Minutes of actions taken by the Board of Governors of the Federal Reserve System on Monday, October 17, 1955. The Board met in the Board Room at 10:00 a.m.

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

Mr. Carpenter, Secretary
Mr. Kenyon, Assistant Secretary
Mr. Solomon, Assistant General Counsel
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:

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

> In accordance with the request contained in your letter of October 10, 1955, the Board approves the appointments of George William Metz and Gurdon G. Potter as examiners for the Federal Reserve Bank of Philadelphia, effective October 3, 1955.

Approved unanimously.

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

> In accordance with the request contained in your letter of October 5, 1955, the Board approves the appointment of Thomas I. Fetzer as an assistant examiner for the Federal Reserve Bank of Dallas. Please advise as to the date upon which the appointment is made effective.
>
> It is noted that Mr. Fetzer is indebted to the Security State Bank, Houston, Texas, a nonmember State

bank, in the amount of $150.00, and that you will not permit him to participate in any examination of the bank as long as this indebtedness exists.

Approved unanimously.

Letter to Mr. MacDonald, Chief Examiner, Federal Reserve Bank of Boston, reading as follows:

Reference is made to your letter of September 28, 1955, regarding the request of the Hadley Falls Trust Company, Holyoke, Massachusetts, for an extension to January 17, 1956, of the time within which to establish a branch at or in the vicinity of the junction of High Street and Maple Avenue, Holyoke, Massachusetts.

On the basis of the information submitted, the Board of Governors concurs in your recommendation and extends to January 17, 1956, the time within which Hadley Falls Trust Company, Holyoke, Massachusetts, may establish the branch at the aforementioned location in Holyoke, Massachusetts, as originally approved in the Board's letter of April 20, 1955. Please advise the bank accordingly.

Approved unanimously.

Letter to Mr. Denmark, Vice President, Federal Reserve Bank of Atlanta, reading as follows:

In accordance with the recommendation contained in your letter of October 3, 1955, the Board of Governors extends to January 23, 1956, the time within which the Guaranty Bank & Trust Company, Hammond, Louisiana, may accomplish membership. Please advise the applicant to this effect.

Approved unanimously.

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

This refers to your letter of October 4, regarding the penalties incurred by the Merchants National Bank of Allentown, Allentown, Pennsylvania, on deficiencies in its required reserves for the two semimonthly periods in August 1955.

It is noted that the deficiencies resulted from the erroneous omission of deferred credits due the Federal Reserve Bank for cash items sent for remittance in their semimonthly deposit report for determining reserve requirements, a condition that had existed since June 20, 1955, but now corrected; that your Bank had waived the penalty for the second half of August under Paragraph E of the Board's rulings because of the excellent record of the member bank, but this waiver became invalid because of receipt of corrected figures for the period ended August 15, which changed that period from a reserve excess to a deficiency; and that in both cases the deficiencies were less than 5 per cent of requirements.

In the circumstances, the Board ratifies the waiving of the $133.15 penalty for the last half of August and assumes that your Bank will waive the $96.32 penalty for the first half of August under Paragraph E of the Board's rules.

Approved unanimously.

Letter to Bank of America, New York, New York, reading as follows:

The Board of Governors of the Federal Reserve System authorizes Bank of America, New York, New York, pursuant to the provisions of Section 25(a) of the Federal Reserve Act and the Board's Regulation K, to establish a branch in Beirut, Lebanon, and to operate and maintain such branch subject to the provisions of such section and regulation; upon condition that unless the branch is actually established and opened for business on or before October 1, 1956, all rights hereby granted shall be deemed to have been abandoned, and the authority hereby granted shall automatically terminate on such date.

Please advise the Board of Governors in writing, through the Federal Reserve Bank of New York, when the branch is opened for business, together with information as to its location in Beirut. It is understood, of course, that no change will be made in the location of such branch without the prior approval of the Board of Governors.

Approved unanimously, for transmittal through the Federal Reserve Bank of New York, with copies to the Federal Reserve Bank of San Francisco and the Comptroller of the Currency.

At this point Mr. Sherman, Assistant Secretary, entered the room.

