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Minutes for May 17, 1962

To: Members of the Board

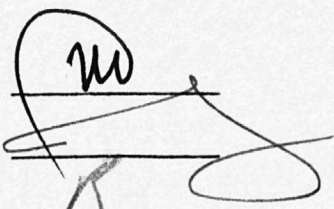
From: Office of the Secretary

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.

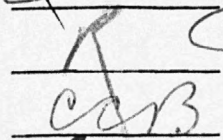
Should you have any question with regard to the minutes, it will be appreciated if you will advise the Secretary's Office. Otherwise, please initial below. If you were present at the meeting, your initials will indicate approval of the minutes. If you were not present, your initials will indicate only that you have seen the minutes.

Chm. Martin

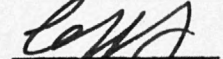


Gov. Mills

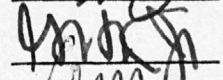
Gov. Robertson



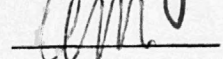
Gov. Balderston



Gov. Shepardson



Gov. King



Gov. Mitchell

Minutes of the Board of Governors of the Federal Reserve System on Thursday, May 17, 1962. 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. 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. Fauver, Assistant to the Board  
Mr. Cardon, Legislative Counsel  
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. O'Connell, Assistant General Counsel  
Mr. Hooff, Assistant General Counsel  
Mr. Holland, Adviser, Division of Research  
and Statistics  
Mr. Dembitz, Associate Adviser, Division of  
Research and Statistics  
Mr. Conkling, Assistant Director, Division  
of Bank Operations  
Mr. Daniels, Assistant Director, Division  
of Bank Operations  
Mr. Leavitt, Assistant Director, Division  
of Examinations  
Mr. Thompson, Assistant Director, Division  
of Examinations  
Mr. Potter, Senior Attorney, Legal Division  
Mr. Schwartz, Assistant to the Director,  
Division of Research and Statistics  
Mr. Veenstra, Technical Assistant, Division  
of Bank Operations  
Mr. Guth, Review Examiner, Division of  
Examinations

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

	<u>Item No.</u>
Letter to the Bureau of the Budget recommending that a proposed uniform statute amending the Negotiable Instruments Law to eliminate the necessity of protest with respect to domestic drafts and checks be submitted to the Committee of State Officials on Suggested State Legislation of the Council of State Governments for consideration.	1
Letter to the Post Office Department regarding authorization to its field officials to use direct air flights for dispatching Federal Reserve shipments of currency and negotiable securities valued at \$250,000 or more.	2
Letter to Manufacturers and Traders Trust Company, Buffalo, New York, approving the establishment of a branch in the Boulevard Mall Shopping Center, Amherst.	3
Letter to The First National Bank of Hope, Hope, Arkansas, approving its application for fiduciary powers.	4
Letter to Union Bank, Los Angeles, California, approving an extension of time to establish a branch at Wilshire Boulevard and Western Avenue.	5

Mr. Daniels then withdrew from the meeting.

Branch deposit data (Item No. 6). There had been distributed to the Board a memorandum from the Division of Bank Operations dated May 11, 1962, regarding the status of the proposal to expand the collection of data on branch deposits from a county to a city basis. Letters on this subject had been sent to the Comptroller of the Currency and the Federal Deposit Insurance Corporation on April 13, 1962. The

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Corporation responded favorably in a letter dated April 25, 1962, although with some indication that it might want to reconsider the matter if the Comptroller did not cooperate in the program. The Comptroller's reply dated April 26, 1962, was rather vague from the standpoint of whether his Office would or would not eventually decide to cooperate. Question was raised by him as to whether the purposes for which the data were thought necessary could not be served effectively through reports of examination or direct requests for needed data on specific cases.

