Minutes for August 18, 1958

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	
Gov. Szymczak		x
Gov. Vardaman	x	
Gov. Mills		x
Gov. Robertson		x
Gov. Balderston	x	
Gov. Shepardson	x	

Minutes of the Board of Governors of the Federal Reserve System on Monday, August 18, 1958. The Board met in Room 1202 at 10:00 a.m.

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

Mr. Kenyon, Assistant Secretary
Mr. Fauver, Assistant Secretary
Mr. Riefler, Assistant to the Chairman
Mr. Hackley, General Counsel
Mr. Solomon, Assistant General Counsel

Messrs. Young, Garfield, and Noyes, Miss Burr, and Messrs. Koch, Dembitz, Brill, Gehman, Altmann, Keir, Manookian, Peret, T. Smith, Solomon, Wernick, and Wood of the Division of Research and Statistics
Messrs. Marget, Furth, Sammons, Bangs, Dahl, Reynolds, and Summers of the Division of International Finance

Economic review. In summarizing the review of international trade and financial developments presented by the Division of International Finance, Mr. Marget said that until indications appeared of a strong upward movement in United States exports, it would not be possible to say that economic developments abroad were such as to reinforce the trend toward recovery in the United States. On the other hand, there was no evidence to suggest that foreign developments would serve to retard such recovery.

Statistics cited by members of the Division of Research and Statistics in their review of domestic developments afforded further evidence of a significant upward trend in economic activity.

Members of the two Divisions then commented informally in response to a number of questions raised by members of the Board in the light of the economic review, after which they withdrew from the meeting. Mr. Riefler also withdrew at this point and Mr. Leonard, Director, Division of Bank Operations, entered the room along with Messrs. Masters, Director, Smith, Assistant Director, and Holahan, Supervisory Review Examiner, Division of Examinations.

Items circulated to the Board. The following items, which had been circulated to the members of the Board and copies of which are attached to these minutes under the respective item numbers indicated, were approved unanimously:

	Item No.
Letter to the Federal Reserve Bank of New York concerning their review of employees' ages for purposes of retirement.	1
Telegram to the Federal Reserve Bank of Chicago authorizing expenditures for the completion of nine alteration items at the head office building.	2
Letter to the Federal Reserve Bank of Dallas interposing no objection to the reemployment of certain retired employees for a temporary period in connection with Commodity Credit Corporation work.	3
Letter to the Federal Reserve Bank of San Francisco concerning various matters to be considered when the territory of Alaska becomes a State.	4

Participations between banks under section 6(a) of the Bank Holding Company Act (Item No. 5). In its statement on the General Contract Corporation case, decided earlier this year, the Board expressed the view

among other things that the nonrecourse purchase of instalment paper constitutes a "discount" within the meaning of section 6(a)(4) of the Bank Holding Company Act of 1956, which forbids a bank "to make any loan, discount, or extension of credit to a bank holding company of which it is a subsidiary or to any other subsidiary of such bank holding company". In the course of that statement the Board also said:

> "It may be noted, however, that when one bank seeks participation by another bank to aid in meeting the credit needs of a borrower, there would seem to be no conflict with section 6 if the second bank joined at the outset in making its portion of the loan, since this would not involve the second bank in either a direct loan to the first bank or a purchase of paper from it. This would seem to permit at least a partial solution of the problems involved in participations."

Subsequently, the Northwestern National Bank of Minneapolis, Minneapolis, Minnesota, forwarded through the Federal Reserve Bank of Minneapolis a request for clarification of the above statement with respect to interbank participations. Inquiries also were received from the Federal Reserve Bank of Boston as a result of examinations of member banks which uncovered possible violations of section 6(a) of the Bank Holding Company Act depending, presumably, on interpretation of the Board's statement in the General Contract Corporation case.

Prior to this meeting there had been distributed to the members of the Board copies of a memorandum from Mr. Solomon dated August 14, 1958, outlining four situations which it was believed might be considered to involve a "joining at the outset". These four situations were set forth in

a draft of interpretation which it was suggested might be sent to the Minneapolis and Boston Reserve Banks, as well as to the other Reserve Banks, and also might be published in the Federal Reserve Bulletin. The draft expressed the view that in connection with participations the originating bank might handle the receipt of payments on loans from the borrower for the account of the participating bank without violating section 6 of the Bank Holding Company Act.

In commenting on the matter at the request of the Board, Mr. Solomon said the proposed interpretation did not seem to conflict with the general purposes of the statute and that in the legal staff's opinion it would be desirable for the Board to take the position stated therein.