Reference was made to a letter dated September 2, 1955, from Mr. Hill, Vice President of the Federal Reserve Bank of Philadelphia, transmitting two related questions under Regulation U, Loans by Banks for the Purpose of Purchasing or Carrying Stocks Registered on a National Securities Exchange, which had been submitted by an officer of a member bank with a request for a ruling by the Board regarding the applicability of the regulation. It appeared that a customer of the bank had sold short a registered stock and now proposed to cover the short position by the acquisition and conversion of debentures which were convertible into the registered stock. The debentures would be acquired pursuant to "rights" issued to stockholders and would be convertible into stock for a period of about 10 years. The questions raised were whether a loan to acquire the debentures should be considered to be for the purpose of purchasing or carrying a registered stock and, if so, whether the loan could qualify for the preferential treatment provided by section 3(p) in Regulation U for loans to purchase stocks by exercising stockholders' "rights".

Prior to this meeting, there had been circulated to the members of the Board a draft of reply to Vice President Hill which would take the position that the loan should be considered to be for the purpose of purchasing or carrying a registered stock in view of the fact that the acquisition of the debentures would be merely a step toward the acquisition of the registered stock. The draft would also state that since

the transaction would be contrary to the letter and spirit of section 3(p), the loan could not qualify for the preferential treatment provided by that section.

In commenting on the matter, Mr. Solomon stated that under the current provisions of Regulation U it appeared proper to take the position indicated in the draft of reply. He also said that the questions raised had been discussed with members of the staffs of the New York and Philadelphia Reserve Banks, who agreed with the views stated. He went on to say that several similar questions had come up in the past and that the Board had taken the position that it should look at the end purpose of the transaction and consider the loan as one for the purchase of a registered stock. With regard to the second question, namely, whether the loan could qualify for preferential treatment under section 3(p) of Regulation U, Mr. Solomon said that this provision was included in the regulation for a rather specific and different purpose, one which did not contemplate "trading" of securities.

During a discussion which ensued, reference was made to the Board's letter of September 30, 1955, to the Presidents of the Federal Reserve Banks requesting their comments on a possible amendment to Regulation U which would bring convertible bonds and debentures under the coverage of that regulation. It was stated that replies had now been received from two of the Reserve Banks and that different views were expressed, one Bank being inclined to feel that the matter was not of

sufficient importance to warrant amending the regulation, while the other Bank was inclined toward the opinion that a change in the regulation would be appropriate.

In response to a question, Mr. Solomon discussed the apparent reasons for excluding convertible bonds and debentures from the coverage of Regulation U when it was first adopted, indicating that when the regulation was first issued the Board had in mind that it was of an experimental nature, that banks should be relieved as much as possible from the operational problems created by such a regulation, and that amendment of the regulation could be considered at a later date if more detailed provisions seemed necessary.

Chairman Martin said that in view of the circumstances he would not object to sending the letter, provided a change was made so as to state simply that the transaction would be contrary to section 3(p) rather than contrary to the letter and spirit of that section.

In a further discussion, the view was expressed that under the current provisions of Regulation U, there could well be doubt in the minds of banks and their customers concerning the applicability of the regulation to specific transactions of the general nature referred to by the Philadelphia Reserve Bank, and that quite possibly the regulation was being interpreted in a manner different from that proposed in the draft of reply. It was felt that for this reason some clarification by way of interpretation or amendment of Regulation U might be desirable. In the

circumstances, question was raised whether the reply should be sent until the Board had had an opportunity to decide whether convertible bonds and debentures as such should be covered by Regulation U. It was agreed, however, that the reply should not be delayed until that decision could be made.

At the conclusion of the discussion, unanimous approval was given to a letter to Vice President Hill reading as follows:

This is with further reference to your letter of September 2, 1955 presenting two related questions under Regulation U. The facts involved are substantially as follows: A bank customer has sold short a registered stock (i.e., one registered on a national securities exchange), and now proposes to cover the short position by the acquisition and conversion of debentures which are convertible into the registered stock. The debentures would be acquired pursuant to "rights" issued to stockholders and expiring within ninety days. The debentures are convertible into the stock for a period of about ten years, beginning sixty days after the date by which the rights must be exercised.

You ask whether a loan to acquire the debentures should be considered to be for the purpose of purchasing or carrying a registered stock and, if so, whether the loan can qualify for the preferential treatment which section 3(p) of Regulation U provides in certain circumstances for loans to purchase stocks by exercising stockholders' "rights".

In view of the fact that the acquisition of the debenture would be merely a step toward the acquisition of the registered stock into which it is convertible, the loan should be considered to be for the purpose of purchasing or carrying a registered stock. However, since the transaction would be contrary to section 3(p), the loan cannot qualify for the preferential treatment provided by the section.