The memorandum from the Division of Bank Operations suggested that there appeared to be three alternatives: (1) to accept the Comptroller's suggested alternative; (2) to propose the collection of reports of deposits by counties only (in other words, to continue the biennial reports of deposits by counties, a program that had been in effect since 1941); or (3) to move ahead with the expanded program on a basis whereby the Federal Reserve would collect the branch data from national banks if the Comptroller decided not to participate. Submitted with the memorandum was a draft of letter to the Comptroller indicating why it was felt that the sources of data suggested in his April 26 letter would not provide the needed information. Alternative concluding paragraphs were presented for consideration by the Board.

It developed from discussion of the memorandum that the members of the Board continued to favor the collection of data on



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branch deposits by cities along the lines that had been suggested in the Board's letter of April 13, 1962. It was the consensus, however, that it would be desirable to write again to the Comptroller in order to state for the record why the Board deemed the collection of such data to be essential to the performance of its regulatory functions, and to provide the Comptroller an opportunity to state definitely whether he would wish to cooperate in such a program. A number of suggestions were made for changes in the wording of the letter proposed to be sent to the Comptroller, after which it was agreed unanimously that the letter should be in the form attached as Item No. 6.

As indicated in the approved letter, a copy was to be sent to the Federal Deposit Insurance Corporation in view of its interest in the subject. The Board's action contemplated that upon receipt of a reply from the Comptroller, or within a reasonable time if no reply was received, the staff would inform the Board of developments prior to making final preparations for collection of the expanded branch deposit data in June 1962. It was understood that at such time as the staff made its further report, the Board would have in mind clarifying, if it was not already clear, whether the Federal Deposit Insurance Corporation was prepared to participate in the data collection program even if the Comptroller of the Currency did not participate.

Messrs. Holland, Conkling, and Veenstra then withdrew.

Proposed amendment to Regulation Q re long-term certificates of deposit (Item No. 7). Pursuant to the understanding at the meeting

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on Monday, May 14, there had been distributed a revised draft of letter to the Comptroller of the Currency replying to certain questions that he had raised in a letter of April 25, 1962, with respect to the practice recently instituted by some banks of advertising and selling long-term, low-denomination certificates of deposit.

In this connection, and pursuant to request made at the May 14 meeting, there had also been distributed a memorandum from Mr. Hackley dated May 16, 1962, submitting a possible amendment to section 217.3 of Regulation Q, Payment of Interest on Deposits, in order to make it clear that where a member bank contracted to pay a specified rate of interest to its depositors, the rate must be reduced, if necessary, to comply with any action of the Board of Governors reducing the maximum permissible rate of interest.

The draft of the proposed letter to the Comptroller of the Currency was discussed at some length and certain changes were suggested in the interest of clarification. Some of these suggestions related to the manner of responding to a question in the Comptroller's letter as to whether it was prudent banking practice for a bank to commit itself to pay a fixed rate on deposits for terms that might run as long as 20 years. During the discussion of the proposed reply to the Comptroller, it was also agreed to incorporate therein, with a request for comment, a possible amendment to Regulation Q substantially along the lines proposed in Mr. Hackley's May 16 memorandum.

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At the conclusion of the discussion, unanimous approval was given to a letter to the Comptroller of the Currency in the form attached as Item No. 7, with the understanding that the proposed amendment to Regulation Q would also be sent to the Federal Deposit Insurance Corporation and to the Federal Reserve Banks for comment.

Messrs. Young and Hooff then withdrew.

Question of establishing Federal Reserve branch at Milwaukee.

Prior to Vice Chairman Balderston's appearance before the House Committee on Banking and Currency on Friday, May 11, to testify on S. 1005, a bill that would permit additional construction of Federal Reserve Bank branch buildings, Congressman Reuss of Wisconsin advised Mr. Cardon that he intended to ask certain questions at the hearing with regard to the possible establishment of a Federal Reserve Bank branch at Milwaukee. However, after further conversation with members of the Board's staff, Mr. Reuss dropped his plan to ask such questions at the hearing. Instead, he requested a written reply to a letter to Vice Chairman Balderston dated May 9, 1962. In this letter Mr. Reuss inquired whether, in the event that the financial, business, industrial, agricultural, and civic community of Wisconsin indicated that proper System decentralization required a Federal Reserve branch bank in Milwaukee, full and fair consideration would be given by the Board of Governors to such a request.

