

Minutes for November 28, 1960

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, please initial below. If you were present at the meeting, your initials will indicate approval of the minutes. If you were not present, your initials will indicate only that you have seen the minutes.

Chm. Martin

Gov. Szymczak

Gov. Mills

Gov. Robertson

Gov. Balderston

Gov. Shepardson

Gov. King

Handwritten initials and signatures for each member: Chm. Martin (circled 'M'), Gov. Szymczak (signature), Gov. Mills (signature), Gov. Robertson (initials 'R'), Gov. Balderston (initials 'CCB'), Gov. Shepardson (signature), Gov. King (signature).

Minutes of the Board of Governors of the Federal Reserve System
on Monday, November 28, 1960. The Board met in the Board Room at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Balderston, Vice Chairman
Mr. Szymczak
Mr. Robertson
Mr. King

Mr. Sherman, Secretary
Mr. Kenyon, Assistant Secretary
Mr. Young, Adviser to the Board
Mr. Fauver, Assistant to the Board
Mr. Hackley, General Counsel
Mr. Farrell, Director, Division of Bank Operations
Mr. Solomon, Director, Division of Examinations
Mr. Masters, Associate Director, Division of
Examinations
Mr. Chase, Assistant General Counsel
Mr. Hooff, Assistant General Counsel
Mr. Conkling, Assistant Director, Division of
Bank Operations
Mr. Landry, Assistant to the Secretary
Mr. Collier, Chief, Current Series Section,
Division of Bank Operations

Discount rates. The establishment without change by the Federal Reserve Banks of Richmond and Dallas on November 25, 1960, of the rates on discounts and advances in their existing schedules was approved unanimously, with the understanding that appropriate advice would be sent to those Banks.

Applications for reduced reserve requirements. There had been circulated under date of November 1, 1960, a memorandum from the Division of Bank Operations recommending that permission be granted to Lake Shore National Bank, Lake View Trust and Savings Bank, Mercantile National Bank, Merchandise National Bank, and Northwest National Bank, all of Chicago,

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Illinois, to maintain the reserves required of banks outside of central reserve and reserve cities, but that action on similar applications from Exchange National Bank and Central National Bank, also of Chicago, be deferred until such time as general standards were established for the classification of reserve cities and individual banks.

At its meeting on July 21, 1960, the Board had approved the request of United States Trust Company, Boston, Massachusetts, for permission to carry reduced reserves, and during that meeting reference was made to similar requests from the aforementioned banks in Chicago on which action had previously been deferred on March 23, 1960. The Division of Bank Operations was now resubmitting the Chicago applications, with the exception of one from Chicago City Bank and Trust Company, which withdrew from membership on October 10, 1960, in view of the discussion at the July 21 meeting and the elimination, effective December 1, 1960, of the differential between the reserve requirements of central reserve city and reserve city banks. According to the Division's memorandum, all of the Chicago banks whose applications were resubmitted, except Exchange National and Central National, would be eligible for declassification under the tentative criteria set forth in a memorandum of June 23, 1960, from Mr. Thomas, Adviser to the Board. The Federal Reserve Bank of Chicago recommended approval of reduced reserves for all the banks mentioned except Exchange National, the only central reserve city bank in the group.

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Governor Robertson inquired as to the desirability of acting on further individual applications for reduced reserves prior to the adoption of general criteria.

During a discussion of this point, reference was made to a memorandum dated September 28, 1960, from Mr. Thomas and Mr. Dembitz, Associate Adviser, Division of Research and Statistics, which summarized comments received from the Reserve Banks in reply to the Board's letter of August 23, 1960, along with the report of the Subcommittee on Legislation of the Conference of Presidents and views expressed by the Presidents at their meeting with the Board on September 13. It was indicated that no further staff studies were in progress.

It was then decided to defer action on the applications for reduced reserves from the specified Chicago member banks pending further discussion at an early date of criteria for classifying cities for reserve purposes and exempting individual banks from the reserve city bank classification.

Mr. Collier then withdrew from the meeting and Mr. Noyes, Director, Division of Research and Statistics, entered the room.

