Minutes for May 16, 1963

To: Members of the Board

From: Office of the Secretary

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

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

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

Chm. Martin _____

Gov. Mills _____

Gov. Robertson _____

Gov. Balderston _____

Gov. Shepardson _____

Gov. King _____

Gov. Mitchell _____

Minutes of the Board of Governors of the Federal Reserve System on Thursday, May 16, 1963. The Board met in the Board Room at 10:00 a.m.

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

Mr. Sherman, Secretary
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. O'Connell, Assistant General Counsel
Mr. Shay, Assistant General Counsel
Mr. Dembitz, Associate Adviser, Division of Research and Statistics
Mr. Solomon, Associate Adviser, Division of Research and Statistics
Mr. Conkling, Assistant Director, Division of Bank Operations
Mr. Leavitt, Assistant Director, Division of Examinations
Mrs. Semia, Technical Assistant, Office of the Secretary
Miss Hart, Senior Attorney, Legal Division
Mr. Hricko, Senior Attorney, Legal Division
Mr. Young, Senior Attorney, Legal Division
Mr. Hunter, Supervisory Review Examiner, Division of Examinations
Mr. McClintock, Supervisory Review Examiner, Division of Examinations
Mr. Sanford, Review Examiner, Division of Examinations

Report on competitive factors (Baltimore-Hagerstown, Maryland). There had been distributed a draft of report to the Comptroller of the Currency on the competitive factors involved in the proposed merger of The Nicodemus

National Bank of Hagerstown, Hagerstown, Maryland, into The First National Bank of Maryland, Baltimore, Maryland

After discussion, the report was approved unanimously for transmission to the Comptroller of the Currency. The conclusion of the report read as follows:

> There is virtually no competition between these two banks; however, First National, as a large institution, does solicit the business of large customers throughout the State. Consummation of the proposed merger would alter significantly the banking structure in Hagerstown and provide a potential threat to the ability of other local banks to continue to offer effective competition and remain independent units.
>
> The acquisition of Nicodemus National would not add substantially to First National's resources, second largest bank in the State, but it would continue the trend toward concentration of banking resources in the State.

Applicability of section 32 (Item No. 1). There had been distributed a memorandum dated May 14, 1963, from the Legal Division, accompanied by a draft letter replying to an inquiry from the Federal Reserve Bank of Minneapolis as to whether section 32 of the Banking Act of 1933, as amended, would prohibit a vice president and director of a national bank from serving at the same time as agent of APA, Incorporated, in the sale of partnership units in programs for the development of gas and oil properties by the Apache Corporation, Minneapolis, Minnesota. The proposed reply took the position that the partnership units were "other similar securities" within the meaning of section 32, and that therefore an officer, director, or employee of a national bank might not, at the same time, serve as an agent in the marketing of the units.

After discussion, the letter was approved unanimously. A copy is attached as Item No. 1.

Request for examination reports (Items 2 and 3). There had been distributed a memorandum dated May 15, 1963, from the Legal Division in connection with a request made through the Federal Reserve Bank of Chicago by an attorney for Genesee Merchants Bank & Trust Co., Flint, Michigan, for copies of reports of examination of Davison State Bank, Davison, Michigan, for the years 1957-1962. Davison State Bank merged with and into Genesee Merchants in November 1962. In its transmittal letter the Federal Reserve Bank of Chicago indicated that the request for copies of reports of examination arose from the fact that an officer and an employee of Davison State Bank, at a time prior to its merger with Genesee Merchants, allegedly misapplied funds of Davison State Bank. That bank carried a fidelity bond issued by the America Fore Loyalty Group, and Genesee Merchants had now filed 101 claims under the fidelity bond against the bonding company in respect to the alleged misapplications of Davison State Bank funds. Counsel for Genesee Merchants stated that the bank was willing to make its copies of the reports of examination available to a representative of the bonding company. The Reserve Bank made no recommendation.

The Legal Division recommended that the Board decline to authorize Genesee Merchants to furnish copies of the reports to the bonding company's representative. Pursuant to section 9 of the Federal Reserve Act and section 261.2(d) of the Board's Rules Regarding Information, Submittals, and Requests, the authorization could be given upon the Board's finding

that such disclosure would be in the public interest. In the Legal Division's view, however, no such finding would be justified under the circumstances stated. Despite the minimal information given to the Board regarding either the nature of the claims filed or the particular information sought from the reports of examination, it was believed that only a small portion, if any, of a given report would relate to or bear upon the question whether or not the bonding company was liable under the fidelity bond. Rather, there would result an unwarranted disclosure of a considerable volume of confidential information bearing on persons and matters wholly unrelated to the claims filed.

The memorandum then reviewed previous instances in which the Board had refused similar requests, and with which the suggested refusal in the present matter would appear to be consistent. It was pointed out that, so far as was known, neither Genesee Merchants nor the America Fore Loyalty Group had identified the nature of or basis for the claims filed or the relevancy of any particular portion of the examination reports to those claims. The request was of such a nature that if it were to come before the Board in the form of a subpoena duces tecum, the Legal Division would urge that action be taken to have the subpoena quashed as being too general and unspecific.

The memorandum concluded with the suggestion that, if the Board concurred in the Legal Division's recommendation, a letter be sent to Counsel for Genesee Merchants informing him only that his request was denied for the reason that in the Board's judgment disclosure of the

information in the reports of examination would not be in the public interest. This letter would be sent to the Federal Reserve Bank of Chicago with a transmittal letter explaining more fully the reasons for the Board's denial of the request. Drafts of such letters were attached to the memorandum.

