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
Discount rates. The establishment without change by the Federal Reserve Bank of Atlanta on April 19, 1963, of the rates on discounts and advances in its existing schedule was approved unanimously, with the understanding that appropriate advice would be sent to that Bank.

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

Letter to the Federal Reserve Bank of Philadelphia waiving the assessment of a penalty incurred by Wayne County Bank and Trust Company, Honesdale, Pennsylvania, for a deficiency in its required reserves.
Letter to The Buffalo Bank, Buffalo, West Virginia, approving an investment in bank premises.

Letter to Manufacturers National Bank, Detroit, Michigan, granting permission to organize a corporation to be known as "Manufacturers-Detroit International Corporation," Detroit, Michigan, to engage in international or foreign banking, and transmitting a preliminary permit.

Letter to Davenport Bank and Trust Company, Davenport, Iowa, approving an investment in bank premises.

Letter to Farmers & Merchants Bank, Aberdeen, South Dakota, approving its application for membership in the Federal Reserve System.

Letter to Southern Arizona Bank and Trust Company, Tucson, Arizona, authorizing the acceptance of drafts or bills of exchange drawn for the purpose of furnishing dollar exchange.

Letter to The Chase Manhattan Bank, New York, New York, approving the establishment of a branch in the Town of New Castle.

Letter to The Bank of Georgia, Atlanta, Georgia, approving the establishment of a branch at 494 Peachtree Street, N. E.

Letter to The Company for Investing Abroad, Philadelphia, Pennsylvania, granting its request for consent to purchase and hold stock in generally designated types of corporations.

In connection with Item No. 9, it was noted that all of the outstanding general consents, like the one now before the Board, were scheduled to expire June 30, 1963, that date having been fixed in the
thought that a revision of Regulation K, Corporations Doing Foreign Banking or Other Foreign Financing under the Federal Reserve Act, might have been decided upon by such time. If it developed otherwise, the staff would contemplate recommending extension of the general consents for such further period of time as the Board might deem appropriate. It had been arranged for the Federal Reserve Bank of Philadelphia to explain to The Company for Investing Abroad why its requested general consent was being granted only through June 30, 1963.

Messrs. Shay, Conkling, and Goodman then withdrew from the meeting.

Eligibility of notes for discount (Item No. 10). There had been distributed a draft of reply to an inquiry from the Securities and Exchange Commission as to whether certain notes that The Colwell Company, Los Angeles, California, proposed to issue would be eligible for discount by Federal Reserve Banks. Upon that question rested the right of the company to an exemption of the notes from the registration and prospectus requirements of section 5 of the Securities Act of 1933. The position taken in the draft was that the notes would be ineligible for discount. It was pointed out that they would be not unlike notes originated by investment bankers, which were specifically excluded from discount eligibility in section 13 of the Federal Reserve Act.

At the Board's request, Mr. Hexter commented on the circumstances leading to the inquiry from the Securities and Exchange Commission and the application of various tests of discount eligibility.
In the discussion that ensued, the members of the Board expressed the view that the position taken in the draft reply was well reasoned.

Governor Mills indicated some concern, however, that the position was based on tests for the eligibility of paper for discount under section 13 of the Federal Reserve Act, whereas the Colwell notes conceivably could be used as collateral for advances under section 10(b) of the Act if a Federal Reserve Bank considered them satisfactory for that purpose. Also, while the Board for some time had felt some concern about the restrictiveness of the definitions of eligibility in the existing law and Regulation A, which definitions he considered outmoded in many ways by the evolution of banking practices, it was proposed to use such definitions as the basis of an interpretation upon which the Securities and Exchange Commission would rely to deny the Colwell Company's request. It appeared, also, that the Colwell notes might not be too readily distinguishable from certain notes of finance companies that had been ruled eligible for Federal Reserve discount.