Common trust funds (Item No. 1). Distribution had been made of a memorandum dated November 8, 1960, from Mr. Masters concerning the relationship to Regulation F, Trust Powers of National Banks, of a personal retirement trust plan announced recently by Girard Trust Corn Exchange Bank, Philadelphia, Pennsylvania. This plan, which had received widespread publicity, provided for investment of trusteed funds in either or both of

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two new common trust funds established under the provisions of section 17 of Regulation F. In essence the plan involved:

1. The execution of a printed single-page trust agreement, with Girard named as sole trustee;
2. The opening of an interest-bearing savings account with Girard (minimum deposit \$100) to which the customer may add amounts of \$100 or more from time to time;
3. Transfer of the savings account balance, when it aggregates \$1,000, to the trust of the individual concerned; and
4. Investment of this amount, together with subsequent additions by the customer and accumulations of income and capital gains, in either or both of the two newly-established common trust funds--one a diversified fund and the other an equity fund.

As stated in the memorandum, it was not contemplated under the Girard plan that the settlor would desire any different disposition of his trusteed property than that provided by the trust instrument (revocable at any time and payable to the settlor's estate at death) and no provision was made for the settlor to designate alternative methods of disposition. However, in the event of disability of the settlor, the trustee was authorized at its discretion to apply income and principal of the trust to the comfort and support of the settlor.

It was the view of the Division of Examinations, as expressed in the memorandum, that the purposes of the Girard plan might be regarded as not conforming with the "bona fide fiduciary purposes" specified in section 17 of Regulation F for the creation and use of common trust funds.

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It was felt that acceptance of the argument that the creation of an estate for future retirement and the professional care and management of the property so set aside represented a true fiduciary purpose might lead to labeling any form of saving and investment as a bona fide fiduciary purpose. The appeal made by this plan was apparently not to those who primarily would have need for a trust, in the conventional sense, but to the individual small saver whose primary goal was the accumulation of an estate for the future. Therefore, since an integral part of the plan's appeal was the use of a common trust fund, in this sense the fund became a device to create desire by the individual to establish a savings and investment plan. It was the recommendation of the Division of Examinations that the Board publish in the Federal Register for comment a proposal to amend section 17(a) of Regulation F so as to declare ineligible for common trust fund participation the funds of any inter vivos trust revocable by the settlor and providing for the payment of the principal to the settlor's estate at his death.

In connection with this recommendation, the memorandum noted that there were at least two alternative courses that the Board might follow. It could take the view that the developing practice of extending common trust funds to accounts not originally contemplated for inclusion in such funds was consistent with the best interest of corporate trusteeships, commercial banking, and the public, or it could reject recent developments in this area and adhere to a strict interpretation of section 17 of the

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Regulation. Should the Board be inclined to the first view, attention was called to the Congressional intent inherent in section 584 of the Internal Revenue Code exempting common trust funds, as therein defined, from Federal income taxation, along with the question whether the effects of an expanded use of the common trust fund by member banks would result in violation of section 21 of the Banking Act of 1933, prohibiting banks from engaging in the securities business. With respect to the latter point, the Securities and Exchange Commission had questioned the purposes of Girard's newly-announced plan, and the practices by which accounts would be solicited, apparently against the possibility that the plan involved the sale of securities to the public.

At the request of the Board, Mr. Masters reviewed in some detail the background and original purpose of the common trust fund provisions found in section 17 of Regulation F, emphasizing that such funds were intended to enable banks to administer more effectively smaller trust accounts established for bona fide fiduciary purposes. In his comments Mr. Masters also touched upon the successful experience of banks with the administration of common trust funds and to the growth of changed concepts in some quarters regarding the use of such funds. Reference was made to the difficulty of defining the test of bona fide fiduciary purpose, particularly in the case of revocable living trusts, and to the fact that certain arrangements, exemplified by the Girard plan, seemed to tend in the direction of providing competition for mutual investment trusts.

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Consequently, the question arose whether the administration of common trust funds approaching in purpose those of a mutual investment trust designed for public participation would not constitute in substance a re-entry by banks into the business of selling securities to the public, an activity prohibited by the Banking Act of 1933.

Publication of the proposed amendment to Regulation F, Mr. Masters suggested, would constitute notice to those in the trust field that the Board entertained reservations about the expansion of common trust funds for use in circumstances that did not appear to be in harmony with the purposes for which the establishment of such funds was originally authorized. Thus, it was felt that the publication of such a proposal in the Federal Register would cause banks to exercise caution before proceeding with new plans, even though technically the value of such an amendment as a deterrent might not be too great. Also, this procedure would permit a careful weighing of views and arguments that almost certainly would flow into the Board.