Governor Mitchell, noting that the Legal Division had cited as part of the basis for its recommendation the fact that no information had been given as to the manner in which the examination reports were expected to be used, asked if that information could not be obtained. Response was made that the information could be obtained but that, regardless of the way in which the bonding company expected to use material from the reports, the Legal Division was of the view that the request should be denied.

Other comments brought out that, since the matter was only in the claim stage, the bonding company could not seek to obtain the reports by subpoena; it could resort to subpoena only in the event litigation was begun. It was also observed that in any event the type of information in examination reports did not constitute the best kind of evidence for defalcation proceedings.

After further discussion, the letters to Counsel for Genesee Merchants Bank & Trust Co. and to the Federal Reserve Bank of Chicago were approved unanimously. Copies are attached as Items 2 and 3, respectively.

Mr. O'Connell then withdrew from the meeting.

Report on draft legislation (Item No. 4). On May 15, 1963, the Board discussed a request from the Bureau of the Budget for the Board's

views on a preliminary draft bill to increase deposit insurance coverage and to amend various other provisions of law. In a distributed memorandum dated May 14, 1963, Mr. Hackley summarized the bill, the principal provisions of which would (1) increase insurance coverage for both banks insured by the Federal Deposit Insurance Corporation and institutions insured by the Federal Savings and Loan Insurance Corporation from $10,000 to $15,000; (2) require the maintenance of reserves against time and savings deposits by nonmember insured banks and against withdrawable accounts by institutions that are members of the Federal Home Loan Bank System; (3) give nonmember insured banks access to Federal Reserve discounts and advances; (4) make provision for assuring the liquidity of all insured banks and all members of the Home Loan Bank System; (5) place on a standby basis the authority of the Board of Governors and the Federal Deposit Insurance Corporation to fix maximum interest rates payable by member banks and nonmember insured banks on time and savings deposits, and authorize the Federal Home Loan Bank Board similarly to fix maximum dividend rates payable by members of the Home Loan Bank System on share accounts; and (6) strengthen and make applicable to all insured banks and members of the Home Loan Bank System certain provisions of present law designed to prevent conflicts of interest in dealings by financial institutions with directors, officers, and employees, public examiners, and affiliates of such institutions. Attached to Mr. Hackley's memorandum was a draft of reply to the Bureau of the Budget that, after commenting on various provisions of the proposed bill, stated that the Board would have no objection to introduction and enactment of the

draft bill except in one respect, namely, that extension of reserve requirements against time and savings deposits of nonmember insured banks, but not against their demand deposits, would be highly undesirable. The draft letter expressed the Board's concurrence with the recommendations of the President's Committee on Financial Institutions that reserve requirements against both time and demand deposits be extended to all insured banks and that reserves against demand deposits be computed on a graduated basis.

At the conclusion of the discussion at the May 15 meeting, the staff was requested to prepare a revised draft of reply to the Bureau of the Budget reflecting the views expressed by members of the Board, and such a revised draft had now been distributed.

The revised draft (as had the previous draft) referred to Vice Chairman Balderston's testimony on April 25, 1963, before the House Banking and Currency Committee in connection with H.R. 5130, a bill providing for an increase in insurance coverage of deposits in banks insured by the Federal Deposit Insurance Corporation and share accounts in institutions insured by the Federal Savings and Loan Insurance Corporation from $10,000 to $25,000 for each account. Vice Chairman Balderston had indicated that it was the Board's view that the proposed increase would not be in the public interest; that if any increases were appropriate, they should be small and infrequent; and that effective supervision over the institutions covered was an important prerequisite to insurance protection. The revised draft stated that the Board would interpose no objection to a small increase in insurance coverage, expressing a preference for an increase to $12,500

rather than $15,000. The draft also stated that in the Board's judgment it would be unnecessary and undesirable to include in the bill provisions dealing with maximum rates of interest on deposits in insured banks and with reserves and liquidity of such banks, as proposed in sections 3, 4, and 6 of the bill. The draft indicated that the Board favored the extension to all commercial banks of reserve requirements against both demand and time deposits but felt that this was a matter that should be dealt with, after careful study, in separate legislation rather than on a piecemeal basis as contemplated in the draft bill. Similarly, it might be desirable to revise and place on a standby basis provisions of present law relating to maximum rates of interest on time and savings deposits in member and nonmember insured banks; but again this was a subject that should be studied separately and covered by separate legislation. For the reasons indicated, the Board would oppose the draft bill in its present form, but would consider any revision that would omit the provisions of sections 3, 4, and 6.

At the Board's request Mr. Hackley reported that, as the Board had asked him to do yesterday, he had telephoned Mr. Reeve of the Bureau of the Budget to inform him that the Board had substantive objections to certain provisions of the draft bill, and he had given Mr. Reeve the substance of the statement Governor Mills had submitted yesterday in opposition to the bill. Mr. Hackley and Mr. Reeve had discussed alternatives for handling the various components of the bill, and Mr. Reeve had indicated that the Bureau would like to have the Board's comments today.

Governor Robertson stated that in his view it would be a mistake for the Board to register major objections to the bill. He believed that when the Administration got behind a bill that would effect so many desirable reforms, the Board should accept the whole package, except that the proposals relating to reserve requirements should be made the subject of a separate proposal. He saw no reason to try to prevent the authority to prescribe maximum rates of interest on time and savings deposits from being put on a permissive and standby basis rather than a mandatory one. He did not believe that additional study of that question should be suggested. At most, the suggestion should be for separate legislation, although his own preference would be to include the change in the bill now being drafted. He was not in agreement with the statement in the draft letter that it would be unnecessary and undesirable to include provisions relating to liquidity. He believed they were innocuous, and that the Board could well go along with them and say nothing about bank liquidity in its comments on the proposed bill.