In response to the latter comment by Governor Mills, Mr. Hackley remarked that the interpretation pertaining to the finance company paper was based on the fact that the proceeds would be used ultimately for commercial purposes, whereas the proceeds of the Colwell notes found their ultimate use in permanent investments in land and buildings.

During further discussion it was suggested that the letter indicate that, while it was assumed that the Securities and Exchange
Commission's inquiry contemplated eligibility for discount and the position expressed was confined to that question, it did not necessarily follow that the Colwell notes would be barred from all Federal Reserve credit, such as that available through advances under section 10(b) of the Act.

There being agreement with that suggestion, the letter was approved unanimously with the understanding that language along the lines indicated would be added. A copy of the letter sent to the Securities and Exchange Commission pursuant to this action is attached as Item No. 10.

Regulation A. Governor Robertson commented that the preceding discussion pointed up the desirability of considering a revision of Regulation A, Advances and Discounts by Federal Reserve Banks. In his view, the time might not be too far off when a regulation more consistent with present-day banking practices would be needed.

Mr. Hackley reviewed the developments that had taken place looking toward possible revision of the Regulation. At its meeting on September 10, 1962, the Conference of Presidents, having considered the report of the System Committee on Eligible Paper, approved a recommendation of the Conference Subcommittee on Legislation for a broad revision of the law. The Subcommittee had prepared a draft of proposed legislation, which it recommended be submitted to the Board of Governors. The Subcommittee's recommendation also contemplated that the Farm Credit Administration, the American Bankers Association, and the Association
of Reserve City Bankers would be asked to comment before proposed legislation was submitted to the Congress. (This recommendation was discussed by the Board at its meeting on September 27, 1962.) At its meeting on September 28, 1962, the Board decided to defer consideration of the matter until it could have available draft regulations that would implement the proposed statutory changes. Such a draft was now in preparation, Mr. Hackley stated, and it was hoped that it could soon be submitted for the Board's consideration.

Governor Robertson expressed the view that a revised regulation might be needed before it would be possible to have legislation enacted, which suggested that the staff should also explore the possibilities for limited revision of Regulation A under the existing statutes.

American Banker article. Governor Robertson expressed concern regarding the content of an article on current monetary policy that had appeared in the American Banker on April 23, 1963, particularly insofar as the article reflected views expressed at the most recent meeting of the Federal Open Market Committee.

The meeting then adjourned.

Secretary's Notes: Under date of April 24, 1963, a letter was sent to the Civil Service Commission requesting that the detail to the Board of Governors of Charles W. Schneider, Associate Chief Hearing Examiner for the National Labor Relations Board, be extended for a period not to exceed six months from May 14, 1963, on a reimbursable when-actually-employed basis, for the purpose of allowing Mr. Schneider to conduct a hearing on a request for a determination pursuant to section 4(c)(6) of the Bank Holding Company Act.
On April 23, 1963, Governor Shepardson approved on behalf of the Board the following items:

Letter to the Federal Reserve Bank of New York (attached Item No. 11) approving the appointment of John F. Weber as assistant examiner.

Memoranda from appropriate individuals concerned recommending the following actions relating to the Board's staff:

Appointment

Richard John Niebuhr as Summer Research Assistant in the Division of Research and Statistics, with basic annual salary at the rate of $5,540, effective the date of entrance upon duty.

Salary increase

Bishop Hart, Bindery Worker, Division of Administrative Services, from $5,949 to $6,136 per annum, effective April 28, 1963.

Acceptance of resignation

Janice L. Schoonover, Clerk-Stenographer, Division of Research and Statistics, effective at the close of business April 26, 1963.

Governor Shepardson today approved on behalf of the Board the following items:

Memorandum from Thomas J. O'Connell, Assistant General Counsel, requesting permission to teach an evening course in banking law as an Adjunct Professor of Law at the Georgetown University Law Center.

