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, May 14, 1962. The Board met in the Board Room at 10:00 a.m.

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

         Mr. Sherman, Secretary
         Mr. Kenyon, Assistant Secretary
         Mr. Young, Adviser to the Board and Director,
            Division of International Finance
         Mr. Molony, Assistant to the Board
         Mr. Hackley, General Counsel
         Mr. Noyes, Director, Division of Research
            and Statistics
         Mr. Farrell, Director, Division of Bank
            Operations
         Mr. Solomon, Director, Division of Examinations
         Mr. Chase, Assistant General Counsel
         Mr. Shay, Assistant General Counsel
         Mr. Hooff, Assistant General Counsel
         Mr. Dembitz, Associate Adviser, Division of
            Research and Statistics
         Mr. Conkling, Assistant Director, Division
            of Bank Operations
         Mr. Benner, Assistant Director, Division of
            Examinations
         Mr. Young, Senior Attorney, Legal Division

Independent Bankers Association. Governor Balderston referred
to a letter dated May 8, 1962, from the Chairman of the Government
Fiscal Policy Committee of the Independent Bankers Association indicating
that the Committee expected to meet with representatives of the Treasury
on June 26, 1962, and inquiring whether a visit to the Board could be
arranged on June 25.

1/ Withdrew from meeting at point indicated in minutes.
After discussion, it was agreed that an invitation should be extended to the group to visit the Board's offices on the date indicated, with the understanding that in working out the details of the program—including the question whether a luncheon should be arranged—advice would be sought from the Treasury concerning the status of this group in comparison with the committees of the American Bankers Association and the Investment Bankers Association that meet with the Treasury periodically.

Circulated or distributed items. The following items, which had been circulated or distributed to the Board and copies of which are attached under the respective numbers indicated, were approved unanimously:

Letters to Central National Bank of Chicago and Exchange National Bank of Chicago, both of Chicago, Illinois, denying their applications to maintain reduced reserves.

Letter to the Administrator of the Farmers Home Administration, Washington, D. C., regarding whether promissory notes evidencing loans by member banks to farmers which are insured by the Farmers Home Administration are eligible as security for advances to member banks by Federal Reserve Banks under section 13 of the Federal Reserve Act.

In connection with Items 1 and 2, question was raised by Governor Mitchell as to why recommendations had been made by the Board of Directors of the Chicago Reserve Bank and whether this procedure was appropriate in the case of requests for permission to carry reduced reserves. It was pointed out by the staff that it had been customary
for such requests by member banks in the Chicago area to be forwarded to the Board of Governors with a recommendation of the Chicago directors. In the case of Central National Bank, the recommendation of the directors had originally been favorable. However, in view of changed circumstances, including a merger involving the bank, the matter was referred back to the Reserve Bank following discussion at the Board meeting on March 8, 1962, and the directors had now recommended unfavorably. It was further pointed out that in certain other Districts it was customary for such matters to be forwarded to the Board with a recommendation of the Reserve Bank officers, as contrasted with the directors. The lack of procedural uniformity with respect to the submission of recommendations on matters in the bank supervisory field had been discussed by the Board several years ago, but no decision was made at that time to press for uniformity of procedure.

The discussion of these items also raised a question with respect to the status of the Board's study of the classification of cities for reserve purposes, and Governor Balderston indicated that he understood Chairman Martin was endeavoring to arrange a meeting with at least one member of the Senate who had expressed interest. A view was stated that the Board should give further consideration to the subject following the Chairman's return.

With respect to Item No. 3, agreement was expressed with a suggestion by Mr. Hackley that the letter to the Farmers Home
Administration be made the subject of an "S" letter to all Federal Reserve Banks and that an interpretation be published in the Federal Reserve Bulletin. There was also agreement with his suggestion that the published interpretation should include language differentiating this case from the interpretation, published in 1960, wherein certain Government insured Merchant Marine Bonds were held not to be eligible as security for advances by Federal Reserve Banks under section 13 of the Federal Reserve Act.

Mr. Young (Senior Attorney) then withdrew from the meeting.

Certificates of deposit. Pursuant to the request at the Board meeting on January 15, 1962, there had been distributed a memorandum from Messrs. Dembitz, Benner, and Chase dated April 13, 1962, discussing developments with regard to two kinds of interest-bearing certificates of deposit now being issued by commercial banks: (1) the shorter-term negotiable certificates that some banks had been issuing in large denominations during the past year or so; and (2) certificates with maturities of five years or more that specified in advance the basis on which interest would be paid or credited over the life of the certificate.

There had also been distributed a draft of reply to a letter dated April 25, 1962, in which the Comptroller of the Currency called attention to the practice recently instituted by some banks of advertising and selling long-term, low-denomination certificates of deposit and
presented the questions: (1) whether a bank was misleading the public when it advertised those deposits as carrying a "guaranteed" rate of interest; and (2) whether it was prudent banking practice for a bank to commit itself to the payment of a fixed rate of interest on deposits for terms running as long as 20 years.