Governor Mills asked if the issue was not whether the package of proposed statutory changes should be accepted hastily or whether they should come before the Board for more deliberate consideration.

Governor Mitchell expressed a strong feeling that the whole package ought to be supported. He did not concur with the suggestion that the provisions relating to reserves should be dealt with separately, although he did agree that they should be expanded to impose reserve requirements on demand deposits as well as time and savings deposits of insured nonmember

banks. In his opinion, the Board was in a poor position in regard to the subject of reserves, and he had liked the recommendation in the report of the President's Committee on Financial Institutions because it gave the Board an opportunity to get out of that position. Even after long study, it had not been possible to arrive at a new set of standards for classification of reserve cities, and the Board was in the position of removing cities from reserve city status haphazardly. The draft bill presented an opportunity to gain important advantages to the Board's ultimate goals, such as the extension of reserve requirements to insured nonmember banks, placing the authority to prescribe maximum interest rates on a standby basis, and subjecting savings and loan associations to reserve requirements, by going along with a measure proposed by another Governmental body. In his view, the Board should vigorously endorse the complete package, with the added recommendation that the reserve requirements proposals be expanded to cover demand deposits.

Chairman Martin reviewed the attitudes expressed by members of the Board yesterday; there had been general agreement that a strong stand must be taken as to the necessity to extend reserve requirements to demand deposits as well as time deposits of insured nonmember banks, but the prevailing view had been that it might be wiser to reserve several elements of the draft bill for later consideration. The latter point, of course, involved a matter of judgment.

Governor Shepardson added that his position was that on a quid pro quo basis the Board might have a better chance to obtain enactment of the

provisions it considered most important than it would if the package approach were not followed.

At the Board's request, Mr. Cardon commented on the probable fate of the bill's provisions in the Banking and Currency Committees and in the Congress. Although that was a matter that could not be foretold with certainty, it would be his expectation that the entire package would be unlikely to be reported out by the Committees. If he understood correctly that the Board's question was whether the advantage of the increase in insurance coverage made the bill sufficiently attractive to carry acceptance of the features that would be unattractive to nonmember insured banks and to savings and loan associations, his view was that it did not.

During further discussion as to how the various elements of the draft bill might fare in the course of the legislative process, Governor Shepardson commented that it would be well for the Board to make it clear that the bill was acceptable to it only if it included certain features, and that if any of the provisions that the Board considered important were dropped through amendments the Board would not be foreclosed from registering its objections and pointing out inequities that might result from such deletions.

Governor Balderston expressed the view that it would be the worst thing that could happen if nonmember banks were afforded access to Federal Reserve discount facilities merely in return for maintaining reserve requirements against their time deposits.

Chairman Martin observed that the two members of the Board who had not been present during yesterday's discussion were in favor of supporting

the proposed bill as a package, a position toward which Governor Shepardson had expressed some leaning yesterday. This seemed to confront the Board with the question whether the consensus of yesterday should be reversed.

Governor Robertson commented that to him it seemed advisable for the Board to take advantage of the lift supplied by the recommendations in the report of the President's Committee on Financial Institutions in order to have the authority to prescribe maximum interest rates put on a permissive rather than a mandatory basis and to obtain extension of reserve requirements to nonmember banks.

Governor Mills stated that the draft bill involved fundamental issues that had been debated over not merely months but years, and for the Board to take a position on them in its report on the draft bill seemed to him a very hasty and ill-considered action. The Board's comments would become a matter of public knowledge, which would place the Board in a poor position if, after further deliberation, it should arrive at a different view on any of the points involved.

Chairman Martin remarked that in yesterday's discussion thought had been given to whether, on more mature judgment, the members of the Board might have a different attitude toward the proposals in the bill.

Governor Mitchell questioned what mature judgment should be considered to be. The proposals under consideration had been studied for a long time and by many groups, such as the Commission on Money and Credit, the Comptroller of the Currency's Advisory Committee, and the President's Committee on Financial Institutions. In his view, the Board should be

prepared to take a position; he felt that no amount of further study would change his appraisal of the merits of the proposals.

Governor King commented that he had heard repeated remarks from bankers that loan standards were declining, especially to enable banks to obtain higher earnings in order to pay as much interest as possible on time and savings deposits. In the face of deteriorating standards, he considered that the present was the wrong time to put on a standby basis the authority to prescribe maximum permissible interest rates. In his view, if the present restrictions were lifted, the only time the Board would ever reimpose them would be when chaos had already developed.

Governor Mills expressed concurrence with Governor King's comments.

There ensued a discussion of the procedures specified in the draft bill for reimposition by the Board of maximum interest rates on time and savings deposits. The bill would require that the Board consult with the Federal Deposit Insurance Corporation and the Federal Home Loan Bank Board, and that the Board make an affirmative finding that any interest rate limitation would be consistent with the Employment Act of 1946 and "required by general credit conditions or to prevent unsound competitive or other practices among member banks that would endanger the safety" of such banks. Also, the draft bill permitted the fixing of different maximum rates on a more flexible basis, including differentiation based on the nature or location of the depositor or the member bank.

Mr. Hackley suggested that the Board's letter to the Bureau of the Budget might include a caveat to the effect that, while the Board supported

the provisions of the draft bill in principle, it reserved the right to reconsider any of them on the basis of the language of the bill in final form.

