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Minutes for September 25, 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.

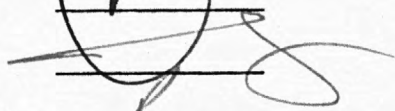
It is not proposed to include a statement with respect to any of the entries in this set of minutes in the record of policy actions required to be maintained pursuant to section 10 of the Federal Reserve Act.

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.

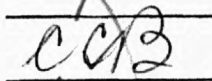
Chm. Martin



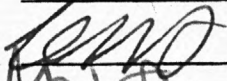
Gov. Mills



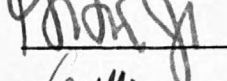
Gov. Robertson



Gov. Balderston



Gov. Shepardson



Gov. King



Gov. Mitchell

Minutes of the Board of Governors of the Federal Reserve System on
Monday, September 25, 1961. The Board met in the Board Room at 10:00 a.m.

PRESENT: Mr. Balderston, Vice Chairman
Mr. Mills
Mr. Robertson
Mr. Shepardson
Mr. King

Mr. Sherman, Secretary
Mr. Hackley, General Counsel
Mr. Solomon, Director, Division of Examinations
Mr. Hexter, Assistant General Counsel
Mr. Leavitt, Assistant Director, Division of
Examinations
Mr. Landry, Assistant to the Secretary
Mr. Fuerth, Legal Assistant

Letter to Massachusetts Commissioner of Banks (Item No. 1).

Under date of September 13, 1961, a letter was received from the Commissioner of Banks, Commonwealth of Massachusetts, inquiring as to the Board's views on what would be appropriate with respect to the size of premiums offered to stockholders of merged banks. Copies of a draft reply indicated that, although in the discharge of its responsibilities under the bank merger legislation of 1960 the amount of premium offered to stockholders was considered to be a relevant fact, the Board had not found it necessary to decide what would be a proper or improper premium.

After discussion during which certain suggestions for modification of the draft reply were made and agreed upon, the letter to the Commissioner of Banks, Commonwealth of Massachusetts, was approved in the form of attached Item No. 1.

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Midyear dividends in excess of net profits (Item No. 2). Copies had been distributed of a memorandum from the Legal Division dated September 19, 1961, attaching a draft of letter to the Federal Reserve Bank of San Francisco in response to its letters of July 18 and August 1, 1961, relating to the First State Bank of Salina, Salina, Utah, a member State bank that on June 22, 1961, declared a dividend of \$22,500 without prior approval of the Board of Governors. The Reserve Bank had inquired whether the dividend declaration violated section 5199(b) of the Revised Statutes, made applicable to member State banks by the sixth paragraph of section 9 of the Federal Reserve Act. Section 5199(b), in effect, provides that

"The approval of the Comptroller of the Currency ^{or the Board of Governors} shall be required if the total of all dividends declared by...^{a national bank or a member State bank} in any calendar year shall exceed the total of its net profits of that year combined with its retained net profits of the preceding two years...."

In the case under consideration the amount of the dividend exceeded the total of the bank's net profits in 1961 up to the date of the dividend declaration, combined with its retained net profits of the preceding two years, which were negative figures. The General Counsel for the Reserve Bank had expressed the view in an opinion dated July 24, 1961, a copy of which was transmitted with the Reserve Bank's letter of August 1, that since section 5199(b) referred to "all dividends declared...in any calendar year" its applicability could not be determined until the

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calendar year was completed, and for that reason it was believed that no violation of the statute had occurred. However, the Legal Division took the position that such an interpretation would substantially defeat the purpose of the statute as revealed by its legislative history. Consequently, the Division recommended in its memorandum that the statutory provisions be construed as relating to dividends declared, and to net profits, in the calendar year up to the date of such declaration and that First State Bank of Salina be considered to have violated the statute. It was the further recommendation of the Legal Division that, should the Board concur in this view, the substance of this interpretation be published in the Federal Register and the Federal Reserve Bulletin. The proposed reply to the Reserve Bank would express the views indicated.

At the request of Governor Balderston, Mr. Hexter commented on the memorandum of the Legal Division, noting that both the Division of Examinations and the Legal Division felt that the purpose of the statute would be lost to a large extent if the narrow interpretation thereof made by Counsel for the Reserve Bank were adopted. He observed that the position recommended by the Legal Division had already been adopted by the Comptroller of the Currency and that it seemed clear this interpretation carried out the intent of Congress.

Mr. Molony, Assistant to the Board, joined the meeting at this point.

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Governor Mills inquired as to the procedure contemplated for handling the case in question, where there had been a violation of the statute according to the Legal Division interpretation, with which he agreed.

