Minutes for October 25, 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, October 25, 1962. The Board met in the Board Room at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
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. Cardon, Legislative Counsel
Mr. Fauver, Assistant to the Board
Mr. Hackley, General Counsel
Mr. Noyes, Director, Division of Research and Statistics
Mr. Farrell, Director, Division of Bank Operations
Mr. Kelleher, Director, Division of Administrative Services
Mr. Harris, Coordinator of Defense Planning
Mr. Hexter, Assistant General Counsel
Mr. Shay, Assistant General Counsel
Mr. Hooff, Assistant General Counsel
Mr. Kiley, Assistant Director, Division of Bank Operations
Mr. Leavitt, Assistant Director, Division of Examinations
Mr. Thompson, Assistant Director, Division of Examinations
Mrs. Semia, Technical Assistant, Office of the Secretary
Miss Hart, Senior Attorney, Legal Division
Mr. Potter, Senior Attorney, Legal Division
Mr. Doyle, Attorney, Legal Division

Report on emergency measures. At Chairman Martin's request, Mr. Harris reported on the System's emergency planning program, against the background of the President's announcement on October 22, 1962, of a quarantine on shipments of offensive military weapons to Cuba.

Mr. Harris then withdrew.

Mr. Young reported on developments in foreign exchange and gold markets following the onset of the present international crisis.

Circulated or distributed items. The following items, copies of which are attached to these minutes under the respective item numbers indicated, were approved unanimously:

	Item No.
Letter to Union Bank, Los Angeles, California, approving the establishment of a branch near Ninth and Main Streets.	1
Telegram to the Federal Reserve Bank of Chicago interposing no objection to the rental, with purchase option, of a second complement of Burroughs B-270 electronic check processing equipment.	2
Memorandum from Mr. Kelleher recommending execution of an agreement between the Board and General Services Administration under which the Federal Reserve System would be afforded the economies of multiple group communication tariffs offered by the American Telephone and Telegraph Company. (The agreement was executed by the Secretary of the Board on October 26, 1962.)	3
Letter to the Chairman of the Conference of Presidents regarding the execution of the agreement described under Item No. 3.	4
Letter to Citizens Bank & Trust Company, Park Ridge, Illinois, granting the bank's request for a further extension of time for discontinuance of its United Security Account plan.	5
Interpretation of Regulation T regarding the time allowed for payment for mutual fund shares purchased in a special cash account. (With the understanding that a copy would be sent to the law firm that had raised the question and that it would be published in the Federal Register and the Federal Reserve Bulletin.)	6

With respect to Item No. 5, there was a discussion during which certain changes in the wording of the draft letter that had been distributed were agreed upon; the letter in the form attached to these minutes reflects those changes.

Application of Virginia Commonwealth Corporation (Items 7 and 8). Pursuant to the decision reached at the meeting on October 11, 1962, there had been distributed a proposed order and statement reflecting the Board's approval of the application of Virginia Commonwealth Corporation, Richmond, Virginia, to acquire more than 50 per cent of the voting shares of The Bank of Virginia, Richmond, Virginia; The Bank of Henrico, Sandston, Virginia; The Bank of Salem, Salem, Virginia; The Bank of Occoquan, Occoquan, Virginia; and Bank of Warwick, Newport News, Virginia.

After discussion during which an editorial change in the statement was suggested and adopted, the issuance of the order and statement was authorized. Copies of the order and statement, as issued, are attached as Items 7 and 8.

Messrs. Farrell, Kelleher, Hooff, Kiley, Thompson, and Potter then withdrew, as did Miss Hart, and Mr. Furth, Adviser, Division of International Finance, entered the room.

Testimony by bank examiner (Item No. 9). Mr. Shay reported that he had received a telephone call from Mr. Rudy, General Counsel of the Federal Reserve Bank of Dallas, who stated that one of the Bank's examiners had been subpoenaed to testify on Monday, October 29, 1962,

at the trial of criminal charges involving a disappearance of funds of First State Bank, Premont, Texas. (The operations of this bank had been suspended effective December 30, 1961.) The examiner would be expected to testify to the effect that during the December 1961 examination of the bank five promissory notes had been placed in the bank's vault, which notes were removed under circumstances tending to incriminate an officer of the bank. At the time of the incident the examiner had written a memorandum about it to former Vice President Pondrom of the Dallas Reserve Bank, and the examiner might be asked to place that memorandum in evidence. Two questions were therefore presented: first, whether the Board would offer any objection to the examiner's testifying, and second, if he did testify, whether the Board would object to having the memorandum supplied for the trial record. Mr. Rudy recommended that no objection be interposed in either regard.

In continuing, Mr. Shay stated that he and Mr. Leavitt had been going through a copy of the examiner's memorandum, but had been unable to complete their review of it before this meeting. Thus far they had found nothing in the memorandum that would seem to point to the inadvisability of allowing it to be placed in evidence. He suggested that, if the Board saw fit to interpose no objection, Mr. Rudy not be notified of that decision until review and evaluation of the memorandum could be completed.