Governor Balderston then outlined the direction in which his thoughts had turned since yesterday's discussion. He shared the concern that other members of the Board had expressed that the climate in which this legislative proposal was being developed suggested the likelihood that the bill would encounter amendments disadvantageous to the System. Yet he was strongly tempted by the possibility of obtaining some of the statutory changes the Board wanted, especially the requirement that nonmember insured banks maintain reserves. He considered the extension of the reserve requirement provisions to demand deposits of nonmember insured banks essential. Should such reserve requirements be written into law, the incentive for State member banks to leave the System would be diminished, and for the hope of attaining that end he would like to see the System on record in support of this concrete proposal even though it seemed unlikely that the entire package would be adopted. The strong opposition that undoubtedly would be exerted by small banks and by banks that liked to wrap themselves in the cloak of a maximum permissible interest rate might prevent the package from even emerging from the Committee. Nevertheless, Governor Balderston would like to see support for the proposals that he personally favored made a matter of public record if he could be sure that that could be done with safety and that the Board would not be surprised with an unhappy outcome. It would be most unfortunate if the extension of reserve requirements to time

and savings deposits were enacted but extension to demand deposits failed, thereby making it advantageous for large State member banks to leave the System.

Governor King remarked that he had great doubt that provision for reserve requirements for demand deposits of insured nonmembers would ever be enacted. Small banks would complain, and they could exert a great deal of influence on members of Congress.

Messrs. Noyes and Solomon commented on the objectives that had guided the staff work of the President's Committee on Financial Institutions and the Budget Bureau and the Treasury Department in developing the preliminary draft bill. The point Governor King had made had been very much in mind, and the package in the bill was designed to make it at least palatable, if not wholly acceptable, to small banks. There were a number of reasons why extension of reserve requirements to demand deposits was not made a part of the bill. Principally, it was thought difficult to tie such a provision to an insurance bill, which was regarded as a means of strengthening supervision of savings and loan associations. However, extension of reserve requirements to demand deposits was an accepted objective, hoped to be accomplished later along with a change to a graduated structure of reserves. In that event, small banks would not be subjected to present reserve requirements, but to lower requirements according to their size, which it was hoped would be acceptable to them in return for obtaining higher insurance coverage.

Governor Mills remarked that the tenor of the discussion emphasized to him that the draft bill represented a lot of horse trading, and support of it would lead the Board down a path the end of which could not be seen.

Governor Robertson expressed the opinion that by swinging behind a proposal that was sponsored by the Administration, although preferably adding to it coverage of demand deposits and a graduated reserve structure, at least some desirable measures might be obtained. The Board might not get everything it wanted, but it was necessary to make a start in order to get anything.

Governor Mitchell stated that he regarded the increase in insurance coverage as a small issue in comparison with the other provisions of the bill. Having the $25,000 maximum that had been proposed originally reduced to $15,000 was sufficient accomplishment, without trying to whittle it further to $12,500.

During further discussion various changes were agreed upon in the draft of letter to the Bureau of the Budget, after which the letter was approved in the form attached as Item No. 4. Governor Mills dissented from this action for the reasons he had expressed yesterday and today.

Messrs. Molony, Cardon, Noyes, Solomon, and Conkling then withdrew from the meeting and Mr. Smith, Senior Economist, Division of Research and Statistics, entered the room.

Application of Sussex County Trust Company. There had been distributed a memorandum dated May 1, 1963, from the Division of Examinations regarding the application of Sussex County Trust Company, Franklin, New

Jersey, to merge with The Farmers National Bank of Sussex, Sussex, New Jersey. The title of the resulting bank would be The Bank of Sussex County. The memorandum analyzed the circumstances underlying the application, with particular reference to the factors cited for consideration by the Bank Merger Act. Upon consideration of the legislative history of the Act, the various banking and competitive criteria required to be considered, and after consultation with the Legal Division, the Division of Examinations recommended that the merger be denied. The Legal Division felt that it would be more difficult under the statutes to support approval than denial on the basis of the information supplied by the applicant. The basis for the Division of Examinations' recommendation was that it did not appear that the positive benefits flowing from the merger would offset unfavorable factors. A fairly significant amount of competition existed between the two banks, which would be increased upon establishment by Sussex County Trust Company of a branch in Vernon Township, six miles east of Sussex, for which it had obtained approval. The below-average earnings of two such banks would probably often weigh in favor of approval; however, in this case one of the banks had delayed action to improve earnings upon the assumption that the merger would be approved. Sussex County Trust had deferred improvment of its capital position, again on the assumption that the merger would be approved. While the merged institution would be able to attract and retain better management, management of each of the banks was now reasonably satisfactory. The convenience and

needs factor was believed to weigh in favor of the merger, but not strongly.

Despite the recommendation of the Division of Examinations for denial as appearing consistent with the Bank Merger Act, on the broader questions of the banking structure and the best interests of the general public, the Division had reservations about denying an application to merge two relatively small institutions, notwithstanding the existence of significant competition between them.

The merged institution would be about the same size as the largest bank now in Sussex County. Those two banks would hold slightly over 60 per cent of deposits and loans of all commercial banks in the County; yet they would still be relatively small banks, with about $20 million each in deposits, total County deposits being about $65 million. This seemed considerably different from a situation in which two banks held 60 per cent of county deposits totaling $650 million or $6,500 million. Moreover, aggregate demand deposits of the two banks were only 29 per cent of the County total; their time and savings deposits equaled about 71 per cent of the County total. There were more sources seeking time and savings deposits than there were sources seeking demand deposits. Since most time and savings deposits require less servicing than do the bulk of demand deposits, it seemed reasonable to conclude that the market area from which financial institutions obtain time and savings deposits was broader than the area from which demand deposits were obtained. It seemed likely that commercial banks in adjacent New Jersey counties and in New York State might

be more effective competitors in Sussex County for time money than for demand money and the savings banks and savings and loan associations were said to solicit savings money throughout the area.

