Minutes for May 8, 1957

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.

Chm. Martin
Gov. Szymczak
Gov. Vardaman
Gov. Mills
Gov. Robertson
Gov. Balderston
Gov. Shepardson
Minutes of actions taken by the Board of Governors of the Federal Reserve System on Wednesday, May 8, 1957. The Board met in the Board Room at 10:00 a.m.

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

Mr. Carpenter, Secretary
Mr. Sherman, Assistant Secretary
Mr. Kenyon, Assistant Secretary
Mr. Riefler, Assistant to the Chairman
Mr. Thomas, Economic Adviser to the Board
Mr. Bethea, Director, Division of Administrative Services
Mr. Young, Director, Division of Research and Statistics
Mr. Sloan, Director, Division of Examinations
Mr. Johnson, Controller, and Director, Division of Personnel Administration
Mr. Hackley, General Counsel
Mr. Horbett, Associate Director, Division of Bank Operations
Mr. Masters, Associate Director, Division of Examinations
Mr. Solomon, Assistant General Counsel
Mr. Hexter, Assistant General Counsel
Mr. Chase, Assistant General Counsel

Proceeding involving Continental Bank and Trust Company. With reference to the current proceeding under section 9 of the Federal Reserve Act involving The Continental Bank and Trust Company, Salt Lake City, Utah, Mr. Masters reported that he and Mr. Hexter had been in telephone conversation with the Board's Special Counsel, Mr. Bolling Powell, concerning an informal meeting yesterday attended by the President and Counsel of Continental, Mr. Powell, and Counsel for the Federal Reserve
Bank of San Francisco, at which it was stated by the representatives of the member bank that arrangements had been made to sell the bank building to a New York syndicate for $2,500,000. The syndicate reportedly had deposited $50,000 in earnest money looking toward completion of the transaction by June 30, 1957, under terms involving a cash payment of $2,000,000 and the holding of a $500,000 second mortgage by Continental, which would continue to occupy the building under a lease-back arrangement at $180,000 per year. Since the bank building is now carried at $1,300,000, the consummation of the sale would provide some improvement in the capital structure of the member bank and, taking into consideration retained earnings and the substitution of liquid assets for the bank building, the net gain might amount to something in the neighborhood of $2,000,000. The latest examination of the bank indicated a capital deficiency of around $2,600,000 and conservative judgment would indicate the possibility of a reduction of the deficiency to a figure in the range of $600,000 to $750,000.

This development apparently was announced by the representatives of the member bank, Mr. Masters said, in the thought that it might be regarded by the Board as representing an acceptable solution to the Board's demand for the introduction of additional capital. Inasmuch as the hearing was to resume in Salt Lake City tomorrow morning, he and Mr. Hexter had asked the views of the Board's Special Counsel
concerning the matter of procedure, and Counsel expressed the strong feeling that the hearing should go forward in the absence of further developments. Among the reasons given by Counsel were: (1) the information developed, and to be introduced by the Board's witnesses, was of sufficient strength to prove a capital inadequacy of around $2,500,000; (2) if the proceeding were continued, a more advantageous proposal might be made by Continental; (3) arrangements had been made for witnesses and additional delay would involve considerable cost and inconvenience; (4) seasonal and other factors might contribute to a substantial delay if the hearing did not continue at this time; and (5) at the present time the hearing could be conducted on the basis of a relatively recent examination.

Mr. Masters emphasized that at this stage nothing of a concrete or formal nature had been put forward by Continental. In those circumstances, he expressed doubt whether the Board would wish to take any action at this time.

Governor Mills then made a statement in which he indicated why he would lean toward suspending the hearing until June 30 in the event of receipt of a formal, written notification from Continental stating that the offer had been received for the bank building and that the bank intended to complete the transaction. While the capital deficiency of the member bank might be larger than $1,500,000, that was the figure mentioned by the Board in its demand for additional capital and one that had come to be essentially public information.
If the Board should be informed that approximately $1,600,000 was going to be added to the capital structure through the sale of the bank building and yet proceeded in such a manner as to suggest that its original demand was not final, the Board might subject itself to criticism from the commercial banking fraternity.