After discussion the Board agreed to interpose no objection to the examiner's testifying at the coming trial or to his furnishing to

the court, if requested, his memorandum regarding the incident in question, on condition that completion of the review of the memorandum by the Board's staff did not disclose any consideration that, in the opinion of the Legal Division, constituted grounds for interposing an objection.

Secretary's Note: The completion of evaluation of the memorandum not having developed any information that the Legal Division considered prejudicial to the interests of the Federal Reserve System, a telegram in the form attached as Item No. 9 was sent later in the day to inform Mr. Rudy of the position taken by the Board.

Mr. Shay then withdrew.

Status of Bank for International Settlements (Items 10 and 11).

There had been distributed a memorandum dated October 24, 1962, from Mr. Hackley relating to the question whether the Bank for International Settlements, Basle, Switzerland, was covered by the October 15, 1962, amendment to section 19 of the Federal Reserve Act (Public Law 87-827) exempting certain foreign institutions from interest rate limitations on time deposits. The memorandum described views conveyed to the Board's Legal Division by counsel for the Treasury and the New York Reserve Bank, both of which organizations were hopeful that the Board would reach an affirmative decision on the question. However, after consideration of the arguments on each side, Mr. Hackley had reached the conclusion that the better legal arguments supported the position that the Bank for International Settlements was not covered by the amendment to section 19.

Although expressing this opinion, he noted that persuasive arguments had been made in support of an affirmative view, particularly the argument that coverage of the Bank for International Settlements would be consistent with the underlying intent and purposes of the statute. Those arguments could, of course, be relied upon if the Board should decide to adopt that position.

The Federal Deposit Insurance Corporation had a parallel interest in the matter insofar as nonmember insured State banks might receive time deposits from the Bank for International Settlements. It was the view of the Corporation's General Counsel that the Bank for International Settlements was not clearly covered by the statute, but that the opposite position could be taken on the ground that coverage would be consistent with the intent and purposes of the statute.

Attached to Mr. Hackley's memorandum was a second memorandum dated October 24, 1962, discussing in detail the question whether or not the recent legislation covered the Bank for International Settlements. The amendment to section 19 accorded exemption from interest rate limitations to three categories of institutions:

(1) Foreign governments;
(2) Monetary and financial authorities of foreign governments when acting as such; and
(3) International financial institutions of which the United States is a member.

Obviously, the Bank for International Settlements was not a foreign government. Consequently, it would have to fall in either category (2) or category (3) in order for its time deposits to be exempt from

interest rate ceilings. Whether there was reasonable ground for coverage of the institution under either category would seem to depend upon whether its organization, powers, and functions were such as to bring it within the language of the statute.

The memorandum then explored in some detail the purposes, history, organization, and nature of the Bank for International Settlements. It seemed clear that the Bank was an "international financial institution." Therefore, it seemed appropriate to inquire whether the United States was a "member" of the Bank. Examination of this aspect of the matter led to the conclusion that, while it might be assumed that the United States could become a "member" of the Bank for International Settlements for purposes of Public Law 87-827, it was not now a member.

The memorandum next weighed the question whether the Bank for International Settlements acts as a monetary or financial authority of foreign governments, presenting a number of arguments on each side of that question. After considering those arguments, Mr. Hackley's opinion was that, as a legal matter, the arguments against classifying the Bank for International Settlements as a monetary or financial authority of foreign governments were more supportable in logic and in the light of the language of the statute than those in favor of coverage.

At the beginning of the discussion at this meeting, Mr. Hackley summarized the elements bearing upon the issue. In response to a question by Chairman Martin as to whether it would make a real difference in the situation if the Federal Reserve were technically a member of

the Bank for International Settlements, he expressed the belief that it would. The statutes of the Bank, as they now stood, cited the Federal Reserve Bank of New York rather than the Board of Governors as the central bank of the United States. If the statutes were amended, the Federal Reserve could become a member of the Bank and that institution, in his judgment, then would fall within the third category of institutions mentioned in the amendment to section 19 of the Federal Reserve Act.

Mr. Hackley noted that a principal argument for considering that the Bank for International Settlements might qualify for inclusion within the second category, "monetary and financial authorities of foreign governments when acting as such", was that central banks of certain European countries held 75 per cent of the Bank's stock and participated in its management. The governors of the central banks were directors and could designate other directors. The Bank maintained an account with the New York Reserve Bank, and it bought and sold gold from and to the United States Treasury. Ninety per cent of the Bank's deposits were deposits of central banks. Private interests held 25 per cent of the Bank's stock and 10 per cent of its deposits; yet it was plausible that the Bank for International Settlements would always act in its official capacity regardless of its private interest participation. In the light of these facts, it could be argued that the Bank operated as a monetary and financial authority of foreign governments.