The Division of Examinations also believed that there were significant economies available upon increases in the size of a bank to some undetermined point, but almost certainly to a size larger than would be the continuing bank if this merger were approved. Banks the size of these two, in combination would be able to effect economies that would permit improved and broadened bank services to the community. Moreover, in this particular instance there would remain within Sussex County a number of alternative sources of banking services with additional sources available in adjoining New York State and New Jersey counties, particularly Passaic County, which had some aggressive large banks.

While it could not be said with any degree of certainty, it appeared likely that the area within which New Jersey banks may branch might be enlarged by the State Legislature in the not-too-distant future. Should this happen, the large banks in neighboring Passaic and other counties might well seek to expand into Sussex County. It would seem that one of the best ways to retain locally headquartered banks would be to permit the local banks to achieve sufficient size to provide reasonably adequate banking services, to attract and retain competent management, and thus be able to compete more effectively with large banks should they be permitted to expand into the area of the smaller bank.

It was these rather intangible considerations that had disturbed the Division of Examinations. While the Division felt that, strictly speaking, denial of the application would be consistent with the Bank Merger Act, it nevertheless was not certain that the best interests of Sussex County residents might not be better served over the long run by approval of the application.

There had also been distributed a memorandum dated May 6, 1963, from the Division of Examinations transmitting two charts that had been prepared for the purpose of illustrating some of the issues involved in the proposed Sussex County Trust merger. One chart showed the hypothetical relation of the number of banks to banking alternatives; the other showed the hypothetical relation of size of bank to ability to serve.

At the Board's request, Mr. Leavitt summarized the salient points of the situation, basing his remarks primarily on the Division of Examinations memorandum of May 1. Among other comments, he stated that the Sussex County area might eventually be part of metropolitan New York. It was difficult for him to believe that the Bank Merger Act was aimed at preventing the merger of two such small banks. It might be more important to build a strong local unit that might compete with city banks that might come into the area in the future; it was a question of what kind of institution would provide the best service to the area. The proposed State legislation, mentioned in the Division of Examinations' memorandum, was a bill that would divide New Jersey into four banking districts. The district in which Sussex County would be located would also include Hudson, Bergen,

and Passaic Counties, in all of which there were large banks. If the bill became law, those banks would probably expand into Sussex County.

Mr. Shay then commented on the application, expressing the view that the reasons that might be set forth as supporting approval were more conjectural than those that might be cited as supporting denial. One of the most troublesome circumstances was perhaps a technical one, namely, that the banks involved had delayed improvements in their situations in the expectation that the merger would be approved. It was possible that they were merely more candid than other applicants, yet their admissions of deliberate delay made it more difficult to support approval of the merger, especially since there was competition between the banks and there would be more when Sussex County Trust's Vernon Township branch was opened. The adverse competitive factor reports received from the Comptroller of the Currency and the Department of Justice also weighed on the side of denial.

Mr. Hackley observed that in some cases the Board's statements on merger decisions had said that while elimination of competition was an adverse circumstance, the Board must also have concern for the general banking structure of the area. It seemed to him that the Bank Merger Act permitted the Board to look at competition in different ways - the elimination of competition in some cases, and the possible effect on the over-all banking structure in others. In the present case, it was possible that the Board might consider that the merger of two small banks near New York City might stimulate competition with New York City banks.

Governor Mitchell stated that he was uneasy as to the statements made that a strict interpretation of the Bank Merger Act would point to denial of the application. Mr. Shay responded that he was perfectly satisfied that no court would upset a decision to approve, and that there had been no intention to imply that an approval would violate the law. The Legal Division's position had been based partly on the poor record of the two banks in delaying improvements and the fact that the favorable arguments were largely conjectural.

The members of the Board then stated their positions, beginning with Governor Mills, who said that he would vote to approve. In his view, each of the two banks involved, with about $10 million each in deposits, would find it difficult individually to overcome the lead of their largest competitor, which had deposits of more than $20 million. The combination of the two smaller banks would provide more effective competition, especially in an area that was growing markedly. Governor Mills took some exception to the market area that had been chosen for studying competition. In Passaic and Morris Counties, abutting Sussex County, there were large banks not many miles from the banks that were seeking to merge. It seemed to him that approval of the merger would result in having two fair-sized banks in a growing area to offer a buffer against competitive encroachment by large banks from nearby areas at a later date. The merger also would enable Sussex County to be more self-sufficient in its banking resources rather than dependent upon banking facilities in adjoining counties. He believed that Sussex County must not be considered

as isolated but as adjacent to the other counties. Judged in relation to the large banks in those counties, the merged institution would still be a relatively small bank.

Governor Robertson stated that he would vote for denial for the reasons given by the Division of Examinations.

Governor Shepardson said that he would vote for approval, principally for the reasons cited by Governor Mills. In addition, it appeared to Governor Shepardson that the area involved was developing industrially and had need for further credit resources. Those resources were being supplied at present by the larger banks in adjoining areas. If the Board was concerned about the future of local banks, it seemed to him that there was much better prospect for the merged bank than there was for either of the two banks separately. The potential competitive situation, intangible though it might be at present, offered a possibility for the large neighboring banks to extend their activities. He considered that approval was called for in the interests of the needs of the growing industrial community and of a strong local institution.

