Minutes for March 20, 1956.

To: Members of the Board

From: Office of the Secretary

Attached is a copy of the minutes of the Board of Governors of the Federal Reserve System on the above date.

It is not proposed to include a statement with respect to any of the entries in this set of minutes in the record of policy actions required to be maintained pursuant to section 10 of the Federal Reserve Act.

Should you have any question with regard to the minutes, it will be appreciated if you will advise the Secretary's Office. Otherwise, if you were present at the meeting, please initial in column A below to indicate that you approve the minutes. If you were not present, please initial in column B below to indicate that you have seen the minutes.

	A	B
Chm. Martin	x	W
Gov. Szymczak	x	
Gov. Vardaman	x	
Gov. Mills	x	
Gov. Robertson	x R	
Gov. Balderston	x CCB	
Gov. Shepardson	x	

Minutes of actions taken by the Board of Governors of the Federal Reserve System on Tuesday, March 20, 1956. The Board met in the Board Room at 10:00 a.m.

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

Mr. Kenyon, Assistant Secretary
Mr. Fauver, Assistant Secretary
Mr. Riefler, Assistant to the Chairman
Mr. Thomas, Economic Adviser to the Board
Mr. Leonard, Director, Division of Bank Operations
Mr. Vest, General Counsel
Mr. Young, Director, Division of Research and Statistics
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 stated:

Memorandum dated March 14, 1956, from Mr. Johnson, Personnel Security Officer, recommending that interim security clearance be granted in the case of James W. Allison, Special Consultant to the Board, pending completion of the full-field investigation previously authorized; and that the position of Secretary to Mr. Thurston be declared sensitive and a full-field investigation instituted for the employee currently assigned to that position (Ruth E. Morris) to clear her for access to classified security information.

Approved unanimously.

Letter to Mr. Leach, President, Federal Reserve Bank of Richmond, reading as follows:

In response to your letter of March 9, 1956, the Board authorizes the expenditure of approximately $101,000 for

improvements to the lighting and air conditioning system on the first floor of the original head office building.

As more fully explained in your letter, this represents an increase of $16,000 over the earlier estimate for the cost of this work which was authorized in the Board's letter of August 24, 1955.

The Board also approves an allowance of an additional $9,000 to provide for unforeseen contingencies which might arise in connection with the program.

Approved unanimously.

Letter to the Presidents of all Federal Reserve Banks reading as follows:

The indicated number of copies of the following forms are being forwarded to your Bank under separate cover for use of State member banks and their affiliates in submitting reports as of the next call date. A copy of each of these forms is attached:

Number of copies	
	Form F.R. 105 (Call No. 139), Report of condition of State member banks.
	Form F.R. 105e (Revised November 1955), Publisher's copy of report of condition of State member banks.
	Form F.R. 105e-1 (Revised November 1955), Publisher's copy of report of condition of State member banks.
	Form F.R. 105e-2 (Revised November 1955), Publisher's copy supplement.
	Form F.R. 220 (Revised March 1952), Report of affiliate or holding company affiliate.

Form F.R. 220a (Revised March 1952), Publisher's copy of report of affiliate or holding company affiliate.

All of the forms are the same as those used on December 31, 1955.

Approved unanimously, with the understanding that the letter would be sent at an appropriate later date.

At the meeting on February 20, 1956, consideration was given to an inquiry from the Federal Reserve Bank of Boston regarding the eligibility of municipal tax anticipation obligations as collateral for advances by Federal Reserve Banks to member banks under section 13 of the Federal Reserve Act. The staff recommended a response which would affirm the position of the Board, first adopted in 1916, that such obligations are not eligible for use as collateral for section 13 advances. However, in view of questions raised by Governor Vardaman, the staff was requested to explore the matter in more detail. Such a study was made, and in a memorandum dated March 13, 1956, which had been circulated to the members of the Board prior to this meeting, Mr. Hackley stated it to be the consensus of the staff that for a number of reasons, including the following, obligations of the kind in question should not be declared eligible:

1. There was no evident need for making such obligations eligible, since member banks have adequate holdings of Government obligations and paper already eligible for discount or for use as collateral for advances.

2. In any particular case in which a member bank is in difficulty and does not have adequate holdings of eligible paper, it can use tax anticipation obligations of municipalities as collateral for advances under section 10(b) of the Federal Reserve Act.

3. Although in some instances tax anticipation obligations of municipalities may represent highly liquid short-term assets soundly based and readily marketable, in many cases such obligations are issued by municipalities faced with financial difficulties and are acquired by local banks largely as a matter of public service. Consequently, in order to prevent abuses, it would not seem advisable to grant any blanket authority for the eligibility of such obligations. On the contrary, it would seem necessary for the Board to prescribe certain rather rigid and detailed requirements and credit standards somewhat comparable to those now prescribed in Regulation E, Purchase of Warrants. It was believed that relatively few municipal tax anticipation obligations could meet these requirements and there was not evidence of sufficient need for the use of such obligations as collateral to justify the preparation and issuance of regulations of that kind.