Mr. Hexter replied to the effect that the attention of the San Francisco Reserve Bank had been drawn to the problem under discussion in connection with inspection of the most recent report of examination of First State Bank of Salina and subsequent inspection of the bank's report of income and dividends for the six months' period ended June 30, 1961. Since the language of the statute could be interpreted as had been done by the Reserve Bank, it was suggested that under the circumstances the best course to pursue would be for the Reserve Bank to make clear to First State Bank of Salina and to other banks that the statute applied to dividends declared for the first half of the year. Caution against a recurrence would be given to the member bank by drawing attention to the interpretation contained in the proposed letter to the Reserve Bank that would be published in the Federal Register and the Federal Reserve Bulletin, should the Board approve the recommendations of the Legal Division in this regard.

After further discussion during which it was indicated that all members of the Board present favored the recommendations of the Legal Division, as well as the procedure suggested for handling the violation in question, the letter to the Federal Reserve Bank of San Francisco

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concerning dividend payments made by the First Bank of Salina was approved unanimously, with the understanding that the substance of the interpretation contained therein would be published in the Federal Register and the Federal Reserve Bulletin. A copy of the letter, as sent, is attached as Item No. 2.

Eligibility for service as Class A director (Item No. 3). On September 22, 1961, a telegram had been received from the Federal Reserve Bank of San Francisco advising that Mr. John A. Schoonover, a Class A director of the Reserve Bank, had resigned effective September 14, 1961, from his official position with a member bank, remaining, however, as a director of that bank, with plans to continue as director of the Reserve Bank to the expiration of his term on December 31, 1961. The view was expressed in the telegram that because of the short time of Mr. Schoonover's remaining term as director of the Reserve Bank, no objection was seen to his continuance in this capacity through December 31, 1961. A proposed telegram to the Reserve Bank would indicate that there was no objection to Mr. Schoonover's continuing to serve as a Class A director for the remainder of his term.

Following a brief discussion, a telegram was approved unanimously for transmission to the Federal Reserve Bank of San Francisco in the form of attached Item No. 3.

Request from Congressman Patman (Item No. 4). Governor Balderston referred to receipt of a letter from Congressman Patman dated September 22, 1961, requesting a list of all bank merger applications pending before the

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Board. Although no such list had been published by the Board, it was noted that the information sought could not be regarded as confidential, since it was available to the public at least in newspapers published in the communities where the head offices of applicants were located, as required by law. In this connection, reference was made to the fact that the Board publishes in the Federal Register notice of receipt of applications filed under the provisions of the Bank Holding Company Act of 1956.

Following a discussion, there was agreement with a suggestion that Mr. Patman be provided with the information asked for. A copy of the letter transmitting the list of merger applications pending before the Board is attached as Item No. 4.

A discussion then ensued regarding the advisability of making public on a periodic basis notice of applications received by the Board under the Bank Merger Act of 1960. At the conclusion of the discussion, it was agreed that such information would hereafter be made available periodically in a release distributed to the public.

Mr. Fauver, Assistant to the Board, joined the meeting during the foregoing discussion.

Further request from Congressman Patman. Governor Balderston noted receipt of another letter from Congressman Patman dated September 23, 1961, requesting an updating of data and provision of certain additional items in a tabulation captioned "Decreases in Number of Commercial Banks

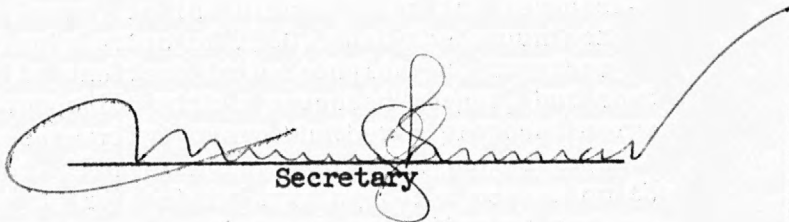
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Because of Consolidations and Absorptions," which appeared as Table 4 on page 27 of an interim report of the Antitrust Subcommittee of the House of Representatives entitled "Corporate and Bank Mergers" published in 1955. Governor Balderston said that Mr. Patman had also requested a breakdown for 1960 and 1961 to date showing how many bank mergers had been approved by each of the Federal bank supervisory agencies and in each instance the dollar volume of deposits and the percentage of total deposits of all commercial banks involved.

After a discussion of the advisability of furnishing some of the requested data to Mr. Patman, it was understood that the staff would undertake to compile such of the material as was available for transmission to Congressman Patman.

The meeting then adjourned.


Secretary

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

Item No. 1
9/25/61

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD



September 25, 1961

Mr. Edward A. Counihan, III,
Commissioner of Banks,
The Commonwealth of Massachusetts,
150 Causeway Street,
Boston 14, Massachusetts.