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A draft of proposed reply to Congressman Reuss had been distributed to the Board under date of May 15, 1962. The draft indicated why it had appeared, after study of a Chicago Reserve Bank survey filed with the Board in 1954, that additional branches in the Seventh District were not justified at that time. It also referred to various factors deserving consideration in connection with decisions on establishing Reserve Bank branches and set forth several types of information that might be submitted on behalf of a request for consideration of the establishment of a branch in Milwaukee.

General discussion of the proposed reply to Congressman Reuss and the surrounding circumstances resulted in a suggestion, originated by Governor Mitchell and supported by Governor Robertson, that there be included in the letter to Mr. Reuss a description of the functions of a Reserve Bank branch. The thought was that such a description might be helpful to the Congressman in determining whether he would or would not want to take steps looking toward the collection of data for submission to the Board in connection with a request for consideration of the establishment of a branch in Milwaukee.

Certain other changes in the proposed letter were also suggested, and it was understood that a revised draft would be prepared for consideration by the Board, probably at the meeting on Tuesday, May 22.



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Mr. Dembitz then withdrew.

Application of Marine Corporation. There had been distributed memoranda from the Division of Examinations and the Legal Division dated May 4 and May 11, 1962, respectively, regarding an application by The Marine Corporation, Milwaukee, Wisconsin, for prior approval of the acquisition of shares of Security State Bank, Madison, Wisconsin. The recommendations of the Federal Reserve Bank of Chicago and the Division of Examinations were favorable, and the Commissioner of Banks of Wisconsin had expressed no objection. In the opinion of the Legal Division, either approval or disapproval of the application would be upheld by a court as being within the discretionary authority of the Board.

Comments by Governors Mills, Robertson, Shepardson, and King indicated that they would be inclined to accept the recommendation of the Division of Examinations that the application be approved. Governor Robertson noted that he found no factors sufficiently objectionable to cause him to feel that the application should be disapproved. Therefore, although he did not find substantial affirmative factors, he would be willing to approve the application.

Governor Mitchell commented that he was not particularly impressed by the arguments advanced by the applicant to the effect that the community in question would be benefited by the acquisition of Security State Bank by the holding company. He gathered that the Division of Examinations was not particularly impressed by those

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arguments. In the circumstances, he was desirous of being better informed about the holding company. If its principal functions were to acquire additional banks, receive dividends from such banks, and render only nominal service to them, he might be inclined to oppose the current application. In his review of the material presented to the Board, he had found it alleged by the holding company that certain services were available to the subsidiary banks, but he had not found evidence that those services were actually being rendered. Therefore, he would like the file on the case augmented to include information on what services the holding company was in a position to provide and what services it was actually performing.

In the light of Governor Mitchell's comments, it was agreed to defer action on the application pending the availability of information such as he had mentioned.

Messrs. Molony, Cardon, O'Connell, Leavitt, Thompson, Potter, and Guth then withdrew.

Boston computer. In a letter dated April 6, 1962, President Ellis of the Federal Reserve Bank of Boston informed the Board that the Bank had contracted for the lease of an IBM 1620 electronic computer, for use by the Research Department, at a cost of \$2,030 monthly. Mr. Ellis did not ask for Board approval because the rental involved was below the amount set forth in the Board's letter of November 16, 1961, in which the Reserve Banks were asked to inform the Board of proposals to acquire electronic equipment having a rental cost in excess of \$4,000

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a month before any firm commitments were made. The Board's staff had been advised informally that the equipment referred to in the letter from President Ellis had now been installed.

In a memorandum from the Division of Bank Operations dated May 14, 1962, which had been distributed, it was noted that the rental of the IBM 1620 computer had been discussed by the Board's staff with President Ellis, at which time Mr. Ellis was handed copies of a memorandum from Mr. Schwartz dated May 4, 1962, in which some reservations were expressed regarding the desirability of the lease of a separate computer for use by the Research Department. The recommendation in the memorandum was that no Board action be taken at this time, subject to the understanding that the staff would keep in touch with further developments.

