

809
9/62

Minutes for December 17, 1962

To: Members of the Board

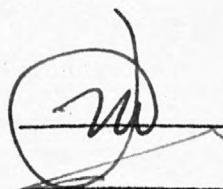
From: Office of the Secretary

Attached is a copy of the minutes of the Board of Governors of the Federal Reserve System on the above date.

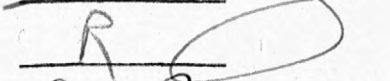
It is not proposed to include a statement with respect to any of the entries in this set of minutes in the record of policy actions required to be maintained pursuant to section 10 of the Federal Reserve Act.

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.

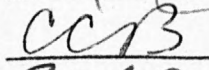
Chm. Martin



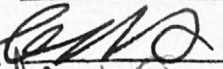
Gov. Mills



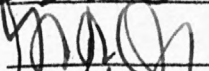
Gov. Robertson



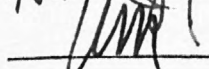
Gov. Balderston



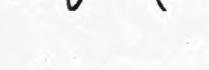
Gov. Shepardson



Gov. King



Gov. Mitchell



Minutes of the Board of Governors of the Federal Reserve System on Monday, December 17, 1962. The Board met in the Board Room at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Balderston, Vice Chairman
Mr. Robertson
Mr. Shepardson
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. Spencer, General Assistant, Office
of the Secretary

Messrs. Noyes, Garfield, Holland, Koch,
Williams, Dembitz, Eckert, Gehman,
Partee, Solomon, Yager, Freedman,
Trueblood, and Wernick of the Division
of Research and Statistics

Messrs. Furth, Hersey, Sammons, Katz, Wood,
Irvine, Gekker, Klein, Maroni, Reynolds,
and Swerling of the Division of International
Finance

Economic review. The Divisions of International Finance and Research and Statistics presented a review of recent foreign and domestic economic and financial developments.

All members of the staff except Messrs. Sherman, Kenyon, and Spencer then withdrew and the following entered the room:

Mr. Hackley, General Counsel
Mr. Farrell, Director, Division of Bank
Operations
Mr. Solomon, Director, Division of
Examinations

12/17/62

-2-

Mr. O'Connell, Assistant General Counsel
 Mr. Potter, Senior Attorney, Legal Division
 Mr. Collier, Chief, Current Series Section,
 Division of Bank Operations

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

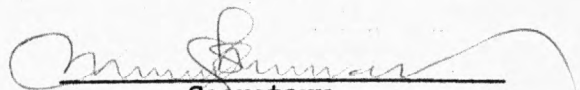
	<u>Item No.</u>
Letter to the Federal Reserve Bank of Boston waiving the assessment of a penalty incurred by Franklin County Trust Company, Greenfield, Massachusetts, because of a deficiency in its required reserves.	1
Letter to the Federal Reserve Bank of Cleveland approving the appointment of James D. Kelly as Assistant Federal Reserve Agent.	2
Letter to The Farmers and Merchants State Bank, Oldenburg, Indiana, approving the declaration of a dividend in December 1962.	3
Letter to Muscatine Bank and Trust Company, Muscatine, Iowa, approving the declaration of a dividend in December 1962.	4
Letter to The Farmers and Merchants State Bank, Colby, Kansas, granting permission to exercise additional fiduciary powers.	5
Letter to the Federal Reserve Bank of Dallas regarding use of a Federal radio transmitting frequency at the Bank's head office and branches for communication between the armored cars and guard headquarters.	6
Letter to the Federal Reserve Bank of St. Louis regarding possible violations of section 6 of the Bank Holding Company Act involved in loan participations among certain subsidiaries of General Bancshares Corporation, St. Louis, Missouri, (with the understanding that copies of the letter would be sent to the Federal Reserve Banks, the Comptroller of the Currency, and the Federal Deposit Insurance Corporation.)	7

12/17/62

-3-

In the course of commenting upon Item No. 7, Mr. Potter reviewed a memorandum that he had received from Governor Mills in which agreement was expressed with the reply being made to the Federal Reserve Bank of St. Louis. Governor Mills expressed serious concern about a practice whereby a bank holding company would develop a large volume of consumer instalment loans and allocate such paper among its subsidiary banks, since he felt that this practice was likely to emphasize earnings advantages to the detriment of the solvency standards of those banks and their ability to serve the legitimate credit needs of local communities. In his (Governor Mills') view, however, such objections appeared to be largely obviated in the instant case by limiting the intersubsidiary participations to new loans rather than outstanding loans.

