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Minutes for February 27, 1961

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

Minutes of the Board of Governors of the Federal Reserve System on Monday, February 27, 1961. The Board met in the Board Room at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Balderston, Vice Chairman
Mr. Szymczak 1/
Mr. Mills
Mr. Robertson
Mr. Shepardson
Mr. King

Mr. Sherman, Secretary
Mr. Kenyon, Assistant Secretary
Mr. Fauver, Assistant to the Board
Mr. Hackley, General Counsel
Mr. Noyes, Director, Division of Research and Statistics
Mr. Farrell, Director, Division of Bank Operations
Mr. Masters, Associate Director, Division of Examinations
Mr. Hexter, Assistant General Counsel
Mr. Furth, Adviser, Division of International Finance
Mr. Daniels, Assistant Director, Division of Bank Operations
Mr. Nelson, Assistant Director, Division of Examinations
Mr. Goodman, Assistant Director, Division of Examinations
Mr. Landry, Assistant to the Secretary
Mr. Potter, Legal Assistant

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

	Item No.
Letter to Chase International Investment Corporation, New York City, extending to February 1, 1962, the time within which further investment may be made in Arcturus Investment & Development, Ltd., Montreal, Canada.	1

1/ Withdrew from meeting at point indicated in minutes.

	Item No.
Letter to Chase International Investment Corporation, New York City, granting consent to that Corporation and/or Arcturus Investment & Development, Ltd., to exercise an option to purchase not more than 5 per cent of the shares of B. F. Goodrich Iran S. A., Tehran, Iran.	2

With respect to Item No. 2, Governor Robertson raised a question concerning the indicated unwillingness of Chase International Investment Corporation to make a loan to B. F. Goodrich Iran S. A. unless it was given an option to acquire shares of the borrower. Mr. Furth replied that since loans to firms in less developed countries carry a certain risk, it is customary to seek to improve the return anticipated from them by providing for the possibility of a capital gain, which in this case would result should the shares of B. F. Goodrich Iran S. A. rise in value by an amount in excess of the option price. He noted that this was in keeping with the practice followed by the International Finance Corporation. Mr. Hexter pointed out that Regulation K contemplates that financing corporations may purchase stock whether or not any loan is made.

Messrs. Goodman and Furth then withdrew from the meeting.

Report on competitive factors (Chicago, Illinois). There had been distributed under date of February 21, 1961, copies of a draft of report to the Comptroller of the Currency on the competitive factors involved in the proposed merger of City National Bank and Trust Company, Chicago, Illinois, into Continental Illinois National Bank and Trust Company, also of Chicago.

Following a discussion during which certain changes were agreed upon, the report was approved unanimously in the form containing the following conclusion:

> The proposed merger of the second and sixth largest banks in the area would substantially lessen both existing and potential competition. As both banks serve similar clientele, the elimination of the smaller bank would remove an alternative source of competitive credit and deposit facilities as well as terminate its future capability for growth and enhanced competitive capacity. The competitive position of the applicant, already one of two dominant banks in the city, would be strengthened. As a consequence the preservation of effective competition in the area would be more difficult.

Applications of Liberty Bank of Buffalo (Item No. 3). There had been distributed under date of February 23, 1961, a memorandum from the Division of Examinations recommending, as had the Federal Reserve Bank of New York, approval of the merger of two banks (The National Bank of Fredonia, Fredonia, New York, and Erie County Trust Company, East Aurora, New York) into The Liberty Bank of Buffalo, Buffalo, New York, and the operation of branches by the resulting bank (Liberty Bank and Trust Company) at the present head office and one branch location of The National Bank of Fredonia and at the present head office location of Erie County Trust Company. The Comptroller of the Currency and the Federal Deposit Insurance Corporation had concluded in each instance that the proposed transaction would not have an adverse effect on competition. The Department of Justice stated, with respect to the proposed merger of The National Bank of Fredonia into The Liberty Bank of Buffalo, that the

