worked out by the Reserve Banks.

D. Question

"Whether the Federal Reserve System should take the position that the rules regarding the absorption of exchange charges by collecting banks be uniform as between member banks and nonmember insured banks, and that all insured banks, member and nonmember, should be prohibited from absorbing exchange charges, except where absorption is merely incidental and not related to the solicitation of deposit balances. (In effect, the System took such a position at hearings on the Brown-Maybank bill. In the light of recent developments, however, it seems doubtful whether the recommendation of the Joint Committee on this topic will have any effect.)"

Comment

The Board agrees that nonmember insured banks and member banks should be governed by uniform rules regarding absorption of exchange charges. However, as you know, the Federal Deposit Insurance Corporation has indicated that it is unwilling to consider changing its position with respect to this matter; and, consequently, there would seem to be little likelihood of attaining uniformity in the absence of legislation.

E. Question

"Whether the Federal Reserve System favors the establishment of regional clearing arrangements, where circumstances warrant, for the collection of checks drawn on banks in an area which are received on deposit by other banks in the area. (The

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recommendation makes no reference to participation by the Federal Reserve Banks in the development or operation of such arrangements. Accordingly, the issue of financial support of regional clearing arrangements is not involved.)"

Comment

The Board would favor the establishment of regional clearing arrangements where circumstances warrant and the establishment would result in improved check collection service. As you point out, the Joint Committee's recommendation does not involve the question of financial support of such arrangement by the Federal Reserve Banks. This is a subject that the Board believes should have very careful study and consideration.

The Board trusts that this reply affords the desired assurances.

The letter was approved
unanimously.

In connection with the foregoing matter, Governor Mills requested that Mr. Leonard comment on two subjects: first, the question whether a Federal Reserve Bank should consent to receive items directly from a non-member bank for credit to a member bank, and, second, whether a Federal Reserve Bank would be warranted in contributing to the expense of a regional clearing arrangement where such an arrangement would be to the advantage of the Reserve Bank but in which arrangement the Reserve Bank would not actually participate. He said that there had been much discussion of these questions within the System, that there were differences of opinion, and that at some point the Board might be called upon to give further consideration to them.

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Mr. Leonard said that there was a marked difference of opinion among Federal Reserve Bank representatives as to the propriety and desirability of paying part of the cost of clearing offices in which Reserve Banks do not participate directly. Referring to the Nassau County Clearing House Association arrangement, he said it was the view of a number of persons within the System that where such a scheme is determined to be to the advantage of a Federal Reserve Bank and where a saving to the Reserve Bank can be achieved, the Bank would be derelict if it did not take advantage of the opportunity. He went on to say that the Nassau County organization was handling a substantial number of items that would otherwise come to the Federal Reserve Bank of New York, that the contributions of the New York Bank were less than the cost if the Bank handled the items itself, and that the items were handled more expeditiously. He reported, however, that another group felt strongly that a policy of paying member banks or organizations of member banks to do work that might otherwise come to a Reserve Bank involved a principle which, if established, could be extended in numerous directions and to an almost unlimited extent. Some persons, he said, questioned whether there was proper authority for making such expenditures. He pointed out that if any specific proposal of this kind should be made, it would come before the Board for consideration and approval. He also noted that the recommendation of the Joint Committee on Check Collection System referred not to an arrangement of this kind but to the question of establishing regional clearing arrangements

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without reference to participation by Federal Reserve Banks in their development or operation.

Mr. Leonard said that the acceptance of checks from nonmember banks for collection and credit to the account of member banks also was a controversial matter. Personally, he sided with those who felt that such arrangements would not affect to any substantial extent the matter of membership in the Federal Reserve System. Country banks, he said, send city checks to their city correspondents and by-pass the Reserve Banks completely, and as pointed out by the Joint Committee on Check Collection System, the Reserve Banks in such cases could not handle the items as well, for a substantial number of the checks are on the city correspondent itself. With regard to country checks, however, the situation would be reversed. The majority of such checks are rerouted by the city correspondent to the Federal Reserve Bank and they tend to come to the Reserve Bank in the afternoon, thus creating a more expensive check handling operation and the necessity for an earlier closing hour. If the country checks arrived in the morning, the Reserve Bank could handle them more efficiently and an unnecessary handling by the city correspondent would be eliminated.

Minutes of actions taken by the Board of Governors of the Federal Reserve System on September 15, 1955, were approved unanimously.

All of the members of the staff except Mr. Sprecher then withdrew from the meeting.

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Following the meeting, the Secretary's Office was informed that consideration was given to a recommendation from the Division of Personnel Administration that the Board take no action to prevent the incorporation into the Board plan of the Federal Reserve Retirement System of the provisions of Public Law 369, 84th Congress, amending the Civil Service Retirement Act to provide increased retirement allowances for members currently on retirement or retiring before January 1, 1958; and that unanimous approval was given to the following letter to Mrs. Valerie R. Frank, Secretary, Retirement System of the Federal Reserve Banks, c/o Federal Reserve Bank of New York:

The Board of Governors interposes no objection to incorporating into the Board Plan of the Retirement System of the Federal Reserve Banks the increased benefits provided members of the Civil Service Retirement System by Public Law 369, 84th Congress.

As it is desired to fund these payments in a lump sum, please bill the Board for the total cost of funding this additional benefit for those already retired. The Board understands that the cost of funding the increases due those retiring or becoming eligible for survivorship allowances prior to January 1, 1958, will be included in the Actuary's annual valuation of the Board Plan.

The Secretary's Office also was advised that the Board gave consideration to the request of the Federal Reserve Bank of Richmond for approval of a payment to the Federal Reserve Retirement System in order to fund additional annuities payable to the survivors of Maurice P. Flagg, and that unanimous approval was given to a letter to Mr. Leach, President of the Federal Reserve Bank of Richmond, reading as follows:

For the reasons outlined in your letter of September 9, 1955, the Board of Governors approves the payment of

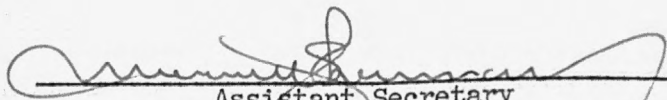
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\$2,090.82 to the Retirement System of the Federal Reserve Banks for the purpose of funding additional annuities payable to the survivors of Maurice P. Flagg, deceased active member of the Federal Reserve Bank of Richmond.

The Board understands that this payment does not constitute a new special benefit but merely a payment in accordance with the agreement set forth in the Board's letter of June 9, 1953.

The meeting then adjourned.


Assistant Secretary