The meeting then adjourned.


Secretary

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

Item No. 1
12/17/62



ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

December 17, 1962

Mr. Earle O. Latham,
First Vice President,
Federal Reserve Bank of Boston,
Boston, Massachusetts.

Dear Mr. Latham:

This refers to your letter of November 30, 1962, regarding the penalties of \$64.01 and \$64.15 incurred by the Franklin County Trust Company, Greenfield, Massachusetts, on deficiencies in its reserves during the bi-weekly computation periods ending February 21 and March 7, 1962, respectively.

It was noted that the deficiencies resulted from a misunderstanding by the clerk who computes the bank's reserve position regarding the proper treatment of federal funds sold which were treated as due from banks and as a deduction item; that although this occurred in six periods, it resulted in deficiencies in only two; that the bank has had an excellent reserve record in the past; and that the penalty of \$64.01 for the period ended February 21 can be waived by your Bank under the provision of Paragraph E of the Board's instructions (S-1123; FRIS #6120).

In the circumstances, the Board authorizes your Bank to waive the assessment of \$64.15 penalty for the reserve period ended March 7, 1962.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.

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

Item No. 2
12/17/62

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

December 17, 1962



Mr. Joseph B. Hall,
Chairman of the Board and
Federal Reserve Agent,
Federal Reserve Bank of Cleveland,
Cleveland 1, Ohio.

Dear Mr. Hall:

In accordance with the request contained in your letter of November 26, 1962, the Board of Governors approves the appointment of Mr. James D. Kelly as Assistant Federal Reserve Agent at the Federal Reserve Bank of Cleveland to succeed Mr. Clifford G. Miller, who is being promoted to official status.

This approval is given with the understanding that Mr. Kelly will be solely responsible to the Federal Reserve Agent and the Board of Governors for the proper performance of his duties, except that, during the absence or disability of the Federal Reserve Agent or a vacancy in that Office, his responsibility will be to the Board of Governors.

When not engaged in the performance of his duties as Assistant Federal Reserve Agent Mr. Kelly, may, with the approval of the Federal Reserve Agent and the President, perform such work for the Bank as will not be inconsistent with his duties as Assistant Federal Reserve Agent.

It will be appreciated if Mr. Kelly is fully informed of the importance of his responsibilities as a member of the staff of the Federal Reserve Agent and the need for maintenance of independence from the operations of the Bank in the discharge of these responsibilities.

It is noted from your letter that, upon the approval of the appointment of Mr. Kelly by the Board of Governors, he will execute the usual Oath of Office which will be forwarded to the Board giving the effective date of his appointment.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.

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

Item No. 3
12/17/62

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD



December 17, 1962

Board of Directors,
The Farmers and Merchants State Bank,
Oldenburg, Indiana.

Gentlemen:

The Board of Governors has received a copy of a letter dated December 3, 1962, written by Mr. Howard R. Heppner, Cashier of The Farmers and Merchants State Bank, to Mr. Hugh J. Helmer, Vice President of the Federal Reserve Bank of Chicago, requesting approval for the declaration of a dividend of \$750 in December 1962. The permission of the Board is required under the provisions of paragraph 6, Section 9 of the Federal Reserve Act and Section 5199(b), United States Revised Statutes.

After consideration of the facts, the Board approves the declaration of this dividend. This letter does not authorize any other declaration of dividends during 1962 or later.

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
12/17/62



ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

December 17, 1962

Board of Directors,
Muscatine Bank and Trust Company,
Muscatine, Iowa.

Gentlemen:

The Board of Governors has been advised by the Federal Reserve Bank of Chicago that Muscatine Bank and Trust Company in a letter dated November 29, 1962, requested approval for the declaration of a dividend of \$37,500 in December 1962 and payable in January 1963. The permission of the Board for the declaration of this dividend is required by the provisions of paragraph 6, Section 9 of the Federal Reserve Act and Section 5199(b), United States Revised Statutes.

The Federal Reserve Bank has advised the Board that dividends totaling \$287,500 have already been paid in 1962 in contravention of the laws noted above. These dividend payments apparently were pursuant to a policy of reducing total capital funds to an amount which it is understood the Board of Directors believes to be consistent with the capital needs of the bank. The present dividend program has brought about an approximate net reduction in capital funds and reserves of \$377,988 during the three years 1960 to 1962, inclusive, when dividends of \$900,000 (including \$37,500 for which approval is presently requested) will have been paid, providing no net retained earnings in the capital accounts. It would now seem to be appropriate for the directors to give consideration to a change in the dividend paying program, making provision for the future growth of capital funds through sound retention of earnings in order to provide for possible increases in deposits and risk assets.