Comments made by Messrs. Farrell and Schwartz at the request of the Board indicated that the principal issue related to the advisability of a Reserve Bank installing a second computer, in this case a machine having some operational limitations, for the particular use of its research staff. This arrangement was in contrast to the decision at several Reserve Banks to equip a single computer for multi-purpose use.

After consideration of the arguments for and against the respective arrangements, a general view prevailed that, despite such reservations as might be entertained, the Board should not object

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actively to a Reserve Bank decision of the kind made by the Boston Bank in this experimental field. It was noted that a copy of the memorandum from Mr. Schwartz had already been handed to President Ellis. Accordingly, it was the consensus that there was no need to reply to Mr. Ellis' letter of April 6, 1962. However, it was understood that the Board's staff would keep in touch with further developments.

All members of the staff except Messrs. Sherman and Kenyon then withdrew.

Travel by Mr. Young. The Board authorized Ralph A. Young, Adviser to the Board and Director of the Division of International Finance, to travel to Paris, France, during the period May 27-31, 1962, to attend a meeting of Working Party 3 of the Economic Policy Committee of the Organization for Economic Cooperation and Development, with reimbursement on an actual expense basis, including official entertainment.

Approval of certain foreign travel. Governor Shepardson, who previously had been authorized, as the member of the Board vested with responsibility for direction of internal affairs of a managerial nature, to approve travel requests from members of the staff in accordance with the official travel regulations of the Board, was additionally authorized to approve foreign travel by staff members for the purpose of attending meetings of Working Party 3 of the Economic Policy Committee of the Organization for Economic Cooperation and Development.



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The meeting then adjourned.

Secretary's Note: Governor Shepardson today approved on behalf of the Board the following items:

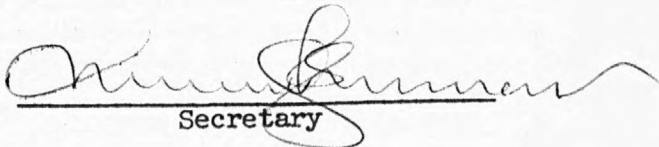
Memoranda from appropriate individuals concerned recommending the appointment of the following persons to the Board's staff, effective the respective dates of entrance upon duty:

Helen Mable Riddick as Minutes Clerk,  
Office of the Secretary, with basic  
annual salary at the rate of \$4,075.

Jaclene Therese Masterson as Stenographer,  
Legal Division, with basic annual salary  
at the rate of \$4,145.

Darlene J. Butler as Research Assistant,  
Division of Research and Statistics,  
with basic annual salary at the rate of  
\$5,355.

Memorandum from Mr. Landry, Assistant to the Secretary of the Board, requesting that a luncheon be provided on May 31, 1962, for Federal Reserve librarians who would be attending the annual meetings of the Special Libraries Association in Washington, D. C.

  
Secretary

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

Item No. 1  
5/17/62

ADDRESS OFFICIAL CORRESPONDENCE  
TO THE BOARD

May 17, 1962



Mr. Elmer B. Staats,  
Deputy Director,  
Bureau of the Budget,  
Washington 25, D. C.

Dear Mr. Staats:

This is in reply to your letter of April 4, 1962, inquiring whether the Board has any proposals for State Legislation which it would desire to present to the Bureau of the Budget for consideration by the Committee of State Officials on Suggested State Legislation of the Council of State Governments.

The Executive Council of the American Bankers Association has approved a recommendation made by the Association's Committee on State Legislation for enactment by the States of a proposed uniform statute amending the Negotiable Instruments Law to eliminate the necessity of protest with respect to domestic drafts and checks. It is understood that the ABA Committee has transmitted copies of the proposed statute to the various State bankers associations urging that they sponsor its enactment.

The proposed statute was drafted in collaboration with a Committee of the Conference of Presidents of the Federal Reserve Banks. In the opinion of the Board, enactment of this statute by the various States would be desirable.