There ensued general discussion with respect to the nature, operation, and growth of common trust funds, and as to the efficacy of an amendment to Regulation F such as had been proposed. It was brought out that the widespread interest evoked by announcement of the Girard plan suggested a need for prompt action of some kind on the part of the Board.

Governor Robertson then suggested that, in addition to following the recommendation of the Division of Examinations, the Board undertake a

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comprehensive study of all features of its common trust fund regulations against the background of the history of common trust funds and their administrative experience, as well as in the light of changing concepts of their purpose and use. In this connection, he proposed the holding of a seminar through which the Board could obtain a full range of views representative of institutions and individuals concerned with the appropriate use of common trust funds by banks and trust companies.

Chairman Martin expressed concurrence in Governor Robertson's suggestion, indicating that he thought the proposed procedure would be helpful in bringing the Board up to date on recent changes in the trust business, which had been considerable over the past several years. He recalled that no comprehensive review of problems in this area had been undertaken by the Board during the period of his service with the Board.

After further discussion, the publication in the Federal Register for comment of the proposed amendment to section 17(a) of Regulation F was unanimously approved. In taking this action it was understood that the proposed comprehensive study of common trust funds would be undertaken and that the staff would submit a memorandum concerning suggested arrangements for a seminar of the type suggested by Governor Robertson.

Secretary's Note: There is attached as Item No. 1 a copy of the press statement relating to the fore-going action which was released on November 29, 1960.

The meeting then adjourned.

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Secretary's Notes: Governor Shepardson today approved on behalf of the Board a letter to the Federal Reserve Bank of Chicago (attached Item No. 2) approving the appointment of Roger E. Schultz as examiner.

Governor Shepardson also approved today on behalf of the Board a letter to the Presidents of all Federal Reserve Banks transmitting copies of the forms to be used by State member banks and their affiliates in submitting reports as of the next call date, it being understood that the letter would be sent when the forms were printed.



Secretary

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Item No. 1
11/28/60

Statement for the Press

For Immediate Release
November 29, 1960.

The Board of Governors of the Federal Reserve System is undertaking a comprehensive study of all features of its common trust fund regulations against the background of the history of common trust funds and their administrative experience, as well as in the light of changing concepts of their purpose and use. In this effort the Board will seek views representative of institutions and individuals concerned with the appropriate use of common trust funds by banks and trust companies.

Common trust funds, as defined by Section 584, Internal Revenue Code and regulated by the Board were intended to aid banks and trust companies establishing such common trust funds to administer more effectively and economically certain accounts for which the bank or trust company held an appointment as trustee, executor, administrator or guardian, provided such accounts were created and used for bona fide fiduciary purposes. The Regulation prohibits "the operation of such common trust funds . . . for other than strictly fiduciary purposes."

Questions have arisen from time to time as to the eligibility of various kinds of trusts for participation in common trust funds so established and regulated. In order to emphasize the special purposes and restricted use of common trust funds, to make more specific the types of trusts which may not be properly invested in participations in common trust funds and to prohibit the use of such funds as a medium attracting individuals primarily seeking investment management of their funds, the Board currently is considering an amendment of the common trust fund provisions of its Regulation F by adding a new sentence following the third sentence of the third paragraph of subsection (a), section 17, as follows:

THE FUNDS OF AN INTER VIVOS TRUST REVOCABLE BY THE
SETTLOR AND PROVIDING FOR THE PAYMENT OF THE PRINCIPAL
OF THE TRUST TO THE SETTLOR'S ESTATE AT HIS DEATH MAY
NOT BE INVESTED IN A COMMON TRUST FUND ESTABLISHED AND
MAINTAINED UNDER THIS SECTION.

Such a proposed amendment is being published in the Federal Register.

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

Item No. 2
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ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

November 28, 1960.



Mr. Hugh J. Helmer, Vice President,
Federal Reserve Bank of Chicago,
Chicago 90, Illinois.

Dear Mr. Helmer:

In accordance with the request contained in your letter of November 16, 1960, the Board approves the appointment of Roger E. Schultz, at present an assistant examiner, as an examiner for the Federal Reserve Bank of Chicago. Please advise if the appointment is not made effective on January 2, 1961, as planned.

Very truly yours,

(Signed) Kenneth A. Kenyon

Kenneth A. Kenyon,
Assistant Secretary.