Dear Mr. Counihan:

This refers to your letter of September 13, 1961, regarding the amounts of premiums offered to the stockholders of merged banks.

As you know, the dollar amount of premiums can be calculated on several different bases such as book values, market values, or some adjustments of these; the premium so calculated can then be stated as a per cent of deposits (or certain kinds of deposits), of earnings, or of one of the bases used to compute the premium. The significance of one comparison or another can vary depending on the circumstances, and it is often difficult to make appropriate comparisons of premiums from one situation to another.

It has seemed to the Board, in the discharge of its responsibilities under the bank merger legislation of 1960, that the amount of premium offered to stockholders is one fact to be considered, together with other relevant facts, in connection with a proposed merger, but that the size of premium would not necessarily govern whether a proposed merger should be approved or disapproved. For example, a premium judged to be large would seem to raise doubts as to a claim arguing for a merger on the grounds that the bank being absorbed was in distress or suffering seriously from problems of management, management succession, or the like. Conversely, a small premium or a discount would somewhat tend to support such a claim.

In the circumstances, the Board has not yet found it necessary to decide what would be a proper or improper premium, nor has it seemed feasible to develop meaningful statistics regarding premiums involved in mergers.

Very truly yours,

Merritt Sherman,
Secretary.



BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM Item No. 2
WASHINGTON 25, D. C. 9/25/61

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

September 25, 1961

Mr. E. H. Galvin, Vice President,
Federal Reserve Bank of San Francisco,
San Francisco 20, California.

Dear Mr. Galvin:

This is in response to your letters of July 18, 1961 and August 1, 1961, relating to the First State Bank of Salina, Salina, Utah. On June 22, 1961 this member bank declared a dividend of \$22,500 without having obtained the approval of the Board of Governors. You inquire whether this action violated Revised Statutes section 5199(b) (12 U.S.C. 60) and the sixth paragraph of section 9 of the Federal Reserve Act (12 U.S.C. 324), which, in effect, provide that

"The approval of the Comptroller of the Currency [or the Board of Governors] shall be required if the total of all dividends declared by... [a national bank or a member State bank] in any calendar year shall exceed the total of its net profits of that year combined with its retained net profits of the preceding two years...."

In this case, the amount of the dividend exceeded the total of the bank's net profits in 1961, up to the date of the declaration, combined with its retained net profits of the preceding two years (which were negative figures).

If the question related only to the literal meaning of words, divorced from the statute's underlying purpose and from the factual situations to which it relates, it might be contended that, since the statute refers to "all dividends declared...in any calendar year" and "the total of its net profits of that year", its applicability cannot be determined until the calendar year is completed. As explained below, however, such an interpretation is not required by the language of the statute and would substantially defeat its purpose, as revealed by the legislative history; and consequently it is believed that the statute should be construed as relating to dividends declared, and to net profits, in the calendar year up to the date of such declaration.

The purpose of the statute was described as follows by the Senate Banking Committee:

Mr. E. H. Galvin

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"This provision is designed to restrict the payment of dividends...where such payments would result in dissipating needed capital funds. This provision strengthens the regulatory authority of the Comptroller [and the Board of Governors]. Under it, he will be able to prevent the declaration of dividends which are not justified by current and recent accumulated earnings, and which would result in a weakened and under-capitalized bank and violate safe and sound banking practice." S. Rep. No. 730, 86th Cong. (Aug. 19, 1959), pp. 6-7.

It seems that Congress had in mind the following test: At the time the dividend is declared, does the bank have available, from profits of the current calendar year and the two preceding calendar years, enough profits to cover the dividend? If not, the dividend may not be declared and paid unless the Comptroller or the Board of Governors specifically approves, in view of the circumstances of the particular case.

Bearing in mind the Senate Committee's reference to "dissipating needed capital funds", it is obvious that the danger that a proposed dividend would unduly weaken a bank's capital structure is just as great if the dividend is declared in June as if it is declared in December. If a bank does not have profits on hand sufficient to cover a proposed dividend, the fact that the declaration is made in one month rather than in another has little or no bearing on the extent to which payment of the dividend may unduly diminish the capital "cushion" on which depend the bank's continued existence and the safety of its depositors.