In continuing, Mr. Hackley expressed the view, however, that the phrase "monetary and financial authorities of foreign governments"

would normally be construed as referring to treasuries and central banks. To construe it to include the Bank for International Settlements would seem to go beyond the normal meaning of the words. He went on to say that the legislative history of the amendment to section 19 clearly indicated its purpose, namely, to encourage foreign authorities to hold balances in dollars and not convert them into gold - a purpose that would be facilitated by an affirmative determination as to the Bank for International Settlements. Yet the legislative history did not contain anything particularly conclusive as to whether the Bank was intended to be covered. There had been statements that the amendment was meant to include foreign agencies that were authorized to buy gold from the United States. However, the hearings contained testimony that the Federal Reserve was not a member of the Bank for International Settlements.

After further comments, Mr. Hackley concluded by observing that arguments could be made on both sides of the question. He would not want to give the impression that he had any strong feeling. While he had come to the conclusion that the better legal arguments were on the side of holding that the Bank for International Settlements was not covered by the recent legislation, attorneys for the Treasury and the New York Reserve Bank, although recognizing that the matter was not clear, were inclined to reach a different conclusion. If the Board should be disposed to take the position that the Bank for International Settlements was not covered, it would seem desirable, before reaching a final decision, to consult further with the Treasury and the Federal

Deposit Insurance Corporation, and possibly with the Bank for International Settlements itself. If the Board should be disposed to take the position that the Bank was covered, that position might be stated in the form of a communication to President Holtrop--of which copies could be sent to the Federal Reserve Banks--stating that in light of the general purposes of the legislation and the organization and functions of the Bank, the Board had concluded that the statute was susceptible of a construction that the term "monetary and financial authorities of foreign governments" included the Bank, and therefore the Bank's time deposits with United States banks would be covered by the statute.

Following additional discussion of the organization and functions of the Bank for International Settlements, Chairman Martin expressed the view that the problem came down to whether the Board could construe the language of the statute in such a way as to accord with the obvious intent. He observed that the Federal Reserve, even though not technically a member, had been using the facilities of the Bank for International Settlements rather freely in a number of ways. Also, 90 per cent of the Bank's deposits were deposits of central banks. Further, the amendment to section 19 was temporary legislation, limited to three years and directed toward a current emergency. In these circumstances, Chairman Martin considered that the Board should try to do as much as it could to be helpful. If there were a clear unanimity of legal opinion, that would be one thing, but there was not.

Governor King expressed surprise that a problem such as this should have arisen so soon after passage of the legislation. Faulty drafting was indicated and, although he would like to be cooperative, there was a question in his mind whether the Board should be called upon to rectify the matter through interpretation at the risk of possible criticism.

Responses indicated that it had apparently been assumed by all the proponents of the legislation that the Bank for International Settlements was covered. Therefore, it had not been detected that the language of the amendment, if strictly interpreted, might not include the Bank. Certainly, this possibility had never occurred to the Board's staff when the proposed legislation was reviewed.

Governor Mitchell expressed the opinion that in the circumstances the sensible thing to do was to interpret the statute so as to make it possible for its privileges to be enjoyed by the Bank for International Settlements. Further, it should be made clear to everyone that it was the Board, rather than the Treasury or the New York Bank, that was making the interpretation.

On the latter point, Chairman Martin expressed the belief that it was clearly understood that the decision was one for the Board to make. This had been recognized by President Holtrop in telephone conversation.

Governor Shepardson stated that as a practical matter, having in mind the intent of the legislation, it seemed to him entirely appropriate

to take the position that the statute was susceptible to the interpretation that the Bank for International Settlements was included. The Federal Reserve had made use regularly of the Bank's facilities, insofar as the System found it convenient to use such facilities, even if not technically a member. Had he been asked when the legislation was under consideration, he would have said that he assumed the Bank was covered by it. In all the circumstances, he thought the suggested interpretation was justifiable.

After further discussion, the Board adopted the position that the October 15, 1962, amendment to section 19 of the Federal Reserve Act was susceptible of the interpretation that the Bank for International Settlements was included in its coverage. Governor King asked that the record show that, while he went along with this position, he did so because the legislation was limited to three years, after which the legislation, if extended, could be clarified. Governor Robertson abstained from participation in the matter, on the ground that, having just returned from travel abroad, he had not had an opportunity to study the question fully.

A copy of the cablegram sent later in the day to President Holtrop of the Bank for International Settlements conveying the position of the Board is attached as Item No. 10. (Before the cablegram was sent, Mr. Hackley informed the Federal Deposit Insurance Corporation of the position the Board had taken.) A copy of a letter of October 25, 1962, informing the Presidents of the Federal Reserve Banks of the Board's position is attached as Item No. 11.

Secretary's Note: An interpretation reflecting the Board's decision was subsequently published in the Federal Register and the Federal Reserve Bulletin.

Israel Discount Bank. At its meeting on September 27, 1962, the Board considered further an inquiry as to whether the New York City branch of Israel Discount Bank Limited, Tel Aviv, Israel, might be regarded eligible, under the first paragraph of section 13 of the Federal Reserve Act, for a nonmember clearing account. The Board's conclusion was that a Reserve Bank was not precluded by the language of the statutes from opening and maintaining a nonmember clearing account for a domestic branch of a foreign commercial bank. President Hayes was informed of this view in a letter dated September 28, 1962. Subsequently, President Hayes addressed a letter to the Board on October 9, 1962, enclosing a memorandum in which the Bank's counsel reiterated the view that the language of the statute cast serious doubt on the legal authority of a Reserve Bank to open such an account. At this meeting several members of the Board referred to this further communication from the Federal Reserve Bank of New York, and it was suggested that the Board give prompt consideration to it. It was understood that the matter would be placed on the agenda at an early date.