addition of the relatively small resources of the former to those of the latter would not appear to affect banking competition adversely in the Buffalo service area. However, the entry of an additional large banking organization into the service area of the merging bank might endanger the ability of the remaining independent bank to compete effectively with branches of three much larger banking institutions. With respect to the proposed merger of Erie County Trust Company into The Liberty Bank of Buffalo, the Department stated that although the proposed merger would not appear to have a substantial impact on banking competition in the service area of the acquiring bank, in the service area of the merging bank the effect of the merger would be to replace an effective independent bank with a branch of a much larger institution to compete with a branch of the largest bank in western New York. This development, it was suggested, might add to the competitive handicaps of two smaller banks in nearby towns.

After consideration of all available information, including the basis for approval suggested by the Division of Examinations, a letter to The Liberty Bank of Buffalo consenting to the proposed mergers and approving the operation of branches incident to the mergers was approved unanimously. A copy of the letter is attached as Item No. 3.

Application of First Virginia Corporation (Item No. 4). At its meeting on February 23, 1961, the Board approved, with Governor King abstaining, an application by The First Virginia Corporation, Arlington,

Virginia, for prior approval, pursuant to section 3(a)(2) of the Bank Holding Company Act of 1956, of the acquisition of 4,080 or more shares of the 8,000 voting shares of Falls Church Bank, Falls Church, Virginia. Pursuant to the foregoing action, the staff was instructed to prepare for subsequent consideration by the Board drafts of an order and an accompanying statement. Reference had been made at the February 23 meeting to an agreement entered into between The First Virginia Corporation and the two principal officers of Falls Church Bank on October 11, 1960, relative to continuation of the services of those officers and lifetime payments to them and their widows. The officers were to exert "their best efforts to obtain offers from other stockholders of Bank to sell their shares to First Virginia if requested so to do by First Virginia...". It was understood at the February 23 meeting that a study would be made by the staff as to whether bank holding companies should be put on notice that in the future the Board would require evidence of full disclosure of such agreements to all stockholders.

Governor Robertson said that since last Thursday's meeting he had reviewed the agreement in question. This agreement called for First Virginia to vote its controlling shares of stock (assuming Board approval of its application) to provide among other things for retention of the two officers as consultants to the bank on a salary basis for the remainder of their lives regardless of any physical disability that they might be suffering at the time, and also for specified monthly payments

to their widows. Governor Robertson noted that if existence of the contracts with these men had been made known to the other stockholders of Falls Church Bank, he would have had no objection to the agreement. On the other hand, since the file on this matter did not show whether there had been such disclosure, he thought it desirable to ask First Virginia to clarify the point. He believed the Board would be placed in an awkward position should it announce approval of the application without having this information in hand.

There ensued a discussion as to the alternative courses of action the Board might pursue should First Virginia Corporation state that the agreement had not been disclosed to other stockholders of the bank. It was pointed out by Mr. Hexter that if the Board were informed by First Virginia that there had been no disclosure of the agreement, it could, if it felt strongly enough, reverse its position and turn down the application on that basis and in the light of such other considerations as might be deemed pertinent. If the Board saw fit to let its approval of the application stand, nevertheless it could, if it so desired, bring out in its statement on the matter that despite the undisclosed agreement the benefits to be derived from acquisition by the holding company of the stock of the Falls Church Bank were regarded as sufficient to justify approval of the application.

In this connection Governor Szymczak pointed out that the application had been approved by the Board on February 23 and the staff

had been requested to prepare drafts of an order and statement reflecting such approval. This action had been taken with the understanding that in order to determine what policy should be followed in future cases, the Board's staff would study the question of requiring full disclosure. It was understood that the staff's recommendations would be presented for the Board's consideration, and that the Board would then decide whether all bank holding companies should be put on notice.

Governor Mills expressed the opinion that on the basis stated by Governor Szymczak the Board might with some reason let its favorable decision on the current application stand. As Governor Szymczak had pointed out, such a procedure would contemplate that the Board would follow through on the general problem to determine whether, with respect to future applications, all bank holding companies should in some manner be put on notice that applications would be subject to criticism unless there was full disclosure to shareholders of any agreements entered into by the holding company in connection with its approach to the bank proposed to be acquired.

