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Minutes for July 31, 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



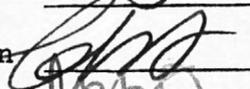
Gov. Mills

Gov. Robertson

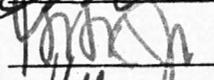
Gov. Balderston



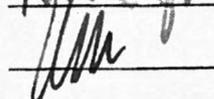
Gov. Shepardson



Gov. King



Gov. Mitchell



Minutes of the Board of Governors of the Federal Reserve System on Tuesday, July 31, 1962. The Board met in the Board Room at 11:55 a.m.

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

Mr. Kenyon, Assistant Secretary
Mr. Hackley, General Counsel
Mr. Shay, Assistant General Counsel

Mr. Hayes, President, Federal Reserve Bank of New York
Mr. Swan, President, Federal Reserve Bank of San Francisco

Israel Discount Bank Limited. Israel Discount Bank Limited, of Tel Aviv, Israel, a privately-owned commercial bank, had raised the question whether its recently established New York City branch would be eligible for admission to membership in the Federal Reserve System. The answer to that question being clearly in the negative, the bank had inquired whether in the alternative it would be eligible to carry a nonmember clearing account with the Federal Reserve Bank of New York under the first paragraph of section 13 of the Federal Reserve Act or to establish an account with the Federal Reserve Bank under section 14(e) of the Act. The matter was discussed by the Board at its meeting on July 12, 1962, but no conclusions were reached. As to the question of the eligibility

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of the New York City branch of Israel Discount Bank Limited for a nonmember clearing account, the bank had already been advised informally by representatives of the New York Reserve Bank that the opening of such an account would be of doubtful legality. On the other hand, it was noted that the Federal Reserve Bank of San Francisco had for many years carried such accounts for Portland and Seattle branches of the Canadian Imperial Bank of Commerce. In the circumstances, the Board decided that it would be appropriate as a next step to have a discussion of the subject with the Presidents of the New York and the San Francisco Banks, and it was for that purpose that today's meeting was held.

Chairman Martin turned first to President Hayes, who made a statement in which he indicated that the questions raised by Israel Discount Bank had been gone into at some length at the New York Reserve Bank by operating personnel and by Counsel. In general, the Reserve Bank thought it desirable for a Federal Reserve Bank to be able to open and maintain an account for a local branch of a foreign commercial bank. However, Counsel entertained serious doubts regarding the legal authority for opening such an account. In the circumstances, it was felt that it might be desirable, if the Board concurred, to attempt to clarify through legislation the authority to open a nonmember clearing account for such a branch. It was also felt that the Federal Reserve Banks

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should continue to have the same discretionary authority, in the case of branches of foreign banks, that they had exercised in the case of domestic banks seeking to establish nonmember clearing accounts. The New York Bank was cognizant of the fact that in the Twelfth Federal Reserve District certain branches of a Canadian bank had carried clearing accounts with the Reserve Bank for some time, presumably with the concurrence of the Reserve Bank's Counsel. However, the New York Bank still felt there were grave doubts as to the legality of such procedure, and would be reluctant to open such an account. It was noted that a bill had been introduced in the Congress by Representative Multer that would enable branches of foreign commercial banks licensed to do business in the United States to obtain deposit insurance through the Federal Deposit Insurance Corporation. This suggested the possibility of tying in with that bill a clarification of the authority to open nonmember clearing accounts for branches of foreign commercial banks licensed to do business in the United States.

President Hayes went on to say that in the opinion of the New York Reserve Bank a clarification of authority under section 13 would be preferable to proceeding under section 14(e) of the Federal Reserve Act, which enables Federal Reserve Banks to open accounts for foreign banks. It was felt that section 14(e) was clearly intended to be used for the purpose of maintaining relations with

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other central banks and not for the purpose of opening accounts for branches of foreign commercial banks.

In further comments, President Hayes said that if legislative clarification of section 13 should be obtained, the New York Bank would propose to use the same standards to determine whether non-member clearing accounts should be made available for branches of foreign banks that were applied in the case of domestic banks. There should be no favoritism. A Reserve Bank should not do more for a domestic bank with the same needs, but neither should it do less. Questions of opening specific accounts should be left to the discretion of the respective Reserve Banks in the same manner that judgments were now made with respect to domestic banks.