Mr. Hackley recalled that this was one of the principal problems growing out of the Board's decision in the General Contract case, and that holding company representatives had discussed the problem at a meeting with the Board. A general interpretation of this kind would help to clarify the situation, and it was his view that the bank holding companies were entitled to such a clarification. Since the proposed interpretation would not necessarily answer all questions, any particular case that involved a material deviation would have to be considered separately. However, he did not have any reservations regarding the opinions expressed in the proposed interpretation.

In response to a question raised by Governor Vardaman, Mr. Solomon confirmed that the proposed interpretation did not relate to specific cases and instead was intended to afford general guidance.

Mr. Masters raised certain questions bearing upon whether an interpretation ought to be so much concerned with the mechanical details of settlement, to which Mr. Solomon replied that to some extent the statute appeared to make it essential to consider the method of settlement. He also pointed out that a certain amount of latitude would be allowed under the proposed interpretation. Mr. Masters then stated that in general the Division of Examinations agreed with the conclusions expressed in the interpretation. He said that if the Board should issue the interpretation, the Division would take steps to see that the Federal Reserve Bank examiners were properly informed.

Thereupon, the proposed statement of interpretation, a copy of which is attached hereto as Item No. 5, was approved unanimously. In accordance with the suggestion in Mr. Solomon's memorandum, this action contemplated that appropriate advice would be given to the Federal Reserve Banks and that the interpretation would be published in the Federal Register and the Federal Reserve Bulletin.

Proposed simultaneous examination of a member bank and its affiliated banks. At its meeting on Friday, August 15, 1958, the Board discussed a proposal of the Division of Examinations that at the time of the next examination of The Continental Bank and Trust Company, Salt Lake City, Utah, there be a simultaneous examination of all of the banks affiliated with that institution through common ownership, including four State member banks, a national bank, three nonmember insured banks, and

three nonmember noninsured banks, all in the Twelfth Federal Reserve District. The national bank and the three nonmember insured banks would be examined by the Comptroller of the Currency and the Federal Deposit Insurance Corporation, respectively, while the four State member banks and the three nonmember noninsured banks would be examined by representatives of the Federal Reserve Bank of San Francisco. The respective State banking departments would be invited to participate in the examinations of all of the State banks.

Governor Vardaman, who had raised certain questions regarding the proposal at the meeting last Friday, stated that subsequent to the meeting he had discussed further with Messrs. Hackley and Masters the statutory provisions relating to the authority of the Federal Reserve System to make examinations of nonmember noninsured banks affiliated with a State member bank. From this additional discussion, he said, it appeared that there was unquestionably a right on the part of a Federal Reserve Bank examiner to go into any nonmember noninsured bank in his discretion if such bank was controlled by the same interests as a State member bank. Despite that technical authority, however, he still had reservations as to the desirability of such a procedure except when the examinations were made at the invitation of the State banking authorities concerned. Further, it was his view that in principle the Federal Reserve System would be in a much better position if it also obtained the consent of the controlling stockholders of the affiliated banks. With further reference to the

matter of interagency cooperation, he suggested that failure to obtain the consent of the State banking authorities might tend to put the System in the position of violating the dignity of the State in question. With reference to attempting to obtain shareholders' consent, he said that he felt such an effort was sound in principle. However, if consent was not forthcoming, he felt that it would be necessary for the System to proceed with the examinations in view of the fact that the statute seems to make such a course mandatory.

Following comments by Mr. Masters on the possibility of cooperation with the Utah State banking authorities and the reasons why it was deemed advisable to make a simultaneous examination which would include the three State nonmember noninsured banks, Governor Vardaman stated that he was in favor of making such examinations. He doubted, however, whether the authority given in the statute was intended to permit violating the traditional independence of the State nonmember bank. On this point Mr. Hackley stated that he thought a nonmember noninsured bank could, if it wished, refuse to be examined and that, if so, the System might be without legal recourse. It could only proceed against the affiliated State member bank by endeavoring to expel that bank from membership in the System.

Governor Vardaman then stated that if the question of the right of the System to enter a State nonmember bank should ever be raised it might amount to opening a Pandora's box, and Chairman Martin agreed that this was

a point to be borne in mind. However, the Chairman said, the case now under consideration was an exceptional situation, and the System should do whatever it could.

In further discussion, Governor Shepardson suggested that in this case it would appear almost hopeless to endeavor to obtain the shareholders' consent.

Governor Vardaman agreed, and indicated that in the circumstances he would not be inclined to make the effort. All of the evidence, he said, seemed to show that it would be a waste of time to try to obtain such consent.