The memorandum also referred to Congressional discussions in the 1930's which, while not conclusive, would tend to support the view that the obligations in question are not eligible under the law as collateral for section 13 advances. It was recommended, in all the circumstances, that the letter previously drafted for the Board's consideration be sent to the Boston Reserve Bank and that copies be sent to the other Federal Reserve Banks to avoid any misinterpretation of Regulation A and make the Board's position clear.

Following comments by Mr. Hackley concerning the views of the staff, Governor Vardaman expressed himself as being in disagreement with

those views, his objections being due principally to developments in municipal financing which he felt warranted recognition in the administration of the discount function. With regard to the broader question of eligibility requirements in general, it was his thought that a study of the prevailing requirements should be made which would include obtaining the comments of parties outside the Federal Reserve System. If the results of such a study warranted, he felt that the System should seek changes in the law so that the Board's regulations could be revised in a manner which would leave mostly to the discretion of the Federal Reserve Banks the acceptance of various types of paper as collateral for discounts and advances.

In a further discussion of the matter, Mr. Thomas said that the matter did not appear to be of great significance at the present time and that he concurred in the staff's views regarding the question now before the Board, particularly for the reason that if municipal tax anticipation obligations were made eligible as collateral for section 13 advances, this might lead to numerous requests that other types of paper also be made eligible. He felt, however, that there was something to be said for giving appropriate consideration to the fundamental issues involved.

Messrs. Vest and Hackley brought out that the Boston Reserve Bank's question was a technical one of rather narrow scope in view of

the present status of the law. If the Board should decide that the matter deserved further study, they felt that such a study must be in the direction of helping the Board to decide whether changes in the law should be sought.

Following a statement by Governor Balderston that it seemed advisable to review all situations where the law and the Board's regulations might have become outmoded over a period of years, various suggestions were made as to how a further study of the subject might proceed but no decision was reached. The comment was made in this connection that lack of uniformity in discount administration throughout the System caused eligibility requirements to assume greater significance than they would otherwise. Only recently, it was pointed out, had steps been initiated, such as periodic meetings of the Reserve Bank discount officers, which might be expected to result in a higher degree of uniformity.

Chairman Martin then suggested that the proposed letter be sent to the Boston Reserve Bank in answer to the specific question which was raised. He also suggested that copies not be sent to the other Federal Reserve Banks at this time and that further thought be given to the broader problem discussed at this meeting.

There being agreement with these suggestions, unanimous approval was given to a letter to Mr. Erickson, President of the Federal Reserve Bank of Boston, reading as follows:

This is in response to your letter of January 27, 1956, regarding the question whether obligations issued by States, counties, and political subdivisions in anticipation of the collection of taxes or the receipt of other revenues are eligible as collateral for advances by Federal Reserve Banks to member banks under section 13 of the Federal Reserve Act. You state that this question has recently been raised by several member banks in your district.

It has been the position of the Board since 1916 that tax anticipation obligations of States, counties, and municipalities are not eligible for use as collateral for advances to member banks under section 13. The revision of the Board's Regulation A which became effective February 15, 1955, was not intended to reflect any change in this position.

Governor Robertson commented on developments since his report at the meeting on Thursday, March 15, concerning the so-called compromise bank merger legislation which was worked out by the staffs of the three Federal bank supervisory agencies, and to which objection was expressed by Assistant Attorney General Barnes at an interagency meeting on March 14. He said that in an effort to arrive at something which might be agreeable to the three agencies and also to the Department of Justice, further discussions had been held by the agencies, with the result that a draft of bill had now been prepared by the Board's Legal Division which would modify the earlier proposal as follows: In the case of proposed mergers or similar transactions coming before a particular supervisory agency for approval, that agency would be required to take into consideration the factors enumerated in section 6 of the Federal Deposit Insurance Act.

It would also be required to take into consideration whether the effect of the proposed transaction might be to lessen competition unduly or to tend unduly to create a monopoly. If the agency was of the opinion that there was a substantial question whether the transaction might have such an effect, it could not grant its approval without first seeking the views of the other two banking agencies with respect to such question; and in such a case, the agency could also request the opinion of the Attorney General.

Governor Robertson then distributed copies of the new draft and discussed the provisions thereof. He said that the draft had been reviewed by persons in the Office of the Comptroller of the Currency and by the Treasury's General Counsel, that they favored such a proposal, and that they expected to discuss the matter with the Secretary of the Treasury today. If the Secretary approved, they had in mind sending the proposal to the Bureau of the Budget, which would in due course seek the views of interested agencies, including the Board. He said that if the Board should indicate today that it favored the amended proposal, he would advise the Comptroller's Office informally.