The Comptroller's letter and the proposed reply drew attention to section 217.3(b) of Regulation Q, Payment of Interest on Deposits, which states that "no certificate of deposit or other contract shall be renewed or extended unless it be modified to conform to the provisions of this part, and every member bank shall take such action as may be necessary, as soon as possible consistently with its contractual obligations, to bring all of its outstanding certificates of deposit or other contracts into conformity with the provisions of this part."

Literally, this provision might be read as permitting a member bank that had contracted to pay a certain rate of interest on a long-term certificate to continue to pay that rate, even though it exceeded the maximum rate prescribed by the Board. The proposed reply pointed out, however, that this was not the intent. As long ago as 1933 the Board had suggested in a published statement that member banks stamp on each time certificate a provision indicating that the rate of interest payable thereon was subject to change to such extent as might be necessary to comply with requirements of the Federal Reserve Board made from time to time pursuant to the Federal Reserve Act. Accordingly, the proposed
letter to the Comptroller would state that any certificate containing
a so-called guaranteed rate of interest should provide in clear and
precise language that the interest rate was subject to reduction if
the Board should reduce the maximum rate of interest that might be
paid on such a deposit.

In regard to the second question presented by the Comptroller,
the proposed reply would state reasons why it was not believed that it
could be established categorically that a bank's commitment to pay a
fixed rate of interest for a long term of years was necessarily
imprudent banking.

In a general discussion of the staff memorandum, the Comptroller's
letter, and the proposed reply, interest centered principally on the
aforementioned provision of Regulation Q that might seem to suggest,
on literal reading, that a member bank could continue to pay a rate
of interest on a long-term certificate of deposit in excess of a maximum
rate subsequently established by the Board. Question was raised whether
it would not be desirable to consider an amendment to Regulation Q
specifying, so as to remove any doubt, that the rate of interest agreed
to be paid by member banks under their deposit contracts would be
reduced, if necessary, to comply with maximum permissible interest rates
prescribed by the Board. Accordingly, it was understood that the staff
would study this possibility, with a view to further consideration of
the matter by the Board at another meeting, at which time the Board
would also consider, in the light of such decision as might be reached in this regard, what type of reply should be made to the Comptroller of the Currency.

Messrs. Farrell, Chase, Shay, Hooff, Conkling, Dembitz, and Benner then withdrew.

Buffalo Branch director. There had been distributed a memorandum from Mr. Sherman dated May 11, 1962, reporting a question raised by the Federal Reserve Bank of New York as to the Board's probable reaction in the event Mr. Raymond E. Olson, Chairman of the Board of the Buffalo Branch, were to accept a directorship with the Lincoln Rochester Trust Company, Rochester, New York. Mr. Olson would have completed six years' service as a director of the branch at the end of 1962. The specific question was whether the Board would object to his continuing as a director of the Buffalo Branch until the end of the present year if he became a director of the member bank in the near future.

Initial expressions by some of the members of the Board were to the effect that they would prefer that Mr. Olson not serve at the same time as a director of the Buffalo Branch and a director of a member bank. In the discussion, however, it was brought out that on certain occasions in the past the Board had permitted branch directors to continue as such for relatively brief periods after they became directors of member banks. It was further pointed out that the Board's branch regulations went no further than to state that it was preferable that
Board-appointed branch directors not be directors of banks. Within the past year or so, the Board had considered whether the branch regulations should be changed to prohibit a Board-appointed branch director from being also a director of a bank, but the change was not made.

It was then suggested that an expression of view on the Olson case be deferred pending the distribution of a memorandum to the Board regarding similar cases that had come up over the past several years, and there was agreement with this suggestion.

Governor Mills withdrew from the meeting at this point.

Interagency committees. Mr. Noyes reported on further meetings that had been held by the interagency committees appointed by the President to study financial institutions and Federal credit programs. In this connection, he described certain substantive questions that were now being taken up by the committee on financial institutions, and there followed a general discussion of some of the implications of these questions. It was understood from Mr. Noyes' comments that these and other matters to which the committee intended to give consideration were interrelated. Accordingly, additional exploration within the committee would be required before the point had been reached where recommendations from the committee to the President could be considered.

The meeting then adjourned.

Secretary's Note: Governor Shepardson today approved on behalf of the Board the following items:
Memorandum from the Division of Research and Statistics recommending acceptance of the resignation of Priscilla S. Goodby, Economist in that Division, effective at the close of business May 9, 1962.

Letters to the Federal Reserve Bank of Chicago (attached Items 4 and 5) approving the appointment of Gaylord Bernahl and Gerald F. Hines as examiners.
Board of Directors,
Central National Bank of Chicago,
Chicago, Illinois.

Gentlemen:

This relates to the application from your bank, submitted through the Federal Reserve Bank of Chicago, for permission to maintain the same reserves against deposits as required to be maintained by banks located outside of central reserve and reserve cities.