Governor King indicated that he would vote for approval for the reasons given by Governors Mills and Shepardson.

Governor Mitchell stated that he would approve because he could not see that the damage to competition was substantial enough to warrant disapproval. He was not impressed with arguments that the merger would improve service in the area, but he was convinced that institutions such

as these, under the conditions presented, should be allowed to do what was best suited to their needs.

Governor Balderston commented that the present case was distinguished in his mind from many that had come before the Board, for the considerations that Mr. Leavitt had discussed. In his view, the Board had to be thinking ahead for some decades as to what the structure of banking might become. Because of the potential situation in the present case, plus the considerations mentioned by Governor Mills, he would vote to approve.

Chairman Martin said that he also favored approval. It seemed to him that in this case disapproval would tend to invite outside interests to take over the territory and the Board would be unable to do anything about it. As he saw it, this merger would tend to preserve local interest and ownership.

The application of Sussex County Trust Company was thereupon approved, Governor Robertson dissenting. It was understood that the Legal Division would prepare for the Board's consideration an order and statement reflecting this decision, and that a statement reflecting Governor Robertson's dissent also would be prepared.

Messrs. Young and Sanford then withdrew from the meeting and Mr. Holland, Adviser, Division of Research and Statistics, entered the room.

Application of Chemical Bank New York Trust Company. There had been distributed a memorandum dated May 13, 1963, from the Division of Examinations in connection with the application by Chemical Bank New York Trust Company, New York, New York, to acquire the assets of and assume

the liability to pay deposits made in Bank of Rockville Centre Trust Company, Rockville Centre, New York. The memorandum contained data based largely on the application, reports of examination of the two banks, and reports on competitive factors. However, it was being submitted in advance of a more comprehensive memorandum that would be distributed to the Board during the week of May 20, 1963, when the findings and conclusions of the Federal Reserve Bank of New York were available. The purpose of the present memorandum was to enable the members of the Board to familiarize themselves with the proposal and also to consider the question whether or not an oral presentation should be held. It was the feeling of the Division of Examinations that the issues in the case were fairly clear and that little would be gained by affording the bank an opportunity to make an oral presentation. It was noted that Mr. Arthur Roth, Chairman of the Board of Franklin National Bank, Franklin Square, New York, had asked to be informed as to the date a public hearing on the matter would be held. He was informed that he would be notified if a public hearing were held, but that whether or not there was to be one was a matter within the discretion of the Board.

After discussion, it was agreed that an oral presentation would not be held in regard to Chemical Bank New York Trust Company's application

Secretary's Note: The Federal Reserve Bank of New York was informed of this decision by the Board in a letter dated May 17, 1963, and was asked also to notify Mr. Roth, Chemical Bank New York Trust Company, and Bank of Rockville Centre Trust Company.

The meeting then adjourned.

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

Letter to the Presidents of all Federal Reserve Banks transmitting forms to be used by State member banks and their affiliates in submitting reports as of the next call date. (With the understanding that the letter would be sent when the forms were printed.)

Letter to the Bureau of the Budget (attached Item No. 5) regarding the terms of the detail to the Bureau on a reimbursable basis of John E. Reynolds, Chief, Special Studies and Operations Section, Division of International Finance, for a period of one year beginning May 8, 1963. The Bureau's request for Mr. Reynolds' services was approved by the Board on April 12, 1963.

Memorandum from Irene M. Fender, Statistical Clerk, Division of Research and Statistics, requesting permission to work on a part-time basis as a telephone solicitor for newspaper subscriptions to the Washington Evening Star.

Secretary

Item No. 1
5/16/63

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

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

May 16, 1963.

Mr. M. H. Strothman, Jr.,
Vice President and General Counsel,
Federal Reserve Bank of Minneapolis,
Minneapolis 2, Minnesota.

Dear Mr. Strothman:

With your letter of April 24, 1963, you forwarded in behalf of the Minneapolis law firm of Henretta, Muirhead, Oberg and Davidson, further material concerning the question presented with your letter of January 16, 1963, and its enclosures, as to whether section 32 of the Banking Act of 1933, as amended, would prohibit a vice president and director of a national bank from serving at the same time as agent of APA, Incorporated, in the sale of partnership units in programs for the development of gas and oil properties by the Apache Corporation, Minneapolis, Minnesota.

From the information that has been submitted, it appears that Apache Corporation, which explores and drills for oil and gas in the United States and Canada, acts as agent for participants in Apache Gas and Oil Programs in acquiring leases on gas and oil properties and conducting exploratory drilling thereon. These programs, which apparently have been conducted annually since 1956, have been financed by the sale of participating units in the programs which, until this year, have been conducted as joint ventures. Beginning with the Apache Gas and Oil Program 1963, the partnership business form was adopted and the partnership units of participants in the 1963 Program, for which Apache Corporation is the Managing Partner, are priced at $15,000 each.

In the Prospectus covering the Apache Gas and Oil Program 1963, a copy of which was enclosed with your earlier letter concerning the matter, it is stated that "These securities [i.e., partnership units in the Program] will be marketed on a 'best efforts' basis by Apache [Corporation], as issuer and by its wholly-owned subsidiary, APA, Incorporated, as underwriter and managing agent of a selling group."