During a discussion of the revised draft, a number of questions were raised regarding the effects of the proposal from the standpoint of administration and policy.

In responding to these questions, Governor Robertson said that each supervisory agency would make a decision based on its own best

judgment, even if the other agencies registered different opinions and even if the Attorney General had been consulted. However, the agency making the decision would be in the position of having to justify its action if necessary. If it appeared that a substantial question relating to competition was involved in the proposed transaction, the agency would be required to ask the views of the other two supervisory agencies, but it would not have to seek the advice of the Attorney General unless it wished to do so. Should the agency go to the Attorney General for an advisory opinion, which would deal only with the competitive aspects of the matter, it would consider this advice, take into account all of the other aspects of the transaction, and then decide whether to follow the advisory opinion. It would not be expected that opinions received from the other supervisory agencies would be made public, but that they would be treated in the same manner as the Board's recommendations to the Comptroller of the Currency on applications for national bank charters. Judicial review of an agency's decision would, of course, be available, as it is now in bank supervisory matters, should it appear that a decision was arbitrary or capricious.

Governor Robertson then commented that the General Counsel for the Federal Deposit Insurance Corporation had expressed, during the course of discussion, the view that the proposed legislation might be so worded as to require each agency to obtain the opinion of the other

agencies on the competitive aspects of all proposed mergers submitted to it for approval.

This alternative was discussed at some length from the standpoint of the work that would be involved and other factors. Some of the members of the Board suggested that compulsory clearance might be desirable to guard against the possibility that at some future time the respective bank supervisory agencies would follow substantially different lines of reasoning in their approach to bank merger cases. It was stated that in such an event there might be, for example, an incentive for banks to withdraw from membership in the Federal Reserve System if they contemplated a merger and it appeared that the Board's policy was more rigid than that of the other supervisory agencies. The thought also was expressed that interagency clearance of cases involving no substantial problem from a competitive standpoint might not entail a substantial amount of work.

Governor Robertson said that although he had some doubt whether the procedure would be necessary, he had no strong feeling against a provision of that kind if it were clearly understood that the interagency clearance would be limited to the competitive aspects of the proposed transactions.

Governor Mills then suggested that it would be desirable for the members of the Board to have additional time in which they might give

consideration to various aspects of the legislative proposal in the form now drafted before the Board expressed an opinion.

In the circumstances, Governor Robertson said, he could inform the Comptroller's Office that while there was nothing to preclude the Treasury from sending the proposal to the Budget Bureau if it so desired, he could not state at this time what the nature of the Board's comments to the Budget Bureau would be. He also said that he could attempt to arrange another meeting with Mr. Barnes to present the amended proposal and ascertain whether Mr. Barnes would withdraw his previous objections and go along with it.

There was agreement that it would be advisable to have such a meeting. In this connection, Governor Mills stated that it would be helpful to him, and presumably to the other members of the Board, if the Legal Division could prepare a memorandum discussing the proposal and the various views regarding it, particularly such views as might be expressed at the meeting with Mr. Barnes.

At the conclusion of the discussion, it was understood that Governor Robertson would advise the Comptroller's Office along the lines which he had suggested, that he would endeavor to arrange another meeting between representatives of the supervisory agencies and Mr. Barnes, and that a memorandum of the kind proposed by Governor Mills would be prepared.

During the foregoing discussion Messrs. Riefler, Thomas, and Young withdrew from the meeting.

Governor Robertson called attention to the practice followed by a relatively small number of banks of "window dressing" their mid-year and year-end condition statements by inflating the volume of loans through various devices and, on the other hand, utilizing the reserve-averaging privilege to borrow from the Reserve Bank prior to the date of the statement and then repay the borrowing so as not to have it reflected in the statement. The supervisory agencies being aware of this practice, he felt it was incumbent upon them to endeavor to effect correction. He stated that in the absence of objection he would like to bring the matter up for discussion at the next meeting of the Interagency Committee on Bank Supervisory Matters, following which he would report to the Board. One approach, he said, would be to change the call date from time to time or at least to suggest such a possibility on an appropriate occasion.

There followed a discussion of the reasons for the practice and alternative courses of action on the part of the supervisory authorities, including the possibility of dealing with individual banks directly, perhaps in connection with examination of the banks. It was pointed out that considerable work on the part of the examiners would be required to establish proof of the practice in concrete enough form to warrant mentioning it in the examination report or at a conference with the bank's directors. The thought also was expressed that it would be undesirable to bring the practice to the attention of the public, at least in such a

way that confidence in the accuracy of bank statements might be impaired.

At the conclusion of the discussion, it was agreed that there would be no objection to Governor Robertson's mentioning the subject at the next meeting of the Interagency Committee in such a manner as he deemed appropriate, with the understanding that he would then make a report to the Board.

The meeting then adjourned.

Kenneth A. Kenyon
Assistant Secretary