Memorandum dated April 23, 1963, from the Division of Personnel Administration recommending that a "Certificate of Availability of Federal Employee" for entry on active duty if ordered to active military service in the U. S. Air Force during a period of mobilization be executed for George G. Noory, Assistant Review Examiner, Division of Examinations, with the understanding that the certificate may be rescinded by the Board at any time within a 60-day period, unless an emergency has been proclaimed by the President or declared by the Congress.

Memorandum dated April 22, 1963, from the Division of Administrative Services recommending that authority be granted to that Division to proceed with necessary repair work, as outlined in the memorandum, on the
main roof of the Federal Reserve Building and three roof decks at the first floor level at an approximate cost of $34,700. This authorization constituted approval of a corresponding overexpenditure in the 1963 budget of that Division, to be carried as an unbudgeted special project.
Mr. Harry W. Roeder, Vice President,  
Federal Reserve Bank of Philadelphia,  
Philadelphia 1, Pennsylvania.

Dear Mr. Roeder:

This refers to your letter of April 10 regarding the penalty of $40.56 incurred for the nine-day period of March 21-29 by the Wayne County Bank and Trust Company, Honesdale, Pennsylvania.

It is noted that there was a daily deficiency of $32,900 in its reserves but, since the bank voluntarily withdrew membership in the Federal Reserve System as of the close of business March 29, 1963, your Bank feels that it would be inappropriate to make the assessment.

In the circumstances, the Board authorizes your Bank to waive the assessment of the penalty of $40.56 for the period March 21-29, 1963.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman  
Secretary.
April 24, 1963

Board of Directors,
The Buffalo Bank,
Buffalo, West Virginia.

Gentlemen:

The Board of Governors of the Federal Reserve System approves, under the provisions of Section 24A of the Federal Reserve Act, an investment in bank premises in an amount not exceeding $125,000 by The Buffalo Bank, Buffalo, West Virginia, for the purpose of purchasing land and constructing a new building. The proposed expenditure represents the entire cost of new premises to be constructed in Eleanor, West Virginia, in connection with the bank's relocation of its head office from Buffalo to Eleanor, West Virginia.

Very truly yours,

(Signed) Elizabeth L. Carmichael

Elizabeth L. Carmichael,
Assistant Secretary.
April 24, 1963

Mr. R. A. Mewhort, Executive Vice President,
Manufacturers National Bank,
151 West Fort Street,
Detroit 26, Michigan.

Dear Mr. Mewhort:

The Board of Governors has approved the Articles of Association and the Organization Certificate, dated March 21, 1963, of Manufacturers-Detroit International Corporation, and there is enclosed a preliminary permit authorizing that Corporation to exercise such of the powers conferred by Section 25(a) of the Federal Reserve Act as are incidental and preliminary to its organization. The Corporation may not exercise any of the other powers conferred by Section 25(a) until it has received a final permit from the Board authorizing it generally to commence business. The steps which must be taken prior to issuance of a final permit are enumerated in Section 211.3(c) of the Board's Regulation K.

Very truly yours,

(Signed) Elizabeth L. Carmichael

Elizabeth L. Carmichael,
Assistant Secretary.

Enclosure.
Preliminary Permit

IT IS HEREBY CERTIFIED that the Board of Governors of the Federal Reserve System, pursuant to authority vested in it by Section 25(a) of the Federal Reserve Act, as amended, has this day approved the Articles of Association and Organization Certificate, dated March 21, 1963, of MANUFACTURERS—DETROIT INTERNATIONAL CORPORATION duly filed with said Board of Governors, and that MANUFACTURERS—DETROIT INTERNATIONAL CORPORATION is authorized to exercise such of the powers conferred upon it by said Section 25(a) as are incidental and preliminary to its organization pending the issuance by the Board of Governors of the Federal Reserve System of a final permit generally to commence business in accordance with the provisions of said Section 25(a) and the rules and regulations of the Board of Governors of the Federal Reserve System issued pursuant thereto.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

(SEAL)

By (Signed) Elizabeth L. Carmichael

Elizabeth L. Carmichael, Assistant Secretary.