At the instance of Governor Shepardson, there followed some discussion of the question of making the arrangements for simultaneous examination through the Federal Reserve Bank of San Francisco in accordance with the customary procedure. Governor Vardaman indicated that he would be inclined to follow the usual procedure and that, in any event, it appeared to be too late to make a change in this particular case.

Governor Vardaman then raised the question whether there should be consultation with the Board's Special Counsel, Mr. Powell, with regard to the proposed arrangements for simultaneous examination, and agreement was expressed with the view that it would be desirable to check with Mr. Powell.

At the conclusion of the discussion, the proposal for simultaneous examination was approved by unanimous vote, with the understanding that

the necessary procedural steps would be taken by the Division of Examinations in conjunction with the Legal Division.

Mr. Holahan then withdrew from the meeting.

Incident at Jacksonville Branch. With further reference to his report at the Board meeting on Thursday, August 14, regarding the contest prize claimed by the wife of a Cash Department employee at the Jacksonville Branch of the Federal Reserve Bank of Atlanta on the strength of a dollar bill bearing a certain serial number which the employee had abstracted from the Bank's cash supply in exchange for a dollar bill of his own, Mr. Leonard stated that the matter now appeared to have been brought to a satisfactory conclusion. The employee's wife had renounced her claim to the contest prize on the basis that the dollar bill had not yet been placed in circulation and therefore should not have been submitted for the purpose of claiming the prize. At the same time, the employee, whose attitude had been highly cooperative, was assured by the management of the Reserve Bank that the incident would not be held against his employment record.

Messrs. Leonard and Solomon then withdrew from the meeting.

Reports of examination of the San Francisco and St. Louis Reserve Banks. Reports of examination of the Federal Reserve Banks of San Francisco and St. Louis made as of April 15, 1958, and May 15, 1958, by the Board's field examining staff had now completed circulation to the Board and, upon request, Mr. Smith commented on the findings of the two

examinations. In the light of these comments, it was understood that Chairman Martin would discuss with President Mangels a margin account reportedly maintained with a stock brokerage house by an employee of the San Francisco Reserve Bank. It appeared that the maintenance of the account antedated the individual's employment by the Reserve Bank and that, although the account had been reduced subsequent to his employment, it had not been eliminated at the time of the examination. With respect to a planned conversion to purchased steam at the head office of the St. Louis Reserve Bank, it was understood, in view of questions raised by Governor Vardaman, that Mr. Smith would check with the Division of Bank Operations to ascertain whether the Reserve Bank had in mind maintaining a standby arrangement for power and that, if necessary, Mr. Smith would report back to the Board on the matter.

Discount rates. Chairman Martin referred to the action taken by the Board last Thursday, August 14, in approving for the Federal Reserve Bank of San Francisco a discount rate of 2 per cent and for other Reserve Banks a rate of 1-3/4 per cent. He suggested that if advice should be received from any Reserve Bank that it had established either a rate of 1-3/4 per cent or a rate of 2 per cent, the Board authorize the Secretary's Office to notify such Bank of the approval of such rate.

The procedure suggested by Chairman Martin was approved unanimously, with the understanding that the authorization would continue in effect until further action on the part of the Board.

The meeting then adjourned.

Kenneth A. Kenyon
Assistant Secretary

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON 25, D. C.

Item No. 1
8/18/58

August 18, 1958

Mr. Walter H. Rozell, Jr.,
Vice President,
Federal Reserve Bank of New York,
New York 45, New York.

Dear Mr. Rozell:

This will acknowledge receipt of your letters of July 10 and 14 and Mr. Smedley's letters of August 4 and 6 concerning your review of employees' ages for purposes of retirement.

It is noted that all of the employees involved were inadvertently retained in service past retirement age because of their having reported incorrect birth dates.

Very truly yours,

(Signed) Kenneth A. Kenyon

Kenneth A. Kenyon,
Assistant Secretary.

T E L E G R A M
LEASED WIRE SERVICE

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON

Item No. 2
8/18/58

August 18, 1958

Allen - Chicago

Reurlet of August 4, 1958. Board authorizes, at convenience of and in accordance with best judgment of Bank, completion of nine alteration items as described in your letter at a cost of approximately $286,000 exclusive of architects' fees. It is noted that Bank plans to do much of the work with Bank's own maintenance people, with resulting economies.

(Signed) Kenneth A. Kenyon

Kenyon

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON 25, D. C.

Item No. 3
8/18/58

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

August 18, 1958

Mr. James A. Parker,
Director of Personnel,
Federal Reserve Bank of Dallas,
Dallas 2, Texas.