Accordingly, the Board again recommends that this proposal be submitted to the Committee of State Officials on Suggested State Legislation of the Council of State Governments for its consideration. Copies of the proposed statute and an accompanying statement prepared by the Executive Council of the American Bankers Association are enclosed. By way of supplement to that statement, which was prepared some time ago, it may be mentioned that, according to our present information, the proposed statute has now been adopted in at least fourteen States and the substance of the proposed statute has been incorporated in the Uniform Commercial Code adopted in at least fifteen States.

Very truly yours,  
(Signed) Merritt Sherman

Merritt Sherman,  
Secretary.

Enclosures

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

Item No. 2  
5/17/62

ADDRESS OFFICIAL CORRESPONDENCE  
TO THE BOARD

May 17, 1962

Mr. Edwin A. Riley, Director,  
Classification and Special  
Services Division,  
Post Office Department,  
Bureau of Operations,  
Washington 25, D. C.

Reference: WJW/sd

Dear Mr. Riley:

Reference is made to your letter of March 14, 1962. You asked whether the Board would favor authorization being extended to your field officials to use direct air flights for dispatching Federal Reserve shipments of currency and negotiable securities valued at \$250,000 or more, when in the judgment of the official the number of transfers and transit time by rail would be unfavorable, either from a time or security standpoint, or both.

The Board referred this request to the Federal Reserve Banks for their opinions and none expressed any objection to the proposed procedure.

Because of the relatively short distances existing between most of the 36 Reserve Bank offices and the destinations in their districts to which shipments are made, it is not anticipated that many shipments would come under the proposed plan.

In addition to shipments of currency made by the Federal Reserve Banks, two other types of shipments could be involved. (1) Shipments to member banks and paying agents of negotiable securities. These shipments are covered by insurance purchased at the expense of the member banks for whose accounts the shipments are made. If it is expected that there would be any substantial volume of registered mail shipments dispatched by air flight, you might wish to acquaint the registered mail underwriters with the proposal. (2) Shipments to member banks and others, for the most part negotiable securities on original issue, made by the Reserve Banks



Mr. Edwin A. Riley

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as Fiscal Agents of the United States. These shipments are covered under the Government Losses in Shipment Act. In respect to such shipments, you might wish to notify the Treasury Department of the proposed procedure.

Some concern has been expressed of the risk inherent in air transportation, especially from fire or a scattering of the shipment in case of a plane crash and of robbery in the event of any forcible possession taken of a plane. Probable inadequacy of protective facilities at the air terminals in case of postponement or cancellation of flights has also been mentioned. These are areas wherein it is felt every effort should be made to establish safeguards where possible.

It is understood, from conversations between representatives of the Post Office Department and the Board, that the proposed procedure would not apply at this time to shipments of Federal Reserve notes from Washington. The Board would appreciate being informed of any intention to dispatch shipments of Federal Reserve notes from Washington by air.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,  
Secretary.



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

Item No. 3  
5/17/62

ADDRESS OFFICIAL CORRESPONDENCE  
TO THE BOARD

May 17, 1962

Board of Directors,  
Manufacturers and Traders Trust Company,  
Buffalo, New York.

Gentlemen:

The Board of Governors of the Federal Reserve System approves the establishment of a branch by the Manufacturers and Traders Trust Company, Buffalo, New York, in the Boulevard Mall Shopping Center at the intersection of Niagara Falls Boulevard and Maple Road Extension, Amherst, New York, provided the branch is established within one year from the date of this letter.

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  
5/17/62

ADDRESS OFFICIAL CORRESPONDENCE  
TO THE BOARD



May 17, 1962

Board of Directors,  
The First National Bank of Hope,  
Hope, Arkansas.

Gentlemen:

The Board of Governors of the Federal Reserve System has given consideration to your application for fiduciary powers and grants The First National Bank of Hope authority to act, when not in contravention of State or local law, as trustee, executor, administrator, registrar of stocks and bonds, guardian of estates, assignee, receiver, committee of estates of lunatics, or in any other fiduciary capacity in which State banks, trust companies, or other corporations which come into competition with national banks are permitted to act under the laws of the State of Arkansas. The exercise of such rights shall be subject to the provisions of Section 11(k) of the Federal Reserve Act and Regulation F of the Board of Governors of the Federal Reserve System.