April 24, 1963
Board of Directors,  
Davenport Bank and Trust Company,  
Davenport, Iowa.

Gentlemen:

The Board of Governors of the Federal Reserve System approves, pursuant to Section 24A of the Federal Reserve Act, an additional investment in bank premises of not to exceed $2,525,000, by Davenport Bank and Trust Company through its wholly owned affiliate, Davenport Bank Building Corporation. This amount includes $725,000 for the purchase of real estate and $1,800,000 for the construction of a two-story building, with basement, for expansion of banking quarters and customer parking.

Very truly yours,

(Signed) Elizabeth L. Carmichael

Elizabeth L. Carmichael,  
Assistant Secretary.
Board of Directors,
Farmers & Merchants Bank,
Aberdeen, South Dakota.

Gentlemen:

The Board of Governors of the Federal Reserve System approves the application of Farmers & Merchants Bank, Aberdeen, South Dakota, for stock in the Federal Reserve Bank of Minneapolis, subject to the numbered conditions hereinafter set forth:

1. Such bank at all times shall conduct its business and exercise its powers with due regard to the safety of its depositors, and, except with the permission of the Board of Governors of the Federal Reserve System, such bank shall not cause or permit any change to be made in the general character of its business or in the scope of the corporate powers exercised by it at the time of admission to membership.

2. The net capital and surplus funds of such bank shall be adequate in relation to the character and condition of its assets and to its deposit liabilities and other corporate responsibilities.

In connection with the foregoing conditions of membership, particular attention is called to the provisions of the Board's Regulation H, regarding membership of State banking institutions in the Federal Reserve System, with especial reference to Section 208.7 thereof. A copy of the regulation is enclosed.

It is noted that under its articles of incorporation the bank may exercise fiduciary powers but that at the present time is not exercising such powers. Should the bank at any future time desire to exercise any powers not exercised at the time of admission to membership it will be necessary, under condition of membership numbered 1, to obtain permission of the Board of Governors.
If at any time a change in or amendment to the bank's charter is made, the bank should advise the Federal Reserve Bank, furnishing copies of any documents involved, in order that it may be determined whether such change affects in any way the bank's status as a member of the Federal Reserve System.

Acceptance of the conditions of membership contained in this letter should be evidenced by a resolution adopted by the Board of Directors and spread upon its minutes, and a certified copy of such resolution should be filed with the Federal Reserve Bank. Arrangements will thereupon be made to accept payment for an appropriate amount of Federal Reserve Bank stock, to accept the deposit of the required reserve balance, and to issue the appropriate amount of Federal Reserve Bank stock to the bank.

The time within which admission to membership in the Federal Reserve System in the manner described may be accomplished is limited to 30 days from the date of this letter, unless the bank applies to the Board and obtains an extension of time. When the Board is advised that all of the requirements have been complied with and that the appropriate amount of Federal Reserve Bank stock has been issued to the bank, the Board will forward to the bank a formal certificate of membership in the Federal Reserve System.

The Board of Governors sincerely hopes that you will find membership in the System beneficial and your relations with the Reserve Bank pleasant. The officers of the Federal Reserve Bank will be glad to assist you in establishing your relationships with the Federal Reserve System and at any time to discuss with representatives of your bank means for making the services of the System most useful to you.

Very truly yours,

(Signed) Elizabeth L. Carmichael

Elizabeth L. Carmichael,
Assistant Secretary.

Enclosure.
April 24, 1963

Southern Arizona Bank and Trust Company,
Tucson, Arizona.