Briefly, it appears further that subscriptions to partnership units in the 1963 Program in excess of $15,000 may be made in multiples of $5,000, and that the subscription price is payable in installments. The commencement of any such program depends on whether a stated minimum

total of subscriptions is obtained. If not obtained, the subscriptions terminate and funds received in payment thereof are returned to the investors. Provision is made for disposition of the partnership units by investors without discontinuance of the particular program, any change in which must be put to the vote of the investors. Gains and losses of any program are allocated to the accounts of the investors in a ratio that their subscriptions bear to the total subscriptions of the program.

Section 32 of the Banking Act of 1933 provides as follows:

> "No officer, director, or employee of any corporation or unincorporated association, no partner or employee of any partnership, and no individual, primarily engaged in the issue, flotation, underwriting, public sale, or distribution, at wholesale or retail, or through syndicate participation, of stocks, bonds, or other similar securities, shall serve the same time as an officer, director, or employee of any member bank except in limited classes of cases in which the Board of Governors of the Federal Reserve System may allow such service by general regulations when in the judgment of the said Board it would not unduly influence the investment policies of such member bank or the advice it gives its customers regarding investments."

There is no indication in the material submitted with your letters that APA, Incorporated, is engaged in any activity other than the marketing of program or partnership units, as related above. It is concluded, therefore, that APA, Incorporated, is "primarily engaged" in that activity.

In the enclosures with your letters counsel to Apache Corporation urges that the partnership units are not "securities" of a kind covered by section 32. Following careful consideration of the matter, the Board is of the view that the partnership units fall within the language of the statute. The Board believes that the statute clearly is sufficiently broad to comprehend securities which, while neither stocks nor bonds, have attributes which cause them to be somewhat like either bonds or stocks.

Counsel to Apache Corporation also suggests that an interlocking relationship in the circumstances in question would not be likely to involve abuse of the kind that the statute was intended to prevent. Cases have arisen under the statute from time to time in which it was contended that improper action by the parties involved was highly improbable and that the application of the statute resulted in some

hardship. However, as indicated in the decision in Board of Governors v. Agnew, 329 U. S. 411 (1947), section 32 is aimed at relationships which present the opportunity for improper action, regardless of whether abuses actually exist in specific cases. It should be noted also that, under the statute, it is only by "general regulations" that the Board has authority to exempt relationships which, in its judgment, would not be a source of undue influence. As you know, the Board's Regulation R is limited to situations not related to the case in question.

In view of the foregoing, and on the basis of its understanding of the information submitted, it is the Board's view that an officer, director, or employee of a national bank may not, at the same time, serve as agent of APA, Incorporated, in the marketing of partnership interests in Apache Gas and Oil Programs.

It would be appreciated if your Bank would convey the views expressed herein to either Mr. John A. Muirhead or Mr. Arthur Rubenstein of Henretta, Muirhead, Oberg and Davidson.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.

Item No. 2
5/16/63

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

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

May 16, 1963.

Edward J. Neithercut, Esq.,
Neithercut & Neithercut,
Suite 704, Genesee Bank Building,
Flint 3, Michigan.

Dear Mr. Neithercut:

This refers to your letter, dated May 7, 1963, to Mr. Leland Ross, Vice President, Federal Reserve Bank of Chicago, on behalf of the Genesee Merchants Bank & Trust Co., Flint, Michigan, advising of the request by the America Fore Loyalty Group, the company which issued the fidelity bond for the Davison State Bank, Davison, Michigan, for copies of the reports of examination of the Davison State Bank for the years 1957-1962 prepared by examiners of the Federal Reserve Bank of Chicago. It is understood that the copies of reports of examination referred to are those in the possession of the Genesee Merchants Bank & Trust Co. into which bank the Davison State Bank merged in November 1962, and that the request is said to relate to numerous claims filed by Genesee Merchants Bank & Trust Co. under the fidelity bond issued by America Fore Loyalty Group.

Section 261.2(b)* of the Board's Rules Regarding Information, Submittals, and Requests (12 CFR Part 261) provides that, with certain exceptions not here applicable, the Board will not make available or otherwise disclose reports of examination of any particular bank unless "the Board deems such disclosure to be in the public interest". Upon consideration of the several interests involved in this request, including that of America Fore Loyalty Group in responding to the claims filed, the Board has concluded that furnishing of the reports under the circumstances stated would not be in the public interest. Accordingly, the Board declines to authorize the Genesee Merchants Bank & Trust Co. to furnish copies of or otherwise make available information from reports of examination of the Davison State Bank prepared by examiners of the Federal Reserve Bank of Chicago.

Very truly yours,

*Reference should have been made to Section 261.2(d)

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.

Item No. 3
5/16/63

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

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

May 16, 1963.

Mr. Leland M. Ross, Vice President,
Federal Reserve Bank of Chicago,
Chicago 90, Illinois.

Dear Mr. Ross:

This will acknowledge your letter of May 8, 1963, enclosing a copy of a May 7 letter from counsel for the Genesee Merchants Bank & Trust Co., Flint, Michigan, wherein a request is made for permission for the Genesee Bank to make available to the America Fore Loyalty Group, copies of reports of examination of Davison State Bank, Davison, Michigan, prepared by Federal Reserve Bank examiners during the years 1957 through 1962. It is understood that the America Fore Loyalty Group had issued the fidelity bond under which Davison State Bank operated prior to its merger with the Genesee Bank in November 1962. You advise that Genesee Bank has filed 101 claims under the fidelity bond in respect to losses allegedly suffered by Davison State Bank as a result of alleged manipulations by an officer and an employee of the latter bank, and that in connection with such claims, America Fore Loyalty Group, with the consent of the Genesee Bank, seeks copies of the reports of examination of Davison State Bank for the periods mentioned.