This letter authorizes a declaration of a dividend in December 1962 of \$37,500 only and does not authorize any other declaration of dividends in 1962 or later.

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
12/17/62

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

December 17, 1962

Board of Directors,
The Farmers and Merchants State Bank,
Colby, Kansas.

Gentlemen:

This refers to your request for permission, under applicable provisions of your condition of membership numbered 1, to exercise additional fiduciary powers.

Following consideration of the information submitted, the Board of Governors of the Federal Reserve System grants permission to The Farmers and Merchants State Bank to exercise all other fiduciary powers now or hereafter authorized by its Articles of Incorporation and the laws of the State of Kansas, in addition to permission granted by the Board on November 7, 1958, to exercise limited fiduciary powers.

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
12/17/62



ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

December 17, 1962

Mr. Watrous H. Irons,
President,
Federal Reserve Bank of Dallas,
Dallas 2, Texas.

Dear Mr. Irons:

Reference is made to the correspondence between Mr. Pritchett of your Bank and Mr. Massey of the Board's staff, particularly the former's letter of October 25, 1962, in the matter of obtaining a Federal radio transmitting frequency for a more effective system of communication, at each of your four offices, between your armored cars and guard headquarters.

Enclosed is a copy of a letter dated December 6, 1962, from Mr. D. C. Spitz, Alternate Treasury Department Representative of Interdepartment Radio Advisory Committee, indicating approval of an application on behalf of the Federal Reserve System for such a frequency for use by your Bank. This will be your authority to use the radio frequency as set out and according to the particulars in that letter.

You will note that this authorization includes the use of this frequency at your relocation center in Denton, Texas, if it should be needed there in order to communicate with your armored cars between that point and Dallas. Please note particularly the reference to the situation at Houston and advise the Board of any interference between your facility and the one already in use by the National Aeronautics and Space Administration.

Please also advise the Board of the date on which the use of this facility begins at each of your offices and when any change is desired in this authorization.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

WASHINGTON 25, D. C.

Item No. 7
12/17/62

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

December 20, 1962

Mr. Orville O. Wyrick, Vice President,
Federal Reserve Bank of St. Louis,
St. Louis 66, Missouri.

Dear Mr. Wyrick:

This refers to Mr. Kroner's letter of November 17, 1961, with enclosures, including a memorandum by your Bank's Counsel, Mr. Dunne, concerning possible violations of section 6 of the Bank Holding Company Act ("the Act") disclosed in reports of examination by the Federal Deposit Insurance Corporation of The Baden Bank of St. Louis ("Baden") and the Jefferson-Gravois Bank of St. Louis ("J-G"). The possible violations involve participation by the above-named banks in certain loans originated by the Commercial and Industrial Bank ("C&I"), Memphis, Tennessee, all three banks being subsidiaries of General Bancshares Corporation ("General Bancshares"), St. Louis, a registered bank holding company.

The Board of Governors has considered the questions (1) whether the provisions of the form of "Loan Participation Agreement" used by the banks are consistent with section 6(a)(4) of the Act, and (2) whether the standards followed for determining loans eligible for participation under said Agreements are consistent with section 6(a)(4). The Board is of the opinion (1) that the general procedures established under the Agreements for handling the participations, apart from the question of proper selection of "new" loans, do not contravene the prohibitions of section 6(a)(4), and (2) that the standards for selection of eligible "new" loans are in need of correction, as indicated below.

The Loan Participation Agreement and procedures thereunder. - The Loan Participation Agreement form enclosed with Mr. Kroner's letter to the Board sets up a general procedure to be followed on a routine basis, whereby the Memphis bank (C&I) will from time to time tender to the St. Louis bank (in this case J-G), by telephone or telegram, participations of 75 per cent in personal loans made by C&I, each loan to be identified by the name of the borrower and the face amount of the note as "minimum information". This tender is to be made "before loan

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

Mr. Orville O. Wyrick

-2-

proceeds are disbursed to borrower", and impliedly is to be accepted or rejected before such disbursement. On the day of disbursement of loans accepted for participation, C&I is to charge J-G's account (which will contain sufficient funds), make other necessary book-keeping entries, and mail a participation certificate to J-G. C&I is to service all loans, crediting J-G's account daily with its shares of principal payments received and crediting J-G's account monthly with its agreed share of interest or discount, which is 6 per cent per annum "on the average unpaid balance of your participations hereunder".