Gentlemen:

The Board of Governors of the Federal Reserve System authorizes your Bank, pursuant to the provisions of Section 13 of the Federal Reserve Act, to accept drafts or bills of exchange drawn for the purpose of furnishing dollar exchange as required by the usages of trade in such countries, dependencies, or insular possessions of the United States as may have been designated by the Board of Governors, subject to the provisions of the Federal Reserve Act and the Board's Regulation C issued pursuant thereto. Section 13 of the Federal Reserve Act provides that no member bank shall accept such drafts or bills in an amount exceeding at any time the aggregate of one-half of its paid-up and unimpaired capital and surplus.

The right is reserved to terminate this authorization upon 90 days' notice to your Bank as provided in the Regulation.

Enclosed is a list of the countries with respect to which the Board of Governors has found that the usages of trade require the furnishing of dollar exchange. The Board of Governors may at any time after 90 days' published notice, remove from such list the name of any country, dependency, or insular possession contained therein.

Very truly yours,

(Signed) Elizabeth L. Carmichael

Elizabeth L. Carmichael,
Assistant Secretary.

Enclosures.
Board of Directors,
The Chase Manhattan Bank,
New York, New York.

Gentlemen:

The Board of Governors of the Federal Reserve System approves the establishment of a branch in the Taconic Plaza Shopping Center, Unincorporated Area of Millwood, Town of New Castle, Westchester County, New York, New York, by The Chase Manhattan Bank, provided the branch is established within one year from the date of this letter.

Very truly yours,

(Signed) Elizabeth L. Carmichael

Elizabeth L. Carmichael,
Assistant Secretary.

(The letter to the Reserve Bank stated that the Board also had approved a six-month extension of the period allowed to establish the branch; and that if an extension should be requested, the procedure prescribed in the Board's letter of November 9, 1962 (S-1846), should be followed.)
Board of Directors,
The Bank of Georgia,
Atlanta, Georgia.

Gentlemen:

The Board of Governors of the Federal Reserve System approves the establishment of a branch by The Bank of Georgia, Atlanta, Georgia, in the Doctors Building, 1494 Peachtree Street, N.E., Atlanta, Georgia, provided the branch is established within six months from the date of this letter.

Very truly yours,

(Signed) Elizabeth L. Carmichael

Elizabeth L. Carmichael,
Assistant Secretary.

(The letter to the Reserve Bank stated that the Board also had approved a six-month extension of the period allowed to establish the branch; and that if an extension should be requested, the procedure prescribed in the Board's letter of November 9, 1962 (S-1846), should be followed.)
April 24, 1963

Mr. Stewart M. Walker, Secretary-Treasurer,
The Company for Investing Abroad,
135 South Broad Street,
Philadelphia 9, Pennsylvania.

Dear Mr. Walker:

Consideration has been given by the Board of Governors to the request contained in your letter of April 9, 1963, transmitted through the Federal Reserve Bank of Philadelphia, for the Board's general consent to The Company for Investing Abroad ("TCIA") to purchase and hold stock in generally designated types of corporations.

On the basis of the information furnished as to investment policies to be pursued by TCIA, the Board grants its general consent, for the purposes of the first sentence of Section 211.9(c) of Regulation K, to TCIA to purchase and to hold shares of stock of any foreign corporation, provided the aggregate investment in any one foreign corporation and its subsidiaries (on a combined basis) shall not exceed 5 per cent of the capital and surplus of TCIA, subject to the following conditions:

(1) This authorization shall be applicable only to investments made on or before June 30, 1963. Options to acquire stocks subsequent to the termination date (June 30, 1963) of the general consent may not be exercised unless specifically approved by the Board or permitted under a then effective general consent.