After considering the volume and growth of your bank's total demand deposits, including increases following its consolidation with the Merchants National Bank of Chicago, the activity shown in various classes of your deposit accounts, and your competition with other banks in the Loop, the Board has decided that the character of your bank's business is in many respects more like that of the other central reserve and reserve city banks in Chicago than that of Chicago banks which have been granted permission to maintain reduced reserves. Accordingly, the Board believes that it would not be justified in granting your application for reduced reserves.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.
Board of Directors,
Exchange National Bank of Chicago,
Chicago, Illinois.

Gentlemen:

This relates to the application from your bank, submitted through the Federal Reserve Bank of Chicago, for permission to maintain the same reserves against deposits as are required to be maintained by banks located outside of central reserve and reserve cities.

After considering the volume of your bank's total demand deposits, your competition with other banks, and the kinds of activity shown in various classes of accounts, the Board has decided that the character of your bank's business is in many respects more like that of the other central reserve and reserve city banks in Chicago than that of Chicago banks which have been granted permission to maintain reduced reserves. Accordingly, the Board believes that it would not be justified in granting your application for reduced reserves.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.
May 14, 1962

Mr. Howard Bertsch,
Administrator,
Farmers Home Administration,
Department of Agriculture,
Washington 25, D. C.

Dear Mr. Bertsch:

This is in response to your letter of February 15, 1962 in which you request the Board's views as to whether promissory notes evidencing loans by member banks to farmers which are insured by the Farmers Home Administration are eligible as collateral security for 90-day advances within the meaning of paragraph 8 of section 13 of the Federal Reserve Act.

It is understood that the loans in question are insured pursuant to the Consolidated Farmers Home Administration Act of 1961, which comprises title III of Public Law 87-128 approved August 8, 1961, and pursuant to section 51h of the Housing Act of 1949, as added by title VIII of Public Law 87-70 approved June 30, 1961. Loans insured under Public Law 87-128 are made for farm operating purposes and to permit farmers or ranchers to buy, enlarge, develop, or improve a farm or to refinance debts; to develop water supply systems for irrigation, household use, and livestock; to drain farmland; and to carry out soil conservation measures. Loans insured under Public Law 87-70 are made to individual farmers and groups of farmers, political subdivisions, and public or private nonprofit associations to construct or repair housing and related facilities for domestic farm labor.

Paragraph 8 of section 13 of the Federal Reserve Act provides that any Federal Reserve Bank "may make advances for periods not exceeding ninety days to its member banks on their promissory notes secured by such notes, drafts, bills of exchange, or bankers' acceptances as are eligible . . . for purchase by Federal reserve banks under the provisions of this Act." The insured notes here
The insured notes here involved are to be distinguished from the Government-insured marine bonds considered by the Board in a 1960 published interpretation (1960 Federal Reserve Bulletin 151). The obligations there involved, although technically "notes", were clearly what are generally regarded as securities, and the Board felt that they did not constitute the kind of notes contemplated by the provision authorizing advances to member banks secured by "notes, drafts, bills of exchange, or bankers' acceptances" eligible for discount or purchase by the Federal Reserve Banks. In contrast, the insured notes involved in the present case are not securities as that term is ordinarily used.

Accordingly you are advised that insured notes of the kind here involved are eligible as security for advances to member banks by Federal Reserve Banks.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.
May 14, 1962.

CONFIDENTIAL (FR)

Mr. Leland Ross, Vice President,
Federal Reserve Bank of Chicago,
Chicago 90, Illinois.

Dear Mr. Ross:

In accordance with the request contained in your letter of May 7, 1962, the Board approves the appointment of Gaylord Bernahl, at present an assistant examiner, as an examiner for the Federal Reserve Bank of Chicago, effective June 4, 1962.

It is noted that Mr. Bernahl is indebted to Branch County Savings Bank, Coldwater, Michigan, a non-member bank. Accordingly, the Board's approval of the appointment of Mr. Bernahl is given with the understanding that he will not participate in any examination of that bank until his indebtedness has been liquidated.

Very truly yours,

(Signed) Elizabeth L. Carmichael

Elizabeth L. Carmichael,
Assistant Secretary.
May 14, 1962.

CONFIDENTIAL (FR)

Mr. Leland Ross, Vice President,
Federal Reserve Bank of Chicago,
Chicago 90, Illinois.

Dear Mr. Ross:

In accordance with the request contained in your letter of May 7, 1962, the Board approves the appointment of Gerald F. Hines, at present an assistant examiner, as an examiner for the Federal Reserve Bank of Chicago, effective June 4, 1962.

It is noted that Mr. Hines is indebted to Branch County Savings Bank, Coldwater, Michigan, a nonmember bank. Accordingly, the Board's approval of the appointment of Mr. Hines is given with the understanding that he will not participate in any examination of that bank until his indebtedness has been liquidated.

Very truly yours,

(Signed) Elizabeth L. Carmichael

Elizabeth L. Carmichael,
Assistant Secretary.