An illustration may be helpful. For simplicity, let us assume that a member State bank opened for business on January 1, 1959 with a capital structure of \$300,000, as required by the supervisory authorities. The bank had no net profit in 1959 or 1960. Up to June 30, 1961 it still has no net profits, but nevertheless the directors declare a dividend of \$20,000 on that date. The bank's capital structure is thereby reduced from \$300,000 to \$280,000. It seems that this was precisely what Congress intended should not happen unless the Board of Governors approved the dividend, for adequate reasons. An undesirable situation would exist, and the Congressional purpose would be defeated, if such a weakening of the bank's capital structure were permissible if the dividend was declared and paid (without supervisory approval) in June, whereas the same action would involve a violation of the statute if the dividend was declared and paid, instead, in December. This might actually mean that no violation of section 5199(b) could occur except with respect to end-of-year dividends - unless, perhaps, it could be established that the bank's directors, when they declared the dividend earlier in the year, knew (or had reason to believe) that the bank's net profits for the entire year would not be sufficient.

Mr. E. H. Galvin

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The statutory reference to "all dividends declared...in any calendar year" can be interpreted, even from the viewpoint of literal meaning, as referring to dividends declared in a calendar year up to the date of declaration. Particularly because the clear Congressional purpose would otherwise be largely defeated, it is concluded that this is the correct interpretation and that, consequently, the declaration by First State Bank of Salina on June 22, 1961, without the Board's approval, of a dividend in the amount of \$22,500 was in violation of the applicable statutes, since the amount of that dividend exceeded "the total of [the bank's] net profits of that year combined with its retained net profits of the preceding two years."

Very truly yours,

(Signed) Merritt ShermanMerritt Sherman,
Secretary.

Item No. 3
9/25/61**TELEGRAM**
LEASED WIRE SERVICEBOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON

September 25, 1961.

Swan - San Francisco

Re your wire September 22, 1961, no objection to Mr. Schoonover continuing to serve as Class A director for remainder of term. For your information, Board has heretofore taken position that Class A director continues to be "representative of the stockholding banks" where he continues as director of member bank even though without official position.

(Signed) Merritt Sherman

Sherman

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

Item No. 4
9/25/61

OFFICE OF THE VICE CHAIRMAN

September 25, 1961

The Honorable Wright Patman,
House of Representatives,
Washington 25, D. C.

Dear Mr. Patman:

In accordance with your request of September 22, 1961, there is enclosed a list of bank merger applications pending before the Board of Governors. This list contains the names of the banks involved, the type of action for which permission has been requested (i.e., merger, consolidation, purchase of assets, etc.), and the date on which the application was received by the Board.

Sincerely yours,

(Signed) C. Canby Balderston

C. Canby Balderston,
Vice Chairman.

Enclosure.

APPLICATIONS PENDING BEFORE THE BOARD OF
GOVERNORS OF THE FEDERAL RESERVE SYSTEM UNDER SECTION
18(c) OF THE FEDERAL DEPOSIT INSURANCE ACT AS AMENDED

September 25, 1961

NAMES OF BANKS INVOLVED	TYPE OF ACTION	DATE APPLICATION RECEIVED BY BOARD
1. United California Bank, Los Angeles, California, and The Southwest Bank, Inglewood, California.	Merger	May 2, 1961
2. Wells Fargo Bank American Trust Company, San Francisco, California, and The Farmers and Merchants National Bank of Santa Cruz, Santa Cruz, California.	Merger	June 2, 1961
3. Elston Bank & Trust Company, Crawfordsville, Indiana, and The Waynetown State Bank, Waynetown, Indiana.	Purchase of assets, etc.	July 13, 1961
4. United California Bank, Los Angeles, California, and The First National Bank, La Verne, California.	Merger	July 17, 1961
5. Liberty Bank and Trust Company, Buffalo, New York, and Exchange Bank, Oakfield, New York.	Merger	July 25, 1961
6. The Fifth Third Union Trust Company, Cincinnati, Ohio, and Norwood-Hyde Park Bank and Trust Company, Norwood, Ohio.	Purchase of assets, etc.	July 25, 1961

September 25, 1961

NAMES OF BANKS INVOLVED	TYPE OF ACTION	DATE APPLICATION RECEIVED BY BOARD
7. Farmers State Bank of Alto, Alto, Michigan, and The Edwin Nash State Bank, Clarksville, Michigan.	Consolidation	July 31, 1961
8. Chemical Bank New York Trust Company, New York, New York, and Long Island Trust Company, Garden City, New York.	Merger	August 3, 1961
9. The Chase Manhattan Bank, New York, New York, and Hempstead Bank, Hempstead, Long Island, New York.	Merger	August 28, 1961
10. The Hackensack Trust Company, Hackensack, New Jersey, and The Bank of Saddle Brook & Lodi, Saddle Brook, New Jersey.	Merger	September 8, 1961
11. The Elyria Savings and Trust Company, Elyria, Ohio, and The First Wellington Bank, Wellington, Ohio.	Consolidation	September 19, 1961