(2) The Board of Governors shall be informed promptly in writing, through the Federal Reserve Bank of Philadelphia, when any such investment is made, together with pertinent details regarding such investments, and the Board of Governors shall be furnished within thirty days after acquisition: (a) a balance sheet of the corporation whose stock has been acquired, showing the financial position of the corporation as of a recent date, together with an income statement for the preceding fiscal period; (b) a brief description of the business of the corporation; (c) a list of officers and directors, with addresses and principal business affiliations; (d) a description of the stock acquired; (e) information
concerning the rights and privileges of the various classes of stock of the corporation outstanding; (f) a list of all stockholders holding 5 per cent or more of any class of stock of such corporation and their holdings; and (g) a brief description of any loan or credit transaction with the corporation in connection with which the stock was acquired. If, upon review of such information, the Board of Governors determines that an investment is contrary to the investment program of TCIA as submitted to the Board in your letter of April 9, 1963, or is otherwise objectionable to the Board of Governors, TCIA shall take the necessary steps to divest itself of such investment, upon notice to that effect and within such time as the Board may specify.

(3) Investments by TCIA under this general consent shall be made in accordance with sound financial policies, including among others, (a) appropriate diversification of its loan and investment portfolios so as to avoid undue concentrations in loans to, and investments in, individual enterprises, industries, or otherwise, and (b) proper regard to the relationship between its assets and the maturities of its obligations.

(4) TCIA shall be expected to dispose of its holdings of stock of such foreign corporation, as promptly as practicable, in the event that such foreign corporation should at any time (a) engage in the business of issuing, underwriting, selling or distributing securities; (b) engage in the general business of buying or selling goods, wares, merchandise, or commodities in the United States or transact any business in the United States except such as is incidental to its international or foreign business; or (c) conduct its operations in a manner which, in the judgment of the Board of Governors, is inconsistent with Section 25(a) of the Federal Reserve Act or regulations thereunder.

(5) Such investments shall not be made in the shares of financial corporations or holding companies.

(6) The investment in any such foreign corporation shall not include more than 49 per cent of its voting shares or otherwise enable TCIA to designate a majority of the foreign corporation's board of directors or similar management group.

(7) The aggregate equity investment (at cost) in foreign corporations engaged in the same business (i.e., the manufacture or mining of similar products or the carrying on of similar activities) shall not exceed 25 per cent of TCIA's capital and surplus.
(8) The aggregate equity investment in all foreign corporations doing business in any one country, colony, possession or dependency shall not exceed 25 per cent of TCIA's capital and surplus.

(9) Under this general consent, shares shall be acquired only from the issuer directly.

Very truly yours,

(Signed) Elizabeth L. Carmichael

Elizabeth L. Carmichael,
Assistant Secretary.
Mr. Charles E. Shreve,
Executive Assistant Director,
Division of Corporation Finance,
Securities and Exchange Commission,
Washington 25, D. C.

Dear Mr. Shreve:

This is in reply to your letter of April 4, addressed to the Board's General Counsel, inquiring whether certain notes proposed to be issued by The Colwell Company, Los Angeles, California, would be eligible for discount by Federal Reserve Banks. Enclosed was a draft (dated March 20, 1963) of a letter proposed to be sent to the Commission on behalf of Colwell, describing its operations and the nature of the proposed notes.

Section 3(a)(3) of the Securities Act of 1933 provides that certain described types of notes are exempt from the registration and prospectus requirements of section 5 of that Act, and Colwell contends that this exemption is applicable to the notes it proposes to issue. According to Securities Act Release No. 4412 (a copy of which you enclosed) the exemption provided by section 3(a)(3)

"applies only to prime quality negotiable commercial paper... of a type eligible for discounting by Federal Reserve banks."

It is inferred that the Commission's position that section 3(a)(3) applies only to paper that is eligible for Federal Reserve discount relates to eligibility at the time the security is offered for sale. If this were not so, the exemption would apply to certain securities despite the fact that the requisite Federal Reserve discount eligibility would not come into being until long after the securities were issued and would exist only during the last few months of the period during which they would be outstanding, as explained hereinafter.