The meeting then adjourned.

Secretary's Note: Pursuant to recommendations contained in memoranda from appropriate individuals concerned, Governor Shepardson today approved on behalf of the Board the following actions relating to the Board's staff:

Temporary employment

Modification of the employment status of Stuart H. Altman, whose appointment as Economist was approved by the Board on September 10, 1962, to provide for employment for an initial period of approximately 18 months, notwithstanding his failure to pass a physical examination based on the requirements for ordinary life insurance at normal rates, with the understanding that the question of continued employment would be considered at the end of the 18-month period.

Salary increases, effective October 28, 1962

Betty B. Schieman, Statistical Assistant, Division of Research and Statistics, from $4,885 to $5,045 per annum.

Bishop Hart, Bindery Worker, Division of Administrative Services, from $5,429 to $5,720 per annum.

Advance of sick leave

Boris C. Swerling, Senior Economist, Division of International Finance, up to 26 days of sick leave effective from October 8, 1962.

Secretary

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

Item No. 1
10/25/62

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

October 25, 1962.

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

Gentlemen:

The Board of Governors of the Federal Reserve System approves the establishment by Union Bank, Los Angeles, California, of a branch in the vicinity of the intersection of Ninth and Main Streets, Los Angeles, California, provided the branch is established within six months from the date of this letter.

The Board notes that Union Bank plans to increase its capital structure by from $15 million to $18 million in 1963.

Very truly yours,

(Signed) Kenneth A. Kenyon

Kenneth A. Kenyon,
Assistant Secretary.

TELEGRAM
LEASED WIRE SERVICE

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON

Item No. 2
10/25/62

October 25, 1962.

Helmer - Chicago

Board interposes no objection to your proposal for rental of second complement of electronic check processing equipment at Head Office as outlined in your letter October 11, 1962.

(Signed) Merritt Sherman

Sherman

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Item No. 3
10/25/62

Office Correspondence

To Board of Governors

From J. E. Kelleher

Date October 12, 1962

Subject:

On September 10, 1962, the Conference of Presidents of the Federal Reserve Banks approved a recommendation of the Subcommittee on Cash Leased Wire and Sundry Operations for the acceptance of a proposal from the General Services Administration by which the Federal Reserve System would be afforded the economies of multiple group communication tariffs offered by the American Telephone and Telegraph Company and administered by the General Services Administration. It is estimated that an annual savings of $55,000 would be effected in line rental charges for the System's leased wire system.

The attached letter and agreement from the General Services Administration implements the proposal and is in the form approved by the Presidents Conference and has been reviewed by the Board's Legal Division. It is recommended that the agreement be executed on behalf of the Board and that appropriate advice be given to the Federal Reserve Banks.

(Signed) JEK

Attachment

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

Item No. 4
10/25/62

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

October 26, 1962.

Mr. W. D. Fulton, Chairman,
Conference of Presidents,
Federal Reserve Bank of Cleveland,
Cleveland 1, Ohio.

Dear Mr. Fulton:

Enclosed is a copy of a letter being sent to the Presidents of all the Federal Reserve Banks today informing them of the execution of a contract with General Services Administration, under which the Federal Reserve System would be afforded the economies of multiple group communications tariffs offered by the American Telephone and Telegraph Company. It will be noted that this agreement, acceptance of which was recommended in the Subcommittee report approved by the Conference of Presidents on September 10, 1962, is to become effective October 29.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.

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

Item No. 5
10/25/62

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

October 25, 1962.

The Board of Directors,
Citizens Bank & Trust Company,
Park Ridge, Illinois.

Attention Mr. Edward J. Reilly, President.

Gentlemen:

This refers to Mr. Reilly's letter of October 11, 1962, addressed to Mr. Paul C. Hodge of the Federal Reserve Bank of Chicago, requesting a further extension of the time for discontinuance of your bank's United Security Account plan.

The Board is aware of the hardship, particularly the loss of accrued interest, that would result if a depositor were forced immediately to close his account because of the elimination of the checking privilege. Therefore, the Board will not insist that the plan be discontinued prior to the end of this year, when the depositor will be entitled to receive interest for the six months' period from July 1st. However, this extension is given with the proviso that all depositors under the United Security Account plan be notified by December 1st that after December 31, 1962, no more checks may be drawn thereunder.

Very truly yours,

Merritt Sherman,
Secretary.

TITLE 12 - BANKS AND BANKING

Item No. 6
10/25/62

CHAPTER II - FEDERAL RESERVE SYSTEM

SUBCHAPTER A - BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

[Reg. T]

PART 220 - CREDIT BY BROKERS, DEALERS, AND MEMBERS OF NATIONAL SECURITIES EXCHANGES

§ 220.118 Time of payment for mutual fund shares purchased in a special cash account

(a) The Board has recently considered the question whether, in connection with the purchase of mutual fund shares in a "special cash account" under the provisions of Part 220, the 7-day period with respect to liquidation for nonpayment is that described in § 220.4(c)(2) or that described in § 220.4(c)(3).