A formal certificate indicating the fiduciary powers that your bank is now authorized to exercise will be forwarded in due course.

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. 5  
5/17/62

ADDRESS OFFICIAL CORRESPONDENCE  
TO THE BOARD

May 17, 1962



Board of Directors,  
Union Bank,  
Los Angeles, California.

Gentlemen:

The Board of Governors of the Federal Reserve System extends to May 21, 1963, the time within which Union Bank, Los Angeles, may establish a branch on the southwest corner of the intersection of Wilshire Boulevard and Western Avenue, Los Angeles, California.

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. 6  
5/17/62

ADDRESS OFFICIAL CORRESPONDENCE  
TO THE BOARD

May 17, 1962.

The Honorable James J. Saxon,  
Comptroller of the Currency,  
Washington 25, D. C.

Dear Mr. Saxon:

Thank you for your letter of April 26, 1962, with respect to the collection of more meaningful branch deposit data, which the Board considers essential to the performance of its regulatory functions. Your letter raised the question whether such purposes might not be served effectively through reports of examination or by direct requests for needed data relating to specific cases.

While careful consideration has been given to the alternative sources of data suggested in your letter, the Board feels that its experience with use of examination reports and data furnished in response to requests directed to a limited number of banks has not provided the broad background of information that is needed in considering changes in the banking structure and has been inadequate in a number of specific cases.

These alternative sources do not provide the necessary basis for comparison of the areas involved in specific cases with other similar areas. The variations in dates of information gleaned from examination reports have also been a problem in some instances. Information submitted in response to requests for data in specific cases is always open to challenge as being provided by interested parties. The time involved in gathering deposit information from these sources has also resulted in unfortunate delays in consideration of some cases.

Because current decisions of this nature influence the banking structure for years to come, they should be made on the basis of reliable and current information consistent with the importance and complexity of the problems involved. Great attention has been devoted to the apparent logic behind supervisory decisions influencing concentration and competition in banking, and these





The Honorable James J. Saxon

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decisions should be justifiable by demonstrable fact. That the three Federal bank supervisory agencies, the State banking departments, the Department of Justice and the courts, and many banking analysts often disagree widely on the present nature of the banking structure and the direction in which it should evolve, is an indication of the need for better perspective on the issues involved. The Board feels that cooperative efforts among the banking agencies such as the proposed branch deposits survey and the survey now being conducted by the New York State Banking Department with the cooperation of your Office and the Federal Reserve Bank of New York are useful and justify the modest reporting burden entailed.

The Board is not unmindful of the workload that is imposed upon banks in responding to requests by supervisory agencies for various kinds of data, and careful attention was given to this consideration in formulation of the program outlined in the Board's letter to you of April 13, 1962. With this thought in mind, it was proposed that the branch reports would be confined to the relatively simple breakdown of deposits that has been collected for many years under the regular deposits by counties program and that no loan data would be requested. Prior to the decision to request deposit data, the Board made a rather extensive survey of the availability of such data; a copy of a report of this survey was enclosed with the Board's letter of April 13. As you may have noted, the responding banks indicated, with few exceptions, that the furnishing of deposit data would involve little additional reporting burden.

In these circumstances, and after reviewing the matter carefully, the Board continues to believe that these data should be collected. Participation by your Office in the program outlined in the April 13 letter would be most helpful. It is contemplated that the proposed data will be collected in June of 1962; therefore, an early reply would be appreciated.

A copy of this letter is being sent to the Federal Deposit Insurance Corporation in view of its interest in the matter.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,  
Secretary.

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

Item No. 7  
5/17/62

ADDRESS OFFICIAL CORRESPONDENCE  
TO THE BOARD

May 21, 1962

The Honorable James J. Saxon,  
Comptroller of the Currency,  
Treasury Department,  
Washington 25, D. C.

Dear Mr. Saxon:

This refers to your letter of April 25, 1962, regarding the practice recently instituted by some banks of advertising and selling long-term, low-denomination certificates of deposit.