Governor Mills then noted that in the course of the proceeding a very important milestone had been passed in that the courts had supported the Board's authority to demand and require the introduction of additional capital into a member bank's capital structure, on the penalty of forfeiture of membership in the Federal Reserve System. The proceeding therefore had already produced a significant result in confirming the power of the Board in this respect. If formal notification concerning the sale of the building should be received and the Board then permitted the hearing to proceed, the principal result of testimony given by the witnesses might be to expose management deficiencies and lack of quality in the bank's assets, all of which might lead to public questioning on the part of depositors and others after the ownership of the bank had offered, presumably in good faith, a plan which would meet the original capital demand. Furthermore, with regard to the bank's assets, the report of the most recent examination of the bank seemed to disclose that, while there were still substantial asset problems, there had been some improvement since the date of the previous examination.
For these various reasons, Governor Mills expressed the view that if a formal notice in writing of the sale transaction should become available, the Board should accept that offer in good faith and suspend the hearing until June 30 to allow completion of the transaction, even though additional expense to the Board might be involved. If the additional capital resulting from completion of the transaction should be introduced into the bank's capital structure but the bank's management practices did not improve, the Board would appear to be in an excellent position to proceed under section 30 of the Banking Act of 1933 to remove the management.

In a further discussion of the situation, Mr. Hexter brought out that up to this point there was only a weak basis, at best, for the Board to take any action to suspend the hearing, since the information concerning the proposed sale of the building was received orally, without any formal evidence concerning the facts of the transaction. Consequently, the actual situation might not be precisely as it now appeared. Assuming that the Board obviously would not want to terminate the proceeding on the basis of the developments to date, the alternative would be for the Board's Counsel to state at the resumption of the hearing tomorrow that he had been told of the arrangement to sell the bank building, and on this basis to move for a continuance of the hearing. This would be contrary to the judgment of Mr. Powell and the ensuing delay would involve inconvenience and additional cost. Such action would be taken on the tenuous basis of an informal conversation, and the principal reason for the action would be the possible
damage to the bank concerned or to the banking situation in Salt Lake City which might result from the testimony of the scheduled witnesses, the first two of whom would be examiners from the Federal Reserve Banks of San Francisco and Kansas City, respectively.

Governor Vardaman then suggested that if Continental was interested in a suspension or termination of the proceeding, it would seem logical for the member bank to go before the Hearing Examiner and make the information concerning the sale of the bank building a formal part of the proceeding.

There was general agreement with Governor Vardaman that the initiative in formalizing the information concerning the sale of the property should be taken by Continental and not by the Board. This led to a question by Governor Vardaman as to whether Continental had been given any reason to think that its approach on a matter of this kind could not be to the Board or the Hearing Examiner. On this point, reference was made to an earlier situation where counsel for Continental had been referred to Special Counsel for the Board, but it was noted that the previous occasion involved a matter where counsel for the bank apparently was raising a point without the knowledge of his principals. As to the role of Special Counsel for the Board, Chairman Martin made the further comment that it was Counsel's clear responsibility to keep the Board informed of developments, that he had discharged that responsibility in this instance, and that he had also given the Board his best judgment in the matter. Governor
Vardaman responded that he was not concerned about this particular instance and that his question had related to the general conduct of the proceeding.

At the conclusion of the discussion Chairman Martin said that, as he saw the situation, the current position of the Board was that it had been informed of the oral statements made by representatives of the member bank and would await further developments, there being no basis for action by the Board at present.

Unanimous agreement was expressed with Chairman Martin's statement.

Messrs. Sloan, Masters, Hexter, and Chase then withdrew from the meeting and Mr. Shay, Assistant General Counsel, entered the room.

Designation of Miami, Florida, as a reserve city. On April 17, 1957, the Board met with three representatives of the Miami member banks to receive their views on the possible designation of Miami as a reserve city. Subsequently, there had been distributed to the members of the Board copies of a memorandum from Mr. Horbett dated April 25, 1957, summarizing the principal points made by the Miami bankers and setting forth alternative courses of action open to the Board. These would include (1) designation of Miami as a reserve city, with deferment of the effective date; (2) adoption of one of three previously proposed amendments to the 1947 rule, each of which would have the practical effect of deferring a decision until the next triennial review; and
(3) further deferment of a decision with respect to the reserve city designation of Miami beyond the scheduled decision date, June 1, 1957.