(b) Section 220.4(c)(2) provides as follows:

> "In case a customer purchases a security (other than an exempted security) in the special cash account and does not make full cash payment for the security within 7 days after the date on which the security is so purchased, the creditor shall, except as provided in subparagraphs (3)-(7) of this paragraph, promptly cancel or otherwise liquidate the transaction or the unsettled portion thereof." (Emphasis supplied)

Section 220.4(c)(3), one of the exceptions referred to, provides in relevant part as follows:

> "If the security when so purchased is an unissued security, the period applicable to the transaction under subparagraph (2) of this paragraph shall be 7 days after the date on which the security is made available by the issuer for delivery to purchasers." (Emphasis supplied)

(c) In the case presented, the shares of the mutual fund (open-end investment company) are technically not issued at the time they are sold by the underwriter and distributor. Several days may elapse from the date of sale before a certificate can be delivered by the transfer

agent. The specific inquiry to the Board was, in effect, whether the 7-day period after which a purchase transaction must be liquidated or cancelled for nonpayment should run, in the case of mutual fund shares, from the time when a certificate for the purchased shares is available for delivery to the purchaser, instead of from the date of the purchase.

(d) Under the general rule of § 220.4(c)(2) that is applicable to purchases of outstanding securities, the 7-day period runs from the date of purchase without regard to the time required for the mechanical acts of transfer of ownership and delivery of a certificate. This rule is based on the principles governing the use of special cash accounts in accordance with which, in the absence of special circumstances, payment is to be made promptly upon the purchase of securities.

(e) The purpose of § 220.4(c)(3) is to recognize the fact that, when an issue of securities is to be issued at some fixed future date, a security that is a part of such issue can be purchased on a "when-issued" basis and that payment may reasonably be delayed until after such date of issue, subject to other basic conditions for transactions in a special cash account. Thus, unissued securities should be regarded as "made available for delivery to purchasers" on the date when they are substantially as available as outstanding securities are available upon purchase, and this would ordinarily be the designated date of issuance or, in the case of a stock dividend, the "payment date". In any case, the time required for the mechanics of transfer and delivery of a certificate is not material under § 220.4(c)(3) any more than it is under § 220.4(c)(2).

(f) Mutual fund shares are essentially available upon purchase to the same extent as outstanding securities. The mechanics of their issuance and of the delivery of certificates are not significantly different from the mechanics of transfer and delivery of certificates for shares of outstanding securities, and the issuance of mutual fund shares is not a future event in a sense that would warrant the extension of the time for payment beyond that afforded in the case of outstanding securities. Consequently, the Board has concluded that a purchase of mutual fund shares is not a purchase of an "unissued security" to which § 220.4(c)(3) applies, but is a transaction to which § 220.4(c)(2) applies.

(15 U.S.C. 78w)

Dated at Washington, D. C., this 25th day of October, 1962.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

(SEAL)

Merritt Sherman,
Secretary.

UNITED STATES OF AMERICA

BEFORE THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

WASHINGTON, D. C.

In the Matter of the Application of
VIRGINIA COMMONWEALTH CORPORATION
for permission to become a bank holding company by acquiring stock of five banks in Virginia

ORDER APPROVING APPLICATION UNDER
BANK HOLDING COMPANY ACT

There has come before the Board of Governors, pursuant to section 3(a)(1) of the Bank Holding Company Act of 1956 (12 U.S.C. 1842) and section 4(a)(1) of the Board's Regulation Y (12 CFR 222.4(a)(1)), an application by Virginia Commonwealth Corporation, Richmond, Virginia, for the Board's prior approval of action whereby Applicant would become a bank holding company through the acquisition of more than 50 per cent of the voting shares of The Bank of Virginia, Richmond, Virginia, The Bank of Henrico, Sandston, Virginia, The Bank of Salem, Salem, Virginia, The Bank of Occoquan, Occoquan, Virginia, and the Bank of Warwick, Newport News, Virginia.

As required by section 3(c) of the Act, the Board notified the Commissioner of Banking for the State of Virginia of the receipt of the application and requested his views. The Commissioner stated in writing that his office knew of no reason why it should not be approved.

Notice of receipt of said application was published in the Federal Register on May 18, 1962 (27 F. R. 4748), which notice provided an opportunity for the filing of comments and views regarding the proposed acquisitions, and the time for filing such comments and views has expired and all comments and views filed with the Board have been considered by it.

IT IS HEREBY ORDERED, for the reasons set forth in the Board's Statement of this date, that the said application be and hereby is granted, and the acquisition by Applicant of more than 50 per cent of the voting shares of the above-mentioned banks is hereby approved, provided that such acquisition shall not be consummated (a) within seven calendar days after the date of this Order or (b) later than three months after said date.