In response to a question, Mr. Hackley noted that the fundamental question was whether lack of disclosure was a relevant consideration in reaching a decision on the current application. He felt that it might be so construed if in the Board's judgment the approach followed by First Virginia Corporation was such as to reflect on the integrity or ethics of the management of the holding company. However, since this

would involve questioning the integrity of the management, it seemed to him that the Board would want to be sure that it was on fairly sound ground. A denial of the application on the basis of lack of full disclosure might, of course, be attacked by First Virginia as improper. Without seeming to condone the transaction in question, he felt that it would be desirable to think the matter through carefully in the light of practices followed by holding companies generally, and perhaps by banks involved in merger transactions, in giving indications of continued employment of the principal officers or shareholders of banks sought to be acquired. It might be difficult to draw lines of distinction between such practices and the agreement entered into in the instant case.

After further discussion, the suggestion was made that it should be possible to find out quickly from First Virginia Corporation whether there was any legal or practical necessity for consummation of the proposed acquisition of shares of the Falls Church Bank by the end of this month. It was further suggested that it should be possible to obtain from First Virginia Corporation without too much delay a letter which would clarify whether the existence and terms of the agreement entered into between First Virginia and the two officers of the Falls Church Bank had been disclosed to the other shareholders of the bank.

It was agreed to proceed in such manner, with the understanding that the drafts of order and accompanying statement carrying out the decision reached on the First Virginia case at the February 23 meeting

would be submitted to the Board promptly for consideration in the light of such additional information as might be obtained from the applicant holding company.

Secretary's Note: A copy of the letter sent to The First Virginia Corporation pursuant to this action is attached as Item No. 4.

Messrs. Fauver, Masters, Hexter, Nelson, and Potter then withdrew from the meeting.

Fixed asset and depreciation accounting at Federal Reserve Banks. A memorandum from the Division of Bank Operations dated January 13, 1961, had been distributed to the Board on the subject of fixed asset and depreciation accounting at the Federal Reserve Banks. Reference was made in the memorandum to the studies and discussions engaged in during the past year and a half by the Board, its staff, the Presidents' Conference, and Price Waterhouse & Co., with regard to depreciation on buildings and fixed machinery and equipment at the Banks and related accounting procedures. Attachments included a memorandum summarizing the steps taken in consideration of the matter and a letter dated December 7, 1960, from Price Waterhouse responding to the Board's October 20 request for comment on the August 19, 1960, proposal of the Committee on Collections and Accounting of the Presidents' Conference, which had been approved by the Presidents and discussed with the Board at the joint meeting on September 13. According to this proposal, the annual depreciation rate would be reduced from 2 to 1-1/2 per cent on buildings and from 10 to 5 per cent on fixed machinery

and equipment. Also, supplementary fixed machinery and equipment accounts would be established. The December 7 letter from Price Waterhouse (1) reiterated the accounting firm's earlier opinion that if the net book value of Reserve Bank properties was not brought into line with the useful life of such properties by revaluations, anything else that might or might not be done with respect to property accounting would be of little consequence; (2) stated that by and large all of the formal proposals that had emerged from discussions of this matter had outlined acceptable methods of accounting for Reserve Bank property; and (3) suggested that if the most recent proposal were adopted it would be desirable, in lieu of establishing supplementary fixed machinery and equipment accounts, to segregate property additions by year of acquisition or to establish some similar procedure so that depreciation would not be recorded on fixed machinery and equipment over a period of less than 20 years. The Division of Bank Operations submitted with its memorandum of January 13 a draft of letter to the Presidents of the Reserve Banks that would state that the Board had authorized the Division to revise existing Accounting Manual instructions "along the lines" of the recommendations approved by the Presidents and the suggestion of Price Waterhouse.