The distinction may be observed between participations of the kind described above, which serve the purpose of enabling the originating bank to handle a larger volume of loans than its resources would otherwise permit, and participations that enable the originating bank to serve individual loan requirements that exceed its capacity in terms of the magnitude of the risk, legal lending limits, or otherwise. Yet this appears to be a distinction without a difference for the purposes of section 6(a)(4) of the Act as interpreted by the Board. See In the Matter of General Contract Corporation, 1958 BULLETIN 260. The Board there agreed with the view of the Hearing Examiner that section 6(a) was, generally, intended to prohibit transactions involving the "financing of the business operations of . . . an affiliate". 1958 BULLETIN at 264, 265. The Board concluded, in effect, that such financing would not be involved if "when one bank seeks participation by another bank to aid in meeting the credit needs of a borrower, . . . the second bank joined at the outset in making its portion of the loan, since this would not involve the second bank in either a direct loan to the first bank or a purchase of paper from it". 1958 BULLETIN at 269. This principle may be applied equally to participations in a volume of small loans as to participations to meet the credit needs of a single large borrower.

The offer and acceptance by telephone in conjunction with the underlying written document seem to meet the need for a prior agreement to allocate the risk. Each subject loan is at that time ascertained and nothing remains to be done for the participating bank to be obligated with respect thereto, even though mechanical steps remain, and must be taken promptly, for the participation to be a permissible "joining at the outset". As Mr. Dunne points out in his memorandum, the procedures established for the commitment of J-G's funds appear, regarding each loan separately, to be within the scope of the examples given in the Board's interpretation at 1958 BULLETIN 1059. It does not seem to the Board that the "blanket" aspects of the procedures in this case remove these participations from the permissible "outset" category described in General Contract. The Board considers it significant that the participating bank has no standing obligation to accept all participations

Mr. Orville O. Wyrick

-3-

that may be offered it by the originating bank. That is, while the participations may be effected in a fairly routine manner, their acceptance by the participating bank in fact remains for the exercise of its discretion with respect to each loan offered. In this manner, the participating bank appropriately accepts responsibility for conformity of its participations with the standards for their compliance with the Act, as discussed below.

Standards for selection of "new" loans. - The FDIC examination of The Baden Bank of St. Louis as of August 22, 1961, disclosed 24 participated loans that appeared to be refinancings of existing loans. Twenty-eight such loans were disclosed by the examination of J-G as of August 7, 1961. General Bancshares has reported to your Bank that 5 of these 52 participations, plus 6 others uncovered by General Bancshares on its own, were found not to conform to General Bancshares' policy and have been "returned to C&I". The "policy" referred to is that established by General Bancshares out of concern that "participation of personal loans whose proceeds were applied in payment of pre-existing accounts due the originating bank" might involve "a possible violation of the spirit, even though not the letter, of the Act". In brief, the holding company's policy permits participations in refinancings only if (1) the borrower is different from the borrower on the pre-existing loan, or (2) new funds are advanced, or (3) the collateral is changed or increased.

In line with Mr. Dunne's comments, the Board is of the opinion that these standards do not go far enough. Where a new borrower is substituted in good faith, as in the case of the sale of a financed automobile by the original borrower thereon and the assumption of the loan by the purchaser, the loan may be treated as "new" and therefore eligible for participation. Where, however, the borrower remains the same, the mere advancing of additional funds or the changing of the collateral does not make the whole loan an eligible "new" loan. In these cases the refinancing loan will be eligible for participation only to the extent of any additional funds advanced.

Under the foregoing standards, many of the questioned loans would be nonconforming on the basis of the information enclosed with Mr. Kroner's letter. The total number of participated loans questioned by the FDIC nevertheless appears to be small in relation to the total participation activity among the three banks. For this reason, the tightening of standards in accordance with this letter would seem to involve no great difficulty, even if participations in refinanced loans were stopped entirely. Also, because of the small number, and on the basis of the material submitted with Mr. Kroner's letter, the Board does not consider it necessary to invoke section 8 of the Act ("Penalties") in this matter, provided (1) that all outstanding participations that do

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

Mr. Orville O. Wyrick

-4-

not conform to the standards set forth above are returned to the originating bank and (2) that all future participations conform to such standards.

You are requested to advise General Bancshares Corporation of the Board's conclusions, as set forth herein, to the extent and in the manner that seems appropriate in the light of your Bank's contacts with the holding company on this subject. You are also requested to advise the Board when the procedures and outstanding participations of the General Bancshares' subsidiaries have been brought into conformity with the Board's interpretation of the statute.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.