Dated at Washington, D. C., this 25th day of October, 1962.

By order of the Board of Governors.

Voting for this action: Chairman Martin, and Governors Balderston, Mills, Shepardson, and King.

Absent and not voting: Governors Robertson and Mitchell.

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.

(SEAL)

BOARD OF GOVERNORS

OF THE

FEDERAL RESERVE SYSTEM

Item No. 8
10/25/62

APPLICATION BY VIRGINIA COMMONWEALTH CORPORATION
FOR PERMISSION TO BECOME A BANK HOLDING COMPANY

STATEMENT

Virginia Commonwealth Corporation, Richmond, Virginia ("Applicant"), has applied, pursuant to section 3(a)(1) of the Bank Holding Company Act of 1956 ("the Act"), for the Board's prior approval of action that would result in Applicant becoming a bank holding company - namely, acquisition of more than 50 per cent of the voting shares of The Bank of Virginia, Richmond, Virginia, with deposits of $151 million;* The Bank of Henrico, Sandston, Virginia ("Henrico"), with deposits of $3.2 million; The Bank of Salem, Salem, Virginia ("Salem"), with deposits of $8.9 million; The Bank of Occoquan, Occoquan, Virginia ("Occoquan"), with deposits of $6.4 million; and the Bank of Warwick, Newport News, Virginia ("Warwick"), with deposits of $15.2 million.

* Unless otherwise indicated, deposit and loan figures herein stated are as of December 31, 1961.

The Bank of Virginia is the fourth largest bank in the State and would be the principal bank in the proposed holding company system. With control of that bank and the four smaller banks, the group would still rank fourth in total deposits, although very close in size to the National Bank of Commerce, of Norfolk, which would retain third place.

The Bank of Virginia has 19 offices distributed in five areas, in the Richmond metropolitan area, in Petersburg, in Norfolk, in Newport News, and in Roanoke. Acquisition of the bank in Occoquan would give Applicant representation in the northern part of the State.

A chief admitted advantage to Bank of Virginia from the formation of the proposed holding company system arises out of statutory restrictions on further branching in Virginia. All of that Bank's branches were acquired before a "freeze" imposed by the State legislature in 1948. In 1962, the restriction was relaxed somewhat, but only to permit city banks to establish additional branches in the city where the head office of the bank is located (in this case, in Richmond), or within five miles of the city limits. As a result, Bank of Virginia can only establish more branches in the remaining areas of the State where it now has interests, or in other areas, through mergers.

Statutory factors. - Section 3(c) of the Act requires the Board to take into consideration the following five factors: (1) the financial history and condition of the holding company and the banks concerned; (2) their prospects; (3) the character of their management; (4) the convenience, needs, and welfare of the communities and area concerned; and (5) whether or not the effect of the acquisitions would be to expand the size or extent of the bank holding company system involved beyond limits consistent with adequate and sound banking, the public interest, and the preservation of competition in the field of banking.

Banking factors. - The financial history, condition, prospects, and management of the five banks are satisfactory, as are the proposed financial structure, proposed management, and prospects of the Applicant. Virginia Commonwealth Corporation was incorporated as a Virginia corporation on January 11, 1962, for the purpose of acquiring more than 50 per cent of the outstanding shares of, and furnishing services to, the banks proposed to be acquired by it. Its management is to be made up largely of officers of the banks involved, who are regarded as competent.

The Bank of Virginia was organized in 1922, as a Morris Plan bank. Ten of its branches and two facilities are located in the Richmond metropolitan area, three branches in Norfolk, and one branch each in Portsmouth, Petersburg, Roanoke, and Newport News. As of December 31, 1961, Bank of Virginia had loans of $93 million.

Henrico was organized in 1957, with major assistance from Bank of Virginia. It now operates two branches, and the Virginia State Corporation Commission has authorized the opening of an additional branch. It offers general commercial banking other than trust services, and had $2.4 million of loans on December 31, 1961.

Occoquan has its main office in the town of Occoquan, and has three branches, all within Prince William County, about 75 to 85 miles north of Richmond. It is the third largest of the five banks located in that county. The bank and its branches are situated between Washington, D. C., and Quantico, and the area is predominantly residential. It has loans of $3.8 million.

Salem was organized in 1891. The bank did not operate any branches until 1961 when it established a branch in a shopping center in Roanoke County adjacent to the city of Roanoke. Loans outstanding total $6 million.

Warwick was organized in 1941 in what was then the town of Hilton Village in Warwick County. Subsequently the county became an incorporated city, and later was consolidated with the city of Newport News. Warwick operates two branches in Newport News and has made application for a branch to be located in adjacent York County. Its total loans amount to $7.5 million.

As to the prospects of the proposed holding company, Applicant argues that a notable economic surge forward which Virginia has made in recent years requires, and will require, stronger banking sources, and that creation of the bank holding company system will help

provide such sources with a corresponding opportunity for growth of the five banks as well as of Applicant. In this connection, Applicant contends that the holding company will better be able to raise the capital needed to keep pace with industrial expansion in the State than could the individual banks.