Colwell's draft letter states that the notes in question will have a maturity of "nine months or less". In view of this, it is assumed that their usual maturity probably will be in the range of six months to nine months—in any event, in excess of ninety days.
On the basis of this assumption, it is the opinion of the Board of Governors that the notes, at the time they were issued, would not be "of a type eligible for discounting by Federal Reserve banks."

The only provision of law under which notes for the purposes described in the Colwell letter might be eligible for Federal Reserve discount is the second paragraph of section 13 of the Federal Reserve Act (12 U.S.C. 343). The last sentence of that paragraph reads as follows:

"Notes, drafts, and bills admitted to discount under the terms of this paragraph must have a maturity at the time of discount of not more than 90 days, exclusive of grace."

A similar provision appears in section 201.3(a)(4) of Federal Reserve Regulation A (12 C.F.R. 201.3(a)(4)).

Accordingly, if the notes in question had a maturity of nine months, for example, they would be ineligible for Federal Reserve discount (even if otherwise qualified) at the time of issuance and throughout the first two-thirds of the period during which they would be outstanding. If the maturity was six months, they would be ineligible at the time of issuance and throughout the first half of the period to maturity.

To recapitulate, it is the view of the Board that, if the notes to be issued by The Colwell Company had maturities, at the time of issuance, in excess of ninety days (exclusive of days of grace), such notes would not be eligible, at that time, for discounting by Federal Reserve Banks.

If, however, the Commission should conclude that section 3(a)(3) of the Securities Act applies to paper that may be eligible for Federal Reserve discount at any time during its existence even though not eligible at the time of issuance, or if the notes of The Colwell Company had a maturity of not more than ninety days, exclusive of grace, there would be presented the difficult question whether such notes would be eligible for discount, apart from the problem of maturity.

Section 13 of the Federal Reserve Act authorizes the Board of Governors "to determine or define the character of the paper...eligible for discount". Pursuant to this authorization, section 201.3(a)(1) of Regulation A limits discount eligibility to negotiable paper "which has been issued or drawn, or the proceeds of which have been used or are to be used", for one of the following purposes:

(1) "producing, purchasing, carrying or marketing goods in one or more of the steps of the process of production, manufacture, or distribution";
(2) "meeting current operating expenses of a commercial, agricultural or industrial business";

(3) "carrying or trading in direct obligations of the United States".

Clearly, neither (2) nor (3) applies to the proposed notes of The Colwell Company. Consequently, the question is whether the proceeds of such notes would be used "in producing, purchasing, carrying or marketing goods in one or more of the steps of the process of production, manufacture, or distribution".

Colwell is engaged in the "origination" of mortgage loans "for sale to the ultimate investors [such as insurance companies and savings banks] who furnish the permanent long-term financing of such loans." Its inventory of mortgage loans turns over in some two to five months. Colwell contends that it "manufactures" or "produces" the loans for sale, and that, therefore, the proceeds of its notes would be used "in producing, purchasing, carrying or marketing goods".

Footnote 5 to section 201.3(a)(1) of Regulation A provides that "As used in this Regulation the word 'goods' shall be construed to include goods, wares, merchandise, or agricultural products, including livestock." In view of this enumeration, it is questionable whether mortgage loans, even as part of the short-term current inventory of a mortgage banker, constitute "goods" for this purpose. Nevertheless, in view of the underlying objectives of section 13, the Board might be inclined to interpret "goods" broadly in this connection, if the proposed notes would comply with other applicable provisions of law and regulation. However, it is not necessary to decide this question, for reasons set forth hereinafter.