Governor Vardaman stated that on the basis of his review of the record and subject to evaluation of points which might be raised at this meeting, he was rather impressed with the reasons given for postponing the designation of Miami as a reserve city until the next triennial review, particularly the extent of the seasonal deposit fluctuation at the banks in Miami. In other words, unless more serious problems were involved than occurred to him from reading the record, he felt that postponement of the designation might be warranted.

At the request of the Chairman, Mr. Horbett then summarized his views regarding the situation, saying that according to the evidence now available, Miami very probably would qualify for reserve city designation at the next triennial review on the basis of either call report figures or daily average interbank demand deposits, that the Miami bankers were aware of this, and that their objective apparently was to get the designation deferred until the next review. Considering that the reserve requirements of the Miami banks would be increased substantially under reserve city status, he did not think it unreasonable to give them some time to make the necessary adjustments, and the amendment of a rule to meet a given situation would not be too unusual. Also, while it appeared almost certain on the basis of the record that Miami would qualify for reserve city designation at the next review, this was not an absolute certainty because various developments might occur in the
interim, and the possibility of some basic change in the computation of member bank reserve requirements also must be kept in mind.

Mr. Hackley expressed the view that, if deferment of the designation was favored by the Board, it would be preferable to amend the 1947 rule in some way that would be generally applicable rather than to take specific action with respect to the city of Miami. Among the several possible amendments that had been mentioned, he favored the one which would provide that a new reserve city would not be designated unless it met the prescribed standard on two consecutive triennial reviews because, as opposed to the others, this amendment would not involve an actual change in the present formula. Such an amendment, he felt, would not require publication for comment in the Federal Register in advance of adoption and could be made effective retroactively, with publication of a notice in the Federal Register subsequent to the date of adoption.

Chairman Martin then inquired concerning the effects of the Board's decision in terms of the public interest, and it appeared from the responses that the designation of Miami would in itself have little practical significance, except from the standpoint of the local banks and competitive banking problems.

Governor Mills pointed out, however, that under the theory pertinent to the classification of reserve cities it was held to be advisable in the public interest for banks in the larger communities
holding a greater volume of volatile interbank deposits to carry a higher percentage of reserves. While that original reasoning was now challenged to a certain extent, there appeared to be some degree of substance in it. This would suggest that when the banks in a community accept a volume of interbank deposits, they have an additional responsibility to accept the burden of higher reserve requirements.

Carrying a little further the points mentioned by Governor Mills, Governor Shepardson brought out that the present level of reserve requirements is higher than necessary to satisfy the basic principle that they serve as a safety factor. Therefore, it seemed to him that in the light of existing conditions there was no particular reason from the standpoint of principle to add to the reserve requirements of the Miami banks at this time. In such circumstances, it appeared that much could be said for the amendment favored by Mr. Hackley, which would not change the basic formula, would not be discriminatory, would not do violence to the principle of safety or to monetary policy, and yet would take account of a particular situation.

After Chairman Martin had expressed general agreement with the position of Governor Shepardson, while at the same time indicating that he did not feel strongly on the matter, Governor Balderston stated that he had been principally concerned regarding the question of timing. While he felt basically that when rules are made, affected parties should be expected to abide by them, in a case like this the application of the rule suggested a certain degree of gradualness to allow the banks concerned to accommodate themselves to the new situation. He had not had
in mind a deferment of the new requirements in Miami for as long as three years, but he would be agreeable to the suggested amendment, particularly if advance publication in the Federal Register would not be required.

The point of view expressed by Governor Szymczak was that when a rule has been established and a question of its applicability arises, there is much to be said for applying the rule in the absence of a decision to make changes which apply alike to all affected parties. He noted that when an exception is made in a particular case, other requests for exceptions are likely to follow.