It does not appear to the Board that it would be substantially easier for the banks to raise capital through the holding company system, as apparently none of the banks has experienced difficulty in the past in floating new issues of stock when needed. On the other hand, basically, additional capital is justified by deposit growth, and to the extent that general improvements in management and efficiency of the subsidiary banks promoted deposit growth, their prospects would be improved.

Ready access to the automated equipment already installed by Bank of Virginia should also improve the operating efficiency of the small banks and facilitate their growth, thus improving their prospects.

Turning to the third factor, the character of the management of the Applicant and the banks concerned, it appears that Bank of Virginia has for some years maintained a strong training program. Through the extension of this program, Applicant argues, it will be able to supply the smaller banks with officers who are more qualified than those which the banks individually could attract or develop.

Against this contention, it can be urged that, on Applicant's own showing, the present management of all the banks is satisfactory, and there is no reason to suppose, except in the case of one of them, which has recently had a management succession problem, that they will be unable to attract capable officers in the future. Despite past performance in this regard, however, it would appear that since Applicant will be able to place officers from the smaller banks for periods of training in the more specialized departments of the large bank, and can offer executives of the smaller banks better opportunities of promotion, an advantage would accrue to the smaller banks under this factor.

Convenience and needs of communities. - The fourth factor, the convenience, needs, and welfare of the communities and the areas concerned, is of course intimately interwoven with the first three. Additional arguments which have been brought forward under the fourth factor include the fact that Bank of Virginia has a sizable and active trust department, and Applicant plans to make expert advice and guidance in the trust field available to the smaller banks, although it does not propose to establish trust departments in the three which have none. A second point made by Applicant is that the greater ease of arranging participations within the holding company system would have the effect of raising the effective (although not the legal) lending limit of its subsidiary banks.

While the contemplated guidance on trust matters would be of some assistance to the smaller banks and to their communities, the

scale of their future operations will probably not justify much trust activity. As to the second point, the smaller banks have been able to arrange participations with correspondent banks, particularly with Bank of Virginia, when needed, and should be able to continue doing so were they to remain independent of the system.

Competitive effect. - The final factor, whether the effect of the proposed transaction would be to expand the size or extent of the bank holding company involved beyond limits consistent with adequate and sound banking, the public interest, and the preservation of competition in the field of banking, is more difficult to analyze. However, the Board is of the opinion that the proposed holding company system will remain well within limits consistent with adequate and sound banking, and so far, will be consistent with the public interest.

Applicant's banks would have about 5 per cent of the offices and deposits of all banks in the State. In the areas where more than one of the proposed subsidiaries have offices, the group's proportion of deposits would be about 10 per cent in the case of the Roanoke and Salem banks and 11 per cent of banks in the Richmond metropolitan area. In Newport News, the subsidiary banks would have about 26 per cent of combined bank deposits, considerably less than that of the largest bank in the city. The merger of that bank with First and Merchant's National Bank of Richmond, on October 31, 1962, will make it a branch of the largest bank in the State.

On the question whether there will be a significant lessening of competition in the field of banking as a result of approval, the Department of Justice has urged that

> "The proposed formation of a holding company, which standing alone may appear of not too great significance, may actually be the incipient step which will trigger other and more substantial conglomerations resulting in Virginia banking in every community being dominated by a small number of large holding companies with a consequent diminution in the number of smaller, locally controlled banks."

The Board agrees with the inference in the statement by the Department of Justice that the lessening of present competition which is likely to result from the proposed acquisitions is not sufficient to require denial of the application. Occoquan is about 85 miles from Richmond, and there is no existing competition between Occoquan and Bank of Virginia. In the case of Henrico, the close relationship with Bank of Virginia, as well as the location of Henrico in suburbs of the city, where the larger bank is not represented, has forestalled the development of competition between them.

In the case of Salem, Applicant urges with some reason that the degree of existing competition with the Roanoke branch of Bank of Virginia is slight and due to special, self-terminating factors.

As to Warwick, the $1.05 million of deposits and $.9 million of loans of Bank of Virginia's Newport News branch which originate in the primary service area of Warwick are equivalent to 6.9 per cent of the deposits and 12.2 per cent of the loans of the Bank of Warwick. The

deposits and loans of Warwick which originate in the primary service area of Bank of Virginia's branch are less significant from the competitive point of view, as five commercial depositors, two of whom are directors of Warwick, account for about $.3 million of the $.35 million of such deposits, and three commercial customers, two of whom are directors, account for about 85 per cent of the $.2 million of such loans.

In addition, the size and number of alternative banking sources which would remain would tend to mitigate the lessening of competition which can be expected to result from approval.