Section 201.3(a)(2) of Regulation A denies discount eligibility to notes "the proceeds of which...are to be used for permanent or fixed investments of any kind, such as land, buildings or machinery, or for any other fixed capital purpose". Although the proceeds of the Colwell notes would be used, literally, for investment in land and buildings, it may be reasonably argued that these real-estate loans are not "permanent or fixed investments" in Colwell's hands, since they constitute a current inventory that is liquidated, by sale to investors, within a few months, presumably in time to provide funds sufficient to meet the obligations on Colwell's notes as they mature. (See 1921 Federal Reserve Bulletin 1079.) On the basis of this reasoning, Colwell maintains that the proceeds of its notes would be used to produce, carry, and market "goods" (i.e., real-estate mortgage loans) in the process of "production, manufacture or distribution", rather than "for permanent or fixed investments".
Even if the foregoing contentions were accepted, however, the Colwell notes would be ineligible for Federal Reserve Bank discount, for another reason. Section 13 of the Federal Reserve Act, in addition to restricting discount eligibility to paper "issued...for agricultural, industrial, or commercial purposes, or the proceeds of which...are to be used, for such purposes", provides that the Board's further definition of paper eligible for discount "shall not include notes...covering merely investments or issued...for the purpose of carrying or trading in stocks, bonds, or other investment securities, except bonds and notes of the Government of the United States." This limitation is reiterated in section 201.3(a)(3) of Regulation A.

Underwriters of "stocks, bonds, or other investment securities" (i.e., investment bankers) often "originate" such securities in a manner that, for present purposes, is not unlike the process by which Colwell originates mortgage loans. Such investment bankers, like mortgage bankers, need funds to acquire securities for their inventories and to carry those securities (usually for a short period) pending their sale to permanent investors. Likewise, the proceeds of sale of such securities frequently are used "for permanent or fixed investments...such as lands, buildings or machinery, or for...other fixed capital purpose".

In view of this specific prohibition in the statute and regulation, and the similarity, in relevant respects, of notes covered by that prohibition and the proposed Colwell notes, the Board concludes that notes of the nature described in the draft of letter (dated March 20, 1963) to the Commission on behalf of Colwell would not be eligible for discount by Federal Reserve Banks, even if those notes complied with the ninety-day maturity requirement of section 13 of the Federal Reserve Act and section 201.3(a)(4) of Regulation A. In this connection, see also 1937 Federal Reserve Bulletin 1190 and 1938 Bulletin 86.

Apart from the question whether notes of The Colwell Company would be disqualified from the exemption provided by section 3(a)(3) of the Securities Act because they would not be eligible for Federal Reserve discount, it is noted that Securities Act Release No. 4412 states that "the current transactions standard [of section 3(a)(3)] is not satisfied where the proceeds are to be used for...the funding of commercial real estate developing or financing; the purchase of real estate mortgages or other securities; [or] the financing of mobile homes or home improvements".

The following comment is made in order to avoid possible misunderstanding, although it is not otherwise relevant to your inquiry. The question presented in your letter is whether the proposed notes of
The Colwell Company would be eligible for discount by Federal Reserve Banks. Accordingly, the Board's response relates to that question alone. However, it should not be inferred that the Federal Reserve Banks could not in any event extend credit to member banks on the security of such notes of Colwell. Paper that is not eligible for discount may nevertheless be eligible as collateral for advances made under section 10(b) of the Federal Reserve Act (12 U.S.C. 347b), which provides that

"Any Federal Reserve bank, under rules and regulations prescribed by the Board of Governors of the Federal Reserve System, may make advances to any member bank on its time or demand notes having maturities of not more than four months and which are secured to the satisfaction of such Federal Reserve bank." (emphasis added)

Advances under section 10(b), however, must bear interest at a rate not less than one-half per cent higher than the highest discount rate in effect at the Reserve Bank when the advance is made.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman, Secretary.
April 23, 1963

Mr. Howard D. Crosse, Vice President, Federal Reserve Bank of New York, New York 45, New York.

Dear Mr. Crosse:

In accordance with the request contained in your letter of April 17, 1963, the Board approves the appointment of John F. Weber as an assistant examiner for the Federal Reserve Bank of New York, effective May 2, 1963.

Very truly yours,

(Signed) Elizabeth L. Carmichael

Elizabeth L. Carmichael, Assistant Secretary.