At the request of the Chairman, Mr. Farrell reviewed the several steps in the recent consideration of the question of fixed asset and depreciation accounting, noting in his remarks that the history of the subject went back to discussion of reserves for contingencies of the

Reserve Banks in 1959, at which time question was raised whether the Reserve Banks needed to continue charging depreciation. He recalled that the Subcommittee on Accounting of the Conference of Presidents rendered an initial report on the subject in November 1959 and that Mr. Theodore Herz of Price Waterhouse & Co. reported orally on the subject at a meeting of the Board on December 17, 1959. Subsequently, Mr. Farrell said, the subject was reassigned to the Subcommittee on Accounting, and the Board authorized the Division of Bank Operations to work with Price Waterhouse & Co. in developing new procedures. There followed a letter report from Price Waterhouse, a proposal by the Subcommittee on Accounting, a compromise proposal by Mr. Farrell, and finally the proposal of the Committee on Collections and Accounting.

It was evident, Mr. Farrell said, that Price Waterhouse attached central significance to the view that if the net book value of Reserve Bank properties was not brought into line with the useful life of such properties through revaluation, proposals such as those which had emerged from consideration of this matter by the Conference of Presidents would not be of great consequence. However, the Reserve Bank Presidents were unanimously opposed to revaluations of this kind, particularly because in most instances this apparently would result in the writing up of assets. Accordingly, the recommendations made by the Committee on Collections and Accounting were viewed rather passively by Price Waterhouse.

There followed a discussion based on comments by Mr. Farrell concerning the principal features of the proposal of the Committee on Collections and Accounting, along with the effects of revising the accounting procedures along those lines. In this connection, comments were made on the reasons that might be cited for and against reducing the current depreciation rates on buildings and on fixed machinery and equipment, including the effect of such a change on the payments made by the Federal Reserve Banks to the Treasury. In response to questions, Mr. Farrell and Mr. Daniels indicated that the Division of Bank Operations had no strong feeling for or against adoption of the recommendations of the Committee on Collections and Accounting. They pointed out, however, that the adoption of such recommendations would not accomplish too much in the way of simplification of accounting procedures, which was an original objective of the study of fixed asset and depreciation accounting at the Federal Reserve Banks. They expressed agreement with the suggestion of Price Waterhouse that, if the Committee proposal were adopted, it would be desirable, in lieu of establishing supplementary fixed machinery and equipment accounts, to segregate property additions by year of acquisition or to establish some similar procedure so that depreciation would not be recorded on fixed machinery and equipment over a period of less than 20 years. Further, if the Committee proposal should be adopted, they felt it would be desirable to provide some latitude for the Division of Bank Operations in revising the instructions contained in the Accounting Manual.

The question of the depreciation rates that would be most appropriate was believed to involve essentially a policy determination.

A lengthy discussion ensued, the essential question being whether the recommendations of the Committee on Collection and Accounting appeared to offer sufficient advantages, in comparison with current accounting procedures, to warrant making the changes incident to their adoption. Some of the members of the Board were inclined to the view that any advantages would be of such minor consequence that the Board would be warranted in making a decision to maintain the status quo. It was noted that the Board's records would reflect the fact that the accounting procedures had been the subject of exhaustive review, but that it had not been possible to achieve agreement within the System on any procedures substantially different from those currently in effect. Other members of the Board suggested that the amount of work that had gone into the review of accounting procedures might make a decision to maintain the status quo questionable. It was pointed out that although Price Waterhouse apparently was not enthusiastic about the current proposal, nevertheless the accounting firm had indicated that in general the procedures recommended by the Committee on Collections and Accounting would involve acceptable methods of accounting for the property of the Reserve Banks. In the circumstances, and since the current proposal appeared to introduce some improvements, even though modest in nature, these members of the Board felt that there was something to be said for accepting the proposal.

Question was raised regarding the possibility of further consultation by the Board with Price Waterhouse, but it was brought out that the views of the accounting firm appeared to be fairly evident and that it seemed doubtful whether much would be gained from additional discussion.