Dear Mr. Parker:

Referring to your letter of August 4, 1958, the Board interposes no objection to your Bank's re-employing Mrs. Bertha S. Russ, who retired May 1, 1958, for a temporary period, in connection with an increase in the volume of work in the Commodity Credit Corporation Department that it is anticipated will be of short duration.

The Board also understands that your Bank may re-employ three other retirees under similar arrangements as set forth in your telephone conversation of July 30, 1958, with Mr. Johnson, and interposes no objection to these re-employments.

Very truly yours,

(Signed) Kenneth A. Kenyon

Kenneth A. Kenyon,
Assistant Secretary.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON 25, D. C.

Item No. 4
8/18/58

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

August 18, 1958

Mr. H. N. Mangels, President,
Federal Reserve Bank of San Francisco,
San Francisco 20, California.

Dear Mr. Mangels:

Please accept our thanks for your letter of July 22, 1958, calling attention to various matters which the Federal Reserve System will have to consider when the territory of Alaska becomes a State.

As you know, the Board has received a suggestion that an additional Federal Reserve District be established to serve the Pacific Northwest and Alaska. This would, of course, require legislation. It is assumed that Alaska will become a State within a few months. If that is the case, it is the Board's intention to include Alaska in the Twelfth Federal Reserve District when statehood becomes effective. This action would be without prejudice as to any subsequent decision which may be reached in the light of a study being made of appropriate changes in Federal Reserve District lines to include Alaska and Hawaii, should the latter also become a State.

The new statute provides that existing national banks in Alaska shall become members of the System within 90 days after admission of the State into the Union, and no permission by the System is required. To this extent, such banks appear to be similar to other national banks which automatically are admitted to membership without examination by a Federal Reserve Bank.

As noted above, the national banks do not have to become members until 90 days after admission of the State into the Union. It is possible that some banks may take steps to become members immediately, while others may await the full 90 days. Consequently,

further thought will have to be given to the timing of a public announcement of membership in the System.

In connection with check collections, it would be most desirable, as you suggest, for Alaskan banks to make a local exchange of a substantial share of Alaskan items, thus eliminating the two-way transportation of items drawn on Alaskan banks originating in that State.

It will be appreciated if you will continue to give the Board advice of any developments pertaining to Alaska as they affect System matters.

Very truly yours,

(Signed) Kenneth A. Kenyon

Kenneth A. Kenyon,
Assistant Secretary.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON 25, D. C.

S-1666
Item No. 5
8/18/58

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

August 19, 1958.

Dear Sir:

Attached is a copy of an interpretation of section 6 of the Bank Holding Company Act of 1956 and that portion of the Board's Statement in the matter of General Contract Corporation, which appears in the Federal Reserve Bulletin for March 1958, page 269, first full paragraph. The interpretation concerns participation loan agreements between banks under section 6(a) of the Bank Holding Company Act.

The interpretation will be published in early issues of the Federal Register and the Federal Reserve Bulletin.

Very truly yours,

Kenneth A. Kenyon

Kenneth A. Kenyon,
Assistant Secretary.

Enclosure

TO THE PRESIDENTS OF ALL FEDERAL RESERVE BANKS

PARTICIPATIONS BETWEEN BANKS UNDER SECTION 6(a)
OF THE BANK HOLDING COMPANY ACT

The Board's Statement in the matter of General Contract Corporation, which appears in the Federal Reserve Bulletin for March 1958, at p. 260, expressed the view, among other things, that the nonrecourse purchase of installment paper constitutes a "discount" within the meaning of section 6(a)(4) of the Bank Holding Company Act of 1956, which forbids a bank "to make any loan, discount or extension of credit to a bank holding company of which it is a subsidiary or to any other subsidiary of such bank holding company." In the course of that Statement the Board also said (p. 269):

> "It may be noted, however, that when one bank seeks participation by another bank to aid in meeting the credit needs of a borrower, there would seem to be no conflict with Section 6 if the second bank joined at the outset in making its portion of the loan, since this would not involve the second bank in either a direct loan to the first bank or a purchase of paper from it. This would seem to permit at least a partial solution of the problems involved in participations."

The Board has been asked further questions as to when a bank may be considered to have "joined at the outset in making its portion of the loan" within the meaning of the principle quoted above.

This principle must be read in the light of a specific exemption appearing in the last sentence of section 6(a) of the Bank Holding Company Act which provides that:

"Non-interest-bearing deposits to the credit of a bank shall not be deemed to be a loan or advance to the bank of deposit, nor shall the giving of immediate credit to a bank upon uncollected items received in the ordinary course of business be deemed to be a loan or advance to the depositing bank."