Your first inquiry relates to the question whether a bank is misleading the public when it advertises deposits as carrying a "guaranteed" rate of interest.

As you know, section 19 of the Federal Reserve Act requires the Board of Governors from time to time to limit by regulation the rate of interest that may be paid by member banks on time and savings deposits. Obviously, the purpose of this provision of the law might be defeated to some extent if member banks could agree by contract to pay a specified rate of interest for a long period of time and continue to pay that rate after any action by the Board reducing the maximum rate below that specified in the contract.

Section 217.3(b) of Regulation Q, referred to in your letter, provides that no certificate of deposit or other contract shall be renewed or extended unless modified to conform to the provisions of the Regulation, and that a 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 or other contracts into conformity with the Regulation. This provision, which was inserted in 1933 when the law was first enacted, was not intended to permit member banks, under contracts made after the enactment of the law, to continue to pay a specified rate of interest after any action of the Board prescribing a lesser maximum rate.

In order that member banks might have "actual knowledge" that the rate of interest is subject to modification to conform to the maximum rate prescribed by the Board, it was suggested by the Board in 1933 (1933 Federal Reserve Bulletin 768) that member banks stamp on each time certificate a provision substantially as follows:



The Honorable James J. Saxon -2-

"The rate of interest payable hereunder is subject to change by the bank to such extent as may be necessary to comply with requirements of the Federal Reserve Board made from time to time pursuant to the Federal Reserve Act."

In other words, deposit contracts between member banks and their customers must be regarded as being made in the light of the statute and the Board's Regulations. In order that the public might not be misled, every certificate of deposit or other deposit contract should contain a provision, substantially similar to that quoted above, stating in clear and precise language (and not in small print or in an obscure place) that the interest rate is subject to reduction in the event that the Board should reduce the maximum rate of interest that may be paid on such deposit. Without such a provision, a certificate providing for a "guaranteed" rate of interest might be particularly misleading to the public.

Since the provisions of section 217.3(b) of Regulation Q may tend to give an impression contrary to the position of the Board as stated above, the Board is giving consideration to an amendment to Regulation Q that would eliminate these provisions and, at the same time, make it clear that the rate of interest agreed to be paid by member banks under their deposit contracts must be reduced, if necessary, to comply with any action by the Board reducing the maximum permissible rate.

A copy of a draft of such an amendment is enclosed and the Board will be glad to have any comments that you may wish to offer. In view of the authority of the Federal Deposit Insurance Corporation to prescribe maximum interest rates on deposits payable by nonmember insured banks, the Board is informing the Corporation of this proposed amendment, in order that the Corporation may consider at the same time whether a similar amendment to its regulations on this subject should be adopted. The comments of the Federal Reserve Banks are also being requested.

Apart from the aspect of the matter discussed above, your letter raises a question as to whether it is prudent banking practice for a bank to commit itself to pay a fixed rate of interest on deposits for terms that may run as long as 20 years. Depending upon the period of time involved in the commitment and the volume of such commitments in relation to the bank's total liabilities, the issuance of certificates of this kind would not necessarily be inconsistent with sound

The Honorable James J. Saxon      -3-

banking practice. It is believed, however, that the use of such instruments bears careful watching and that the bank supervisory agencies should be alert to any undesirable trend toward excessive use of long-term certificates.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,  
Secretary.

Enclosure



## PROPOSED AMENDMENT TO REGULATION Q

Amend section 217.3 of Regulation Q by deleting the present subsection (b) and substituting the following:

"(b) Contract rate subject to reduction to conform to regulation. - Whenever the Board of Governors reduces the maximum rate of interest payable on any time or savings deposit, no member bank shall thereafter pay interest on any such deposit at a rate in excess of such reduced maximum rate, notwithstanding the rate provided in any outstanding deposit contract. Every member bank shall inform its time and savings depositors, by an appropriate provision in every passbook, certificate of deposit, or other deposit contract, that the contract rate is subject to reduction in order to comply with the requirements of this paragraph."