It was brought out that, having received the opinions of the accounting firm, the Reserve Banks, and its own staff, the determination of the instructions that should be included in the Accounting Manual was a matter within the Board's province. Thus, it was suggested, at this point the appropriate procedure might be for the Board to exert leadership in the determination of such procedures as in its judgment would be most satisfactory, rather than to attempt to effect a compromise of the various views that had been expressed. Question was raised whether the Division of Bank Operations, if it were making its own recommendations, as contrasted with endeavoring to reach a solution on a compromise basis, would propose procedures substantially along the lines suggested by Price Waterhouse, and Mr. Farrell indicated that he thought such would be the case.

Governor Mills then commented that before the Board took action with regard to the proposal of the Committee on Collections and Accounting, it might be desirable to request the Division of Bank Operations to submit to the Board for review a plan based essentially on the Price Waterhouse suggestions, and it was agreed that this would be done.

During the discussion of the foregoing topic Governor Szymczak withdrew from the meeting.

Negotiable time deposit certificates. Chairman Martin referred to inquiries he had received over the weekend concerning various aspects of the plan announced recently by several New York City banks to issue negotiable time deposit certificates to corporations and to make a market for those certificates.

In this connection, Governor Mills expressed the view that the banks were embarking on an inadvisable course. The issuance of the certificates appeared to him to be in conflict with the principle that should guide the maintenance of savings deposits; namely, that such deposits should represent funds attracted to a bank pending their use for some other form of investment. The New York City banks, he suggested, were offering an instrument that represented a participation in the whole complex of assets of the issuing bank. From the standpoint of bank supervision, as distinguished from such questions as might fall within the purview of the Securities and Exchange Commission, he noted that the time certificates were to be issued in large denominations, far in excess of the insurance provided by the Federal Deposit Insurance Corporation.

Chairman Martin said he had had in mind that the Board should discuss such considerations and that, if there was no objection, such a discussion would be held at tomorrow's meeting.

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

Foreign travel by Mr. Hersey. The Secretary was informed by Governor Shepardson that during the executive session the Board gave consideration to a memorandum dated February 23, 1961, from Mr. Marget, Director, Division of International Finance, recommending that Mr. Hersey, Adviser in that Division, be authorized to make a six-week trip to Europe for the purpose of attending a special meeting of economists of central banks to be held in Basle, Switzerland, March 11-13, 1961, in connection with the regular monthly meeting of the Bank for International Settlements and also for the purpose of visiting a number of the European central banks for discussion of matters of current interest with the economists of those banks. Governor Shepardson stated that the Board had approved Mr. Marget's recommendation. Also, the New York Reserve Bank had indicated its intention to have a member of its staff attend the meeting of central bank economists in Basle, and no objection was interposed by the Board.

The meeting then adjourned.

Secretary's Note: Pursuant to the recommendation contained in a memorandum from the Division of Examinations dated February 21, 1961, Governor Shepardson today approved on behalf of the Board the transfer of Jeannette Somlyo from the position of Clerk-Stenographer in the Division of Personnel Administration to the position of Stenographer in the Division of Examinations, with no change in her basic annual salary at the rate of $3,970, effective the date she assumes her new duties.

Secretary

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

Item No. 1
2/27/61

February 27, 1961

Chase International Investment Corporation,
18 Pine Street,
New York 5, New York.

Gentlemen:

Reference is made to your letter of January 20, 1961, transmitted through the Federal Reserve Bank of New York, regarding the Board's letters of February 21, 1957, February 19, 1958, February 2, 1959, and February 1, 1960, which authorized your Corporation, subject to various conditions, to make further investment in Arcturus Investment & Development, Ltd., Montreal, Canada (in form of stock or obligations), up to an amount which, with the existing investment, would not exceed US$7,500,000.

In accordance with your request and on the basis of the information furnished, the Board extends to February 1, 1962, the time within which such investment may be made.

Very truly yours,

(Signed) Elizabeth L. Carmichael

Elizabeth L. Carmichael,
Assistant Secretary.