The Chairman then turned to President Swan, who commented that the Portland and Seattle Branches of the San Francisco Reserve Bank had been carrying nonmember clearing accounts for local branches of the Canadian Imperial Bank of Commerce since 1917 and 1918, respectively. Therefore, the current question came as something of a surprise; so far as the Reserve Bank knew, the situation had never been questioned previously. When the San Francisco Bank opened these accounts, it did so on the strength of a letter dated July 30, 1917, containing what was described as an informal opinion of Board Counsel. According to that opinion there was nothing in the Federal Reserve Act that would expressly or by implication prevent the

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Federal Reserve Bank from "receiving deposits and extending the clearing privileges to the Portland Branch of the Canadian Bank of Commerce." In view of the current question, Counsel for the San Francisco Bank had reviewed the matter. Counsel felt, however, that in view of what had happened over the years and the fact that nonmember clearing accounts for branches of foreign banks were not expressly prohibited by the Federal Reserve Act, the legality of the maintenance of the existing accounts should be accepted. Counsel agreed that it was preferable to think in terms of nonmember clearing accounts under section 13 rather than accounts under section 14(e).

President Swan went on to say that while he would have no particular objection to clarification of the law if that was thought necessary, he wondered whether matters could not be left as they stood. If a request for legislative clarification were made and proved abortive, the San Francisco Reserve Bank would be placed in a rather peculiar position. If there seemed any basis for thinking that the maintenance of the present accounts was within the authority of the law, as Board Counsel apparently believed in 1917, he would prefer simply to continue on that basis.

In reply to a question, Mr. Swan brought out that the Portland and Seattle offices were direct branches of the Canadian Imperial Bank of Commerce. In California a branch of a foreign

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bank cannot accept deposits. Therefore, an institution named the Canadian Bank of Commerce (California) had been incorporated under California law. In the State of Washington, the direct branch of the foreign bank was allowed to operate only under a "grandfather clause" in the law, and it was not anticipated that additional direct branches of foreign banks would be opened in Oregon. Hence, the San Francisco Reserve Bank did not expect the question of opening a nonmember clearing account to be raised with it again by any foreign bank on behalf of a domestic branch. The outlook differed, therefore, from that in New York.

Governor Mills asked whether it was not correct to say as a practical matter that nonmember clearing accounts were maintained as a matter of convenience to the local financial community. If the question currently raised was debated too much, it might amount to making a mountain out of a molehill. He was apprehensive that legislative debate of the subject might open up more serious, even though irrelevant, problems.

President Swan indicated that this was the way he felt about the matter.

The Chairman next turned to Mr. Hackley, who said it seemed clear that the legal question was not open and shut. As Mr. Swan had indicated, Board Counsel in 1917 informally expressed the opinion that there was no legal obstacle to opening a nonmember clearing

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account for a branch of a foreign bank. On the other hand, in subsequent interpretations the Board had made certain statements that seemed to run in an opposite direction. Mr. Hackley then discussed the definition of a bank contained in section 1 of the Federal Reserve Act, following which he noted, like Mr. Swan, that if the Board should go to Congress and clarifying legislation were not enacted, doubt might be cast on the legality of the present arrangements in the Twelfth District.

Mr. Shay expressed agreement with Mr. Hackley. He added that the staff of the Federal Deposit Insurance Corporation was believed to look with disfavor on the bill introduced by Congressman Multer that would provide deposit insurance for branches of foreign banks licensed to do business in the United States, which raised a question about the feasibility of attempting to tie a clarification of section 13 into that bill.

Governor Robertson inquired whether it would not seem that the legal interpretation by Board Counsel, which had been outstanding over a long period of time, could be relied upon for authority if a Reserve Bank desired to open an account for a local branch of a foreign bank, to which President Hayes replied that he was not a lawyer but that the New York Reserve Bank's Counsel had expressed the opinion that the Bank should be reluctant to open such an account.

Governor King inquired about potential dangers in opening such an account, to which President Swan replied that the San Francisco

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Reserve Bank had not seen any abuses or potential dangers. If it had, the situation in Portland and Seattle would not have been allowed to continue. Since the local branches of the foreign bank could not become members of the Federal Reserve System and yet were members of the financial community, the nonmember clearing arrangement, which was intended to facilitate the payments mechanism in the areas concerned, seemed to operate to everyone's advantage.