The statement that approval of this application will "trigger other and more substantial conglomerations", as urged by the Department of Justice, seems to imply that approval will in some fashion commit the Board to approving future applications. But it is the statutory duty of the Board to determine the point at which a line should be drawn, deterring further concentration of banking facilities, and it has done so. In one recent case, the matter of the application of Morgan New York State Corporation, where the proposed system would have included the fifth largest bank in New York City, and six of the largest banks in the respective upstate New York areas, thus widening the competitive gap between the larger and the smaller banks in the cities concerned, the Board found that this prospective result compelled the conclusion that formation of the holding company would have adverse consequences for the competitive banking structure of the State and required denial. (48 Federal Reserve Bulletin 567, May 1962)

Approval of the application of First Bancorporation of Florida similarly would have united four powerful banks already "strongly entrenched" in the State's four largest metropolitan areas. The Board found that since "Among relatively large and aggressive banks competing for the business of sophisticated customers such as other banks, small advantages can be decisive", it was "probable that the competitive ability of the remaining major correspondent banks would be seriously diminished" and denied the application. (48 Federal Reserve Bulletin 979 at 982, August 1962)

By contrast, the proposed holding company would not be the dominant banking institution in any area in which it operated. Four of the banks are relatively small, and there would be no change in the relative rank of the principal State banking organizations as a result of approval.

While the shoe industry is, of course, different from the banking industry, it may be relevant to note that in its recent decision in Brown Shoe Co. v. United States, the Supreme Court found that supporters of the 1954 amendment to section 7 of the Clayton Act "indicated that it would not impede, for example, a merger between two small companies to enable the combination to compete more effectively with larger corporations dominating the relevant market" and held that "Congress indicated plainly that a merger had to be functionally viewed, in the context of its particular industry." Indeed, the

Court described as a "mitigating factor" a "demonstrated need for combination to enable small companies to enter into a more meaningful competition with those dominating the relevant markets." (370 U.S. 294 at 319, 321-322, 346 (June 25, 1962)) In the present case, uniting the four smaller banks with Bank of Virginia should enable all these banks to compete more effectively, both with the larger banks in their own areas and with the powerful Richmond and out-of-state banks which are now active in the Virginia banking field. Nor under all the circumstances does it appear that the remaining smaller independent banks would be adversely affected.

Viewing the relevant facts in the light of the general purposes of the Act and the factors enumerated in section 3(c), as well as the cited opinion of the Supreme Court, it is the judgment of the Board that the proposed acquisitions would be consistent with the statutory objectives and the public interest and that the application should be granted.

October 25, 1962

Item No. 9
10/25/62

TELEGRAM
LEASED WIRE SERVICE

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON

October 25, 1962.

Rudy - Dallas

Reference your telephone conversation earlier today with Mr. Shay concerning whether the Board has objection to the appearance by Federal Reserve Examiner William C. Reddick, Jr., pursuant to a subpoena to testify on Monday, October 29 at Corpus Christi, Texas, at the trial of criminal charges that arose following the December 1961 examination of First State Bank, Premont, Texas. It is understood that the United States Attorney has indicated that Mr. Reddick will be expected to testify with respect to the disappearance from the vault of the bank during the aforementioned examination of five promissory notes. You related in addition that Mr. Reddick might be directed during his testimony to furnish in open court a copy of his memorandum to Vice President Pondrom of your Bank, a copy of which was enclosed with Mr. Pondrom's letter to Mr. Solomon of January 19, 1962. You are advised that the Board will interpose no objection to Mr. Reddick's appearance and testimony in pursuance of the aforementioned subpoena, and to furnish a copy of the aforementioned memorandum if directed to do so as outlined herein.

(Signed) Merritt Sherman

Sherman

TELEGRAM
BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

Item No. 10
10/25/62

October 25, 1962

M. W. Holtrop, President,
Bank for International Settlements,
Basle, Switzerland.

This is in response to your recent telephone inquiry to me regarding status of B.I.S. under Public Law 87-827, approved October 15, 1962, regarding rates of interest payable by member banks on time deposits of certain foreign and international institutions. In light of general purposes of that statute and nature of organization and functions of B.I.S., Board has concluded that phrase "monetary and financial authorities of foreign governments" is susceptible of construction as including B.I.S. and that therefore time deposits of B.I.S. when acting in such capacity would be covered by that statute.

(signed) William McC. Martin, Jr.

Martin
Fedreserve

4100

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

S-1844

Item No. 11
10/25/62

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

October 25, 1962.

Dear Sir:

For your information and guidance, there is set forth below the text of a telegram sent today by Chairman Martin to Dr. Holtrop, President of the Bank for International Settlements, in response to a recent telephone call from Dr. Holtrop to the Chairman regarding the question whether time deposits of the B.I.S. with member banks would be exempted from interest rate limitations under Public Law 87-827 approved October 15, 1962, amending section 19 of the Federal Reserve Act:

> This is in response to your recent telephone inquiry to me regarding status of B.I.S. under Public Law 87-827, approved October 15, 1962, regarding rates of interest payable by member banks on time deposits of certain foreign and international institutions. In light of general purposes of that statute and nature of organization and functions of B.I.S., Board has concluded that phrase "monetary and financial authorities of foreign governments" is susceptible of construction as including B.I.S. and that therefore time deposits of B.I.S. when acting in such capacity would be covered by that statute.

Very truly yours,

Merritt Sherman,
Secretary.

TO THE PRESIDENTS OF ALL FEDERAL RESERVE BANKS