As indicated in the Board's letter of September 30, 1955, consideration is being given to certain other aspects of convertible bonds in connection with Regulation U.

During the foregoing discussion Mr. Thomas, Economic Adviser to the Board, entered the room.

Consideration was given to an inquiry from Mr. Richard H. Stebbins, of Richard Stebbins and Associates, Inc., Minneapolis, Minnesota, regarding a promotional program under which client banks would give to new savings depositors opening an account of $10 or more a free billfold containing a dime savings bank. The question raised was whether this program would involve an overpayment of interest on savings deposits under Regulation Q, Payment of Interest on Deposits. A draft of reply had been circulated to the members of the Board which would refer to the Board's general policy of not attempting to make detailed interpretations or rulings with respect to whether particular practices constituted an indirect payment of interest on deposits within the meaning of Regulation Q except after consideration of all the circumstances of a specific case as developed by examination of the member bank involved.

Governor Balderston offered a substitute draft, stating that full information with respect to the promotional program seemed to have been transmitted to the Board and he questioned whether the reply should refer to the examination procedure. While the draft which he submitted took the same general position as the draft submitted by the staff, the language had been changed for this reason so as to eliminate the reference to examination of the bank or banks concerned.

Following a discussion during which agreement was expressed with the draft proposed by Governor Balderston, unanimous approval was

given to a letter to Mr. Stebbins reading as follows, with a copy to the Federal Reserve Bank of Minneapolis:

This refers to your letter of October 4, 1955, regarding the question whether a promotional program used by your client banks would involve an overpayment of interest on savings deposits under this Board's Regulation Q.

It is understood that under this program a client bank would give to each new savings depositor opening an account of $10 or more a free billfold containing a dime savings bank with a maximum capacity of $3.60. You state that the combined value of the wallet and savings bank is $2.65; that the wallet is given in appreciation for new business and the coin bank to encourage the customer to develop a regular savings habit; and that the new customer pledges to have at least $36.50 in his account at the end of the first 12-month period.

Although the Board appreciates the desire of your Company to have a concrete and definite answer as to whether this promotional idea, if followed by member banks, would involve an indirect payment of interest on savings deposits, it hopes that you will understand the reasons why it cannot give you such an answer. For many years, its general policy has been not to attempt to rule in advance as to whether a particular practice constitutes an indirect payment of interest on deposits within the meaning of Regulation Q. The Board has preferred to rely primarily upon the cooperation and good faith of member banks in adapting their practices to conform to the spirit and purpose of the statute provisions on this subject. The Board does not feel that it would be justified in departing from its general policy, and, therefore, regrets that it cannot give you the definite answer that you seek.

The following draft of letter to Mr. Earhart, President of the Federal Reserve Bank of San Francisco, which had been circulated to the members of the Board, was presented for consideration:

Reference is made to your letter of October 7, 1955, enclosing copies of a letter and a resolution indicating the

intention of the Bank of Las Vegas, Las Vegas, Nevada, to withdraw from membership in the Federal Reserve System. We have also received a letter addressed to the Board of Governors concerning this matter and enclosing a signed copy of the letter which you forwarded addressed to the Federal Reserve Bank of San Francisco.

It is noted that the bank has indicated its desire to obtain a waiver of the six months' notice of withdrawal as provided by section 10 of Regulation H. The letter requests an informal opinion as to whether or not the Board of Governors would waive such notice.

The Board of Governors has given consideration to this matter and, in view of the expressed desire of the bank, it hereby waives the requirement of six months' notice of withdrawal with the understanding that the bank is willing to consider its letter as a formal request for such waiver.

Accordingly, upon surrender of the Federal Reserve Bank stock issued to the bank, you are authorized to cancel such stock and make appropriate refund thereon. Under the provisions of section 10(c) of Regulation H, as amended effective September 1, 1952, the bank may accomplish termination of its membership at any time within eight months after notice of intention to withdraw is given. Please advise when cancellation is effected and refund is made.

The certificate of membership should be returned to the Board and the State banking authorities advised of the bank's proposed withdrawal from membership, together with the date such withdrawal becomes effective.

It is noted you have advised the bank that arrangements must be made direct with the Federal Deposit Insurance Corporation for continuation of deposit coverage when the withdrawal becomes effective.

Following comments by Governor Robertson, the letter was approved unanimously.

Minutes of actions taken by the Board of Governors of the Federal Reserve System on October 14, 1955, were approved unanimously.

The meeting then adjourned.

Secretary