Governor King then inquired whether foreign central banks maintained accounts for branches of United States banks abroad, to which Mr. Hayes replied that foreign branches of such banks had accounts with the central bank in almost every country where those branches existed. An exception was the Bank of England. The question of reciprocity did not arise particularly at the moment because, aside from the Israel Discount Bank, the only foreign banks having branches in New York City were British institutions. However, the issue of reciprocity would become pertinent if commercial banks in certain other foreign countries should establish branches in New York City. From a policy standpoint, therefore, the New York Reserve Bank would like to be in the position of being able to open nonmember clearing accounts for local branches of foreign banks, even though it did not have any particular enthusiasm for nonmember clearing accounts as such. It was his feeling that foreign banks

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seeking to have such accounts opened for their New York City branches would be motivated substantially by the prestige factor, since such an account would only be of moderate advantage from the standpoint of facilitating the check-clearing process. Alternative methods of clearing checks were available. Nonmember clearing accounts for domestic banks had not been growing and were not currently of great importance, President Hayes noted. However, it would be a nice thing to extend that privilege to branches of foreign banks if they met the standards applied generally by the Reserve Bank. If the disposition of the Board was to say that under its interpretation of the law the opening of such accounts for branches of foreign banks was permissible, the New York Bank certainly would propose to take another look at its Counsel's advice.

Governor Mitchell questioned the advisability of having two interpretations of the same law within the Federal Reserve System, following which Mr. Hackley pointed out that the Board did not authorize the opening of the accounts by the San Francisco Reserve Bank. The question of opening particular accounts had always been a matter of determination by the Reserve Bank concerned in its judgment. On the other hand, the Board had not raised any objection to the continuance of the accounts opened by the San Francisco Bank.

Governor Robertson suggested the possibility of a letter from the Board that would point out that the two nonmember clearing accounts

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had been maintained by the San Francisco Bank for a period of about 45 years, or since shortly after the Federal Reserve System was created; that at that time there was an informal opinion of Board Counsel with respect to the matter; and that in view of this opinion and the long-continued practice there seemed no reason why the New York Reserve Bank, if it saw fit, should not grant a nonmember clearing account to the branch of the Israel Discount Bank.

President Hayes commented that he felt a letter along such lines would help.

Mr. Shay brought out at this point that a recognition of the eligibility of branches of foreign commercial banks for nonmember clearing accounts might make it a little more difficult to tell private bankers that they were ineligible or to reject requests from institutions that are almost banks but not quite. In other words, it might become a little more difficult to differentiate.

Mr. Shay also commented to the effect that the provisions added to the New York State Banking Law in 1960, which authorized the granting of licenses to branches of foreign commercial banks, required such institutions to conform to practically every law on the books that was applicable to domestic banks. However, the branches of foreign banks were not quite in the same status as domestic banks.

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Governor King noted that, as President Swan had pointed out, branches of foreign banks could not become members of the Federal Reserve System, while that opportunity was open to domestic banks if they made application and met the required standards. As to the opening of nonmember clearing accounts for branches of foreign banks, he would have no objection if a Federal Reserve Bank should decide as a matter of policy that it did not want to open such an account. However, he doubted that an adverse answer should be given on a legal basis in view of the accounts that had been maintained in the Twelfth District for many years. He felt that as a member of the Board he would be willing to concur in a favorable legal opinion if that would help to clarify the matter.

In reply to a question as to whether Counsel for the New York Reserve Bank held the opinion that the law prohibited the opening of a nonmember clearing account for a branch of a foreign commercial bank or whether Counsel held that the law did not affirmatively permit the opening of such an account, President Hayes read portions of the opinion that had been rendered by the Bank's Counsel, concluding with a statement to the effect that Counsel had serious legal doubt as to whether such a branch could qualify for an account.

Governor Balderston noted that it had been suggested that it was an accommodation to nonmember banks to have clearing accounts

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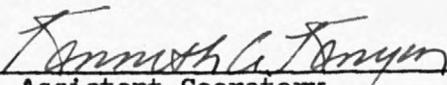
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opened because this was helpful in the processing of checks. If the Board sought clarifying legislation, but that was not obtained, a shadow of doubt would be cast on the arrangements that had existed in the Twelfth District as far back as 1917. A policy decision, he suggested, should take into account what risks were envisaged, and Mr. Swan had stated that in all the years that the clearing accounts had been maintained in the Twelfth District, the Reserve Bank had experienced no problem. In summary, Governor Balderston suggested that the question was one to be settled as a policy matter involving the System as a whole. The advice of the System's lawyers was appreciated, yet the alternative of seeking legislation and the possibility that such a course might cloud the whole situation would cause him to suggest settlement of the question as a policy matter.

Chairman Martin then commented that he felt enough had been gotten out of this meeting so that the matter could be reviewed further by Board Counsel and by the New York Reserve Bank. He thought that it should be possible to work out a solution.

Accordingly, it was understood that Mr. Shay would be in touch with Counsel for the New York Reserve Bank with a view to further consideration of the questions involved.

The meeting then adjourned.


Assistant Secretary