Governor Robertson then stated that while he could agree with much of what had been said during this discussion, any argument that reserve requirements should be considered from the credit control standpoint would seem to have special pertinence in the case of Miami. He then repeated his expression of doubt, previously stated during earlier discussions of the matter, concerning the appropriateness of changing the Board's 1947 rule on the first occasion since its adoption when the Board was confronted with the designation of a new reserve city under the rule. Because of the rapid expansion in the Miami area, Miami should be under the restriction of the higher reserve requirements prescribed for reserve cities. However, he felt that the rule should not be applied in a drastic way and that the affected banks should be given a reasonable time for adjustment. This problem, he
suggested, could be solved by making the reserve city designation in the case of Miami under the 1947 rule and then giving the member banks in that city a year or perhaps 18 months to adjust to the new reserve requirements.

At the conclusion of Governor Robertson's comments, Mr. Hackley suggested that, if the Board desired, it would be possible to amend the 1947 rule to provide that in the case of the designation of a new city as a reserve city, the effective date would be one year after the date of the Board's action or such longer period as the Board might permit.

The members of the Board indicated that they would be agreeable to such an amendment, although Governor Mills said that personally he continued to prefer somewhat the amendment providing for designation of a city only if it qualified under the prescribed standard on two consecutive triennial reviews. His principal reason for leaning toward that proposal was its element of simplicity. However, he did not regard the matter as especially important and would be willing to go along with the rest of the Board if the other approach was favored.

Accordingly, following further discussion of the alternatives, it was agreed unanimously, at the suggestion of Chairman Martin, to amend the 1947 rule in the manner now suggested by Mr. Hackley. This action contemplated that such an amendment would be prepared by the staff for consideration by the Board.

Messrs. Riefker, Thomas, Horbett, and Shay then withdrew from the meeting.
Space requirements of the Board. Last year Governor Balderston, with the assistance of the staff, studied various possibilities for meeting the Board's current and prospective space requirements, including the leasing of outside space, the provision of additional space through alterations to the Federal Reserve Building, and the construction of an annex building on the lot across "C" Street which is owned by the Board. At the conclusion of that study it was decided that the time was not propitious for the construction of an annex and that the Board's needs could be met temporarily by adjustments of office space within the present building. Since then, however, the Board's space requirements had continued to increase, and the staff, under Governor Shepardson's direction, had given further consideration to the availability of outside space.

The results of that exploration were summarized in a memorandum and attachments which Governor Shepardson distributed to the other members of the Board under date of May 1, 1957. These documents dealt particularly with the possibility of purchasing or leasing space in a cooperatively-owned building known as the Potomac Plaza Office Building at 24th Street and Virginia Avenue, N. W., which it was estimated would be ready for occupancy in about two years. While it appeared that the purchase of a floor in the building would be more economical than the leasing of space, a number of legal questions were raised for the Board's consideration. In all the circumstances, Governor Shepardson recommended
in his memorandum that the Board authorize entering into further negotiations for the leasing of approximately 10,000 square feet of space on a ten-year basis. The current offer to the Board envisaged a rate of about $5.50 per square foot per annum, but the memorandum indicated some possibility that more favorable terms might be offered if it became clear that the Board was not interested in the purchase of space in the building. The recommendation contemplated that after further negotiation, the matter would be brought back to the Board for final decision.

In reviewing the matter, Governor Shepardson stated that other rental possibilities were not too favorable and that the Board was faced with the problem of taking some step to solve its space problem as an interim measure until the time appeared proper for construction of an annex. The space in the Potomac Plaza Office Building would be relatively convenient and would offer the opportunity to transfer some division of the Board's staff to adequate outside quarters. The amount of space that would be rented apparently would not be needed in entirety at the beginning, and the proposal contemplated the possibility of subletting any unused space. Based on a projection of the past trend in space requirements of the Board, the availability of this space should provide a solution to the problem for some 10 years, by which time a decision probably could be reached on a longer-range solution.
Governor Shepardson also said that at first the idea of purchasing space in the cooperative building had had considerable appeal to him, particularly on the basis of financial considerations. However, in the light of the legal questions which were raised, he had come to the conclusion that a rental contract would be preferable.

After Governor Shepardson and Mr. Hackley had outlined the legal problems to which the former had referred, a discussion ensued which touched upon the weight that should be given to these legal problems, alternative possibilities for meeting the Board's space requirements, the reasons for not constructing an annex building at this time, and the advantages of space in the Potomac Plaza Office Building from the standpoint of proximity to the Federal Reserve Building and related factors.