This specific exemption must, in turn, be considered against the background of the following statement by the Committee on Banking and Currency of the House of Representatives appearing in a report on the Bank Holding Company Act (H.R. Rep. No. 609, 84th Cong., 1st sess., 25 (1955)):

"Routine banking transactions between subsidiary banks are not treated as extensions of credit and do not fall within the prohibitions of this section."

It is clear from both the exemption and this statement in the House Committee Report, that the exemption refers only to interbank transactions and does not encompass transactions between bank and nonbank affiliates of the same bank holding company. The unique ability of banks to maintain deposit accounts, coupled with the section 6(a) exemption relating to such accounts, distinguishes bank subsidiaries from nonbank subsidiaries, and makes it possible, at least in some circumstances, for both an originating bank and a participating bank to "join at the outset" in making a loan, even though, the originating bank may handle all the arrangements with, and disbursements to, the borrower.

Four different factual situations have been considered by the Board from the point of view of whether they constitute a "joining at the outset" in the light of the above quotation from

the General Contract Corporation case and the exemption set forth in the last paragraph of section 6(a) of the Act. In each of the four factual situations, there was in existence prior to or concurrent with the laying out of funds to the borrower a participation loan agreement between the originating bank and the participating bank; the agreement covered a specific loan or line of credit and a specific borrower, and it did not relate to a mere block of unidentified paper.

The first of the four factual situations was the clearest and simplest case. In this situation, in addition to the existence of the participation loan agreement as mentioned above, the participating bank had on deposit with the bank originating the loan a sum sufficient to cover the participating bank's portion of the loan, and had instructed the originating bank to debit the account of the participating bank to the extent of the latter's participation in the loan. The Board expressed the view that in this situation in which the participating bank has the funds on deposit at the originating bank, the transaction is exempted as a "joining at the outset" even though there may be an interval of time during the day, in accordance with usual banking practices, between the advancing of the funds to the borrower and the actual debiting of the participating bank's account.

The second factual situation was similar to the first one but differed from it in that funds sufficient to cover the participating bank's portion of the loan were not physically on hand at the

originating bank at the time of the laying out of funds to the borrower, but, instead, prior to that time were wire transferred by the participating bank to the credit of the originating bank at a Federal Reserve Bank or some other correspondent of the originating bank. This situation was considered by the Board to be exempt as a "joining at the outset" in view of the similarity between funds actually on deposit with the originating bank and funds transferred to its credit at a correspondent.

In the third factual situation, while there was a specific participation loan agreement as in the other situations, the participating bank did not have a deposit with the originating bank and also did not transfer funds to the account of the originating bank at the latter's correspondent. Instead, the originating bank had a deposit with the participating bank. The originating bank also had instructions from the participating bank that when the former made funds available to the borrower, the originating bank would: (1) concurrently or immediately thereafter make an appropriate entry, in the amount of the participating bank's portion of the loan, to the originating bank's record of its deposit account with the participating bank; (2) promptly forward to the participating bank, in the manner usually followed in the ordinary course of business, evidence of that bookkeeping entry together with a certificate of participation in the loan; and (3) advise the participating bank by telephone or telegraph

of the two preceding steps. The participating bank, upon receipt of that advice, would credit the account of the originating bank with the amount of the participating bank's participation. In view of the fact that this establishment by the participating bank of a credit to the account of the originating bank would be similar to the transfer of funds to the originating bank's account at a correspondent bank in the second situation, the Board reached the conclusion that this third factual situation similarly qualified for exemption as a "joining at the outset".

The fourth factual situation was the same as the third except that step (3) mentioned above, namely, advice by telephone or telegraph from the originating bank to the participating bank, was omitted. As much as a day or so could, therefore, elapse before the participating bank would receive the documents referred to in step (2) and actually make the entry on its own books to show the credit to the account of the originating bank. This fourth situation presented a closer and more doubtful question than the other three. However, considering all the circumstances, including the purposes and legislative history of the last paragraph of section 6(a), the Board expressed the opinion that this fourth situation should also be considered to be exempt as a "joining at the outset".

In connection with each of the four factual situations described above, questions have also been raised as to whether

the originating bank may handle the receipt of repayments by the borrower and may transfer the participating bank's portion of such repayments to the participating bank by crediting a deposit account of the latter at the originating bank. The Board expressed the opinion that these activities are clearly permitted by the exemption in the last paragraph of section 6(a).

Questions involving participation loans between affiliates of the same bank holding company necessarily depend on the particular circumstances involved, and the views outlined above were based on the Board's understanding of the factual information in the respective situations. If in actual practice there are material variations from the factual situations summarized above, the matter would, of course, need to be considered in the light of those circumstances.