The Board's ability to fully appraise the assistance that might be rendered America Fore Loyalty Group through access to the reports of examination in question is substantially impeded by the fact that the request fails to identify the nature of the claims filed by the Genesee Bank, what portions, if any, of some or all of the reports of examination are relevant to the claims filed, or whether part or all of the information sought, whatever its nature, is not equally available from retained records of the Davison State Bank, or elsewhere. On the basis of the information before the Board, it would appear that a major portion of any one or all of the reports of examination sought would not be relevant to claims filed under the fidelity bond, and that disclosure of the confidential contents of these reports would not be in the public interest.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

It will be appreciated if you will transmit to counsel for the Genesee Merchants Bank & Trust Co. the enclosed letter whereby the Board declines to authorize the disclosure requested.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.

Enclosure

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

Item No. 4
5/16/63

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

May 16, 1963.

Mr. Phillip S. Hughes,
Assistant Director for
Legislative Reference,
Bureau of the Budget,
Washington 25, D. C.

Dear Mr. Hughes:

This refers to Legislative Referral Memorandum dated May 13, 1963, requesting the Board's views regarding a preliminary draft bill "To provide for an increase in the maximum amount of insurance coverage for bank deposits and savings and loan accounts, to protect further the safety and liquidity of insured institutions, to strengthen safeguards against conflicts of interest, and for other purposes."

On April 25, 1963, Vice Chairman Balderston of the Board appeared before the House Banking and Currency Committee in connection with hearings on the bill H.R. 5130 that would have increased the limit on insurance coverage of deposits in banks insured by the Federal Deposit Insurance Corporation and share accounts in institutions insured by the Federal Savings and Loan Insurance Corporation from $10,000 to $25,000 for each deposit or account. As indicated in the Vice Chairman's statement at that time, it was the Board's view that the proposed increase in insurance coverage to $25,000 would not be in the public interest, but that, if any increases are appropriate, they should be small and infrequent and that effective supervision over the institutions covered is an important prerequisite to insurance protection.

The preliminary draft bill would (1) increase insurance coverage for both banks insured by the FDIC and institutions insured by the FSLIC from $10,000 to $15,000; (2) require the maintenance of reserves against time and savings deposits by nonmember insured banks and against withdrawable accounts by institutions that are members of the Federal Home Loan Bank System; (3) give nonmember insured banks access to Federal Reserve discounts and advances; (4) make provision for assuring the liquidity of all insured banks and all members of the Home Loan Bank System; (5) place on a standby basis the authority of the Board of Governors and the FDIC to fix maximum interest rates payable by member

banks and nonmember insured banks on time and savings deposits, and authorize the Federal Home Loan Bank Board similarly to fix maximum dividend rates payable by members of the Home Loan Bank System on share accounts; and (6) strengthen and make applicable to all insured banks and members of the Home Loan Bank System certain provisions of present law that are designed to prevent conflicts of interest in dealings by financial institutions with directors, officers, and employees, public examiners, and affiliates of such institutions.

The Board would interpose no objection to the small increase in insurance coverage proposed by the draft bill, in view of the inclusion of provisions regarding regulation of dividend rates paid by member institutions of the Home Loan Bank System, reserves and liquidity requirements for such institutions, and the strengthening and extension of the applicability of present conflict-of-interest provisions.

With respect to the reserve requirement provisions of the bill, however, the Board favors the extension of such reserve requirements to all commercial banks, not only for time deposits but also for demand deposits, as recommended in the Report of the President's Committee on Financial Institutions. Extension of reserves against time deposits to nonmember insured banks, without a like extension of reserves against demand deposits, would result in an inequitable situation, if the quid pro quo were the privilege of borrowing from the Federal Reserve. With access to Federal Reserve credit facilities, nonmember banks would have a major advantage of membership in the Federal Reserve System without being subject to reserve requirements against demand deposits and without assuming other responsibilities that are assumed by members of the System. Moreover, in connection with extension of reserve requirements against demand deposits to nonmember banks, it would be important to change the existing structure of reserve requirements in order to provide a more logical and equitable basis for such requirements, such as the graduated basis recommended by the Committee on Financial Institutions.

For these reasons, the draft bill would be acceptable in principle to the Board of Governors only if modified to include reserve requirement provisions in accordance with the views here expressed. Any bill of this kind relating to such important matters necessarily must be the subject of further careful technical review; and the Board, of course, reserves the right to consider and comment upon detailed provisions of any such bill that may be introduced in Congress.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.

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

Item No. 5
5/16/63

May 16, 1963.

Mrs. Velma N. Baldwin,
Personnel Officer,
Bureau of the Budget,
Executive Office of the President,
Washington 25, D. C.

Dear Mrs. Baldwin:

In accordance with your letter of May 8, 1963, the Board of Governors approves the reimbursable detail of Mr. John E. Reynolds to the Review Committee for Balance of Payments Statistics effective May 8, 1963, for a period of one year.

The Board is agreeable to this reimbursable detail in the manner as set forth in your letter. It is understood that the Bureau will reimburse the Board for Mr. Reynolds' salary and related expenses with the exception of the reimbursement for purposes of retirement, which will be limited to the rate contributed by Civil Service agencies to the Civil Service Retirement Fund (currently 6-1/2 per cent).

It is expected that the Board's Office of the Controller will submit a voucher on a quarterly basis for this reimbursement. The time and attendance reports for Mr. Reynolds mentioned in your letter may be submitted direct to the Board's Division of Personnel Administration.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.