From this discussion, it developed that, primarily because of the various legal considerations, the sentiment of the Board favored rental of space in the cooperatively-owned building as opposed to the purchase of space. On the matter of rental, certain questions were raised by Governor Vardaman, mostly because of the long term of the proposed lease arrangement, but he indicated that, having raised these questions for consideration, he would be prepared to go along with the other members of the Board if a decision was reached to enter into such a contract.
At the conclusion of the discussion, the recommendation of Governor Shepardson, that is, that the staff be authorized to enter into active negotiations for the lease of space on the most favorable terms possible, was approved unanimously, with the understanding that upon the completion of those negotiations the matter would be brought back to the Board for decision.

The members of the staff then withdrew and the Board went into executive session.

The Secretary later was informed that during the executive session the Board gave consideration to a letter from the Assistant Federal Reserve Agent at the Federal Reserve Bank of Richmond, relating to the suggested appointment of an Alternate Assistant Federal Reserve Agent, and that the Board approved unanimously letters to the Chairman of the Richmond Reserve Bank and to the Assistant Federal Reserve Agent in the form of the letters attached to these minutes as Items 1 and 2.

The meeting then adjourned.

Secretary's Note: Pursuant to the recommendation contained in a memorandum dated May 3, 1957, from Mr. Bethea, Director, Division of Administrative Services, Governor Shepardson approved on behalf of the Board on April 7, 1957, the appointment of Arthur Lee Fuller as Messenger in that Division, with basic salary at the rate of $2,690 per annum, effective the date he assumes his duties.
Governor Shepardson also approved on behalf of the Board the following letters, copies of which are attached to these minutes under the respective item numbers indicated:

Letter to the Federal Reserve Bank of New York approving the appointments of Edwin W. Pfaff and Warren C. Straub as assistant examiners.

Letter to the Federal Reserve Bank of Richmond approving the designation of Herbert L. Garrett as special assistant examiner.

Item No.

3

4
May 10, 1957

Mr. John B. Woodward, Jr.,
Chairman,
Federal Reserve Bank of Richmond,
Richmond 13, Virginia.

Dear Mr. Woodward:

Enclosed is a letter received by the Board of Governors from Mr. R. L. Shepherd, Assistant Federal Reserve Agent at the Federal Reserve Bank of Richmond, dealing with a matter which should have your consideration as Federal Reserve Agent.

Also enclosed is copy of a letter advising Mr. Shepherd of this disposition of his letter.

Very truly yours,

(Signed) S. R. Carpenter

S. R. Carpenter,
Secretary.

Enclosures
May 10, 1957

Mr. R. L. Shepherd,
Assistant Federal Reserve Agent,
Federal Reserve Bank of Richmond,
Richmond 13, Virginia.

Dear Mr. Shepherd:

Your letter of April 10, 1957, concerning the Alternate Assistant Federal Reserve Agent at the Federal Reserve Bank of Richmond has been referred to the Federal Reserve Agent of your Bank, Mr. John B. Woodward, Jr., Chairman of the Board. A copy of the letter of transmittal to Mr. Woodward is enclosed.

Very truly yours,

(Signed) S. R. Carpenter

S. R. Carpenter,
Secretary.

Enclosure
May 8, 1957

Mr. A. Phelan, Vice President,
Federal Reserve Bank of New York,
New York 45, New York.

Dear Mr. Phelan:

In accordance with the request contained in your letter of May 2, 1957, the Board approves the appointment of Edwin W. Pfaff and Warren C. Straub as assistant examiners for the Federal Reserve Bank of New York.

Please advise the Board as to the dates on which these appointments are made effective.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,
Assistant Secretary.
May 8, 1957

Mr. N. L. Armistead, Vice President,  
Federal Reserve Bank of Richmond,  
Richmond 13, Virginia.

Dear Mr. Armistead:

In accordance with the request contained in your letter of May 2, 1957, the Board approves the designation of Herbert L. Garrett as a special assistant examiner for the Federal Reserve Bank of Richmond for the purpose of participating in examinations of State member banks only.

Very truly yours,

(Signed) Merritt Sherman  

Merritt Sherman,  
Assistant Secretary.