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

Item No. 2
2/27/61

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

February 27, 1961

Chase International Investment Corporation,
18 Pine Street,
New York 5, New York.

Gentlemen:

In accordance with the request contained in your letter of December 7, 1960, transmitted through the Federal Reserve Bank of New York, and on the basis of the information furnished, the Board of Governors grants its consent for Chase International Investment Corporation ("CIIC") and/or Arcturus Investment & Development, Ltd. ("Arcturus"), Montreal, Canada, to exercise an option to purchase and hold not to exceed 5 per cent of the presently outstanding ordinary shares of B. F. Goodrich Iran S. A., Tehran, Iran, at a cost of approximately US$126,000, such consent to remain in effect until December 31, 1964.

It is requested that you furnish the Board of Governors through the Federal Reserve Bank of New York, pertinent details regarding the investment as outlined in condition numbered (1) of the general consent granted to your Corporation on January 20, 1960.

The Board's consent is granted upon condition that CIIC and Arcturus shall dispose of their holdings of stock of the Iranian company, as promptly as practicable, in the event that the Iranian company should at any time (1) engage in issuing, underwriting, selling or distributing securities in the United States; (2) engage in the general business of buying or selling goods, wares, merchandise, or commodities in the United States or transact any business in the United States except such as is incidental to its international or foreign business; or (3) conduct its operations in a manner which, in the judgment of the Board of Governors of the Federal Reserve System, is inconsistent with Section 25(a) of the Federal Reserve Act or regulations thereunder.

Very truly yours,

(Signed) Elizabeth L. Carmichael

Elizabeth L. Carmichael,
Assistant Secretary.

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

Item No. 3
2/27/61

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

February 27, 1961

Board of Directors,
The Liberty Bank of Buffalo,
424 Main Street,
Buffalo, New York.

Gentlemen:

The Board of Governors of the Federal Reserve System, after consideration of all factors set forth in section 18(c) of the Federal Deposit Insurance Act, hereby consents to merger of the Erie County Trust Company, East Aurora, New York, and merger of The National Bank of Fredonia, Fredonia, New York, into The Liberty Bank of Buffalo, under the charter of the latter bank and with a change of title to Liberty Bank and Trust Company upon merger of Erie County Trust Company, as such mergers are believed to be in the public interest.

The Board of Governors also approves the operation of branches by The Liberty Bank of Buffalo at the following locations:

East Aurora Branch, 670 Main Street, East Aurora, New York
Fredonia Branch, 2 West Main Street, Fredonia, New York
Brocton Branch, 1 West Main Street, Brocton, New York

This approval is given provided the transactions are consummated within six months from the date of this letter substantially in accordance with the Plans of Merger submitted with the applications, and shares of stock acquired from dissenting shareholders are disposed of within three months of acquisition.

Very truly yours,

(Signed) Elizabeth L. Carmichael

Elizabeth L. Carmichael,
Assistant Secretary.

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

Item No. 4
2/27/61

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

February 27, 1961

Mr. Edwin T. Holland, President,
The First Virginia Corporation,
2924 Columbia Pike,
Arlington 4, Virginia.

Dear Mr. Holland:

In connection with your Corporation's application for approval of the acquisition of shares of Falls Church Bank, the Board has given consideration to the agreement entered into on October 11, 1960, between the Corporation and Messrs. Shreve and Walker (Exhibit C(4)).

The Corporation is requested to supplement the information heretofore submitted by advising the Board whether the existence of this agreement, and its terms, have been disclosed to the present shareholders of Falls Church Bank. The Board also requests to be advised as to the nature of any negotiations that have taken place with said shareholders relating to the sale of their stock to the Corporation, as well as any arrangements in the nature of options to purchase, escrow agreements, or the like, that have been entered into with them. Needless to say, the Board would welcome any additional information or comments that would contribute to its full understanding of this matter.

Upon receipt of this information, it is hoped that the application can be acted upon promptly.

Very truly yours,

Merritt Sherman,
Secretary.