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Minutes for November 29, 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

nm

Gov. Mills

[Signature]

Gov. Robertson

[Signature]

Gov. Balderston

[Signature]

Gov. Shepardson

[Signature]

Gov. Mitchell

[Signature]

Gov. Daane

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Minutes of a meeting of the available members of the Board of Governors of the Federal Reserve System on Friday, November 29, 1963. The meeting was held in the Board Room at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Mills
Mr. Robertson

Mr. Sherman, Secretary
Mr. Kenyon, Assistant Secretary
Mr. Young, Adviser to the Board and Director,
Division of International Finance
Mr. Hackley, General Counsel
Mr. Noyes, Director, Division of Research
and Statistics
Mr. Farrell, Director, Division of Bank
Operations
Mr. Solomon, Director, Division of Examinations
Mr. Johnson, Director, Division of Personnel
Administration
Mr. Holland, Adviser, Division of Research
and Statistics
Mr. Conkling, Assistant Director, Division
of Bank Operations
Mr. Daniels, Assistant Director, Division
of Bank Operations
Mr. Kiley, Assistant Director, Division
of Bank Operations
Mr. Smith, Assistant Director, Division
of Examinations
Mr. Mattras, General Assistant, Office
of the Secretary
Mr. Collier, Chief, Current Series Section,
Division of Bank Operations
Mr. Ring, Technical Assistant, Division
of Bank Operations

The following actions were taken subject to ratification at the next meeting of the Board at which a quorum was present:

Discount rates. The establishment without change by the Federal Reserve Banks of Cleveland, Richmond, St. Louis, Minneapolis, and Kansas City on November 27, 1963, of the rates on discounts and advances in

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their existing schedules was approved unanimously, with the understanding that appropriate advice would be sent to those Banks.

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

	<u>Item No.</u>
Letter to The Marine Trust Company of Western New York, Buffalo, New York, approving the establishment of a branch in the Town of Orchard Park.	1
Letter to The Chase Manhattan Bank, New York, New York, approving the establishment of a branch at 1501 Avenue M, Borough of Brooklyn.	2
Letter to Princeton Bank and Trust Company, Princeton Township, New Jersey, approving the establishment of a branch at U. S. Route 206 and Mt. Rose-Rocky Hill Road.	3
Letter to City Trust Company, Bridgeport, Connecticut, approving the operation of branches at 2366 Main Street and 3226 Main Street, Stratford, providing the proposed merger of City Trust Company and The Stratford Trust Company is approved and consummated.	4
Letter to The Guaranty National Bank of Oklahoma City, Oklahoma City, Oklahoma, granting its request for permission to maintain reduced reserves.	5
Letter to United California Bank, Los Angeles, California, approving the establishment of a branch in Garden Grove.	6
Letter to The Sterling State Bank, Mount Sterling, Ohio, approving the declaration of a dividend payable on December 31, 1963.	7

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Reserve deficiencies. Reference was made to a memorandum dated November 27, 1963, that had been addressed to the Federal Open Market Committee and Presidents of the Federal Reserve Banks by Mr. Stone, Manager of the System Open Market Account, and Mr. Farrell, Director of the Division of Bank Operations, with respect to procedures for allocation of the System Open Market Account. The memorandum outlined the three principal elements of the present procedures and noted that they had prevented any Reserve Bank from showing a reserve deficiency on a weekly statement date. The procedures, however, did not insure avoidance of a deficiency by some Reserve Bank or Banks on other than a statement date (an "intra-weekly" deficiency), and it appeared that one or more Reserve Banks might incur intra-weekly deficiencies over the next few weeks. It was suggested that there were three principal alternatives: (a) leave the present procedures unchanged; (b) employ, on days other than statement dates, the "as of" adjustments now employed for statement dates; (c) choose to let intra-weekly deficiencies occur without attempting remedial adjustments.

Mr. Sherman pointed out that the procedures for allocation of the Open Market Account had traditionally been established by the Federal Open Market Committee, which had proceeded on the assumption that it was desirable to avoid reserve deficiencies. However, the policy question whether such deficiencies should be tolerated had always been considered a matter for determination by the Board, or by the Board in consultation with the Presidents of the Federal Reserve

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Banks. In other words, the question of policy involved was whether the Board saw an objection to permitting a deficiency to occur if the current allocation procedures did not avoid it. Deficiencies had occurred in the past, and taxes had been paid by the Reserve Banks. The Open Market Committee, in determining procedures for allocation of the Open Market Account, should know whether, in the Board's view, it was an over-riding objective to avoid deficiencies at all costs as long as anywhere in the System there were enough gold certificate reserves to prevent such deficiencies from occurring.

Chairman Martin commented that it had been his thought that there might be some preliminary consideration of the subject today, with further discussion next Monday when a quorum of the Board would be available.

In the discussion that followed, Governor Mills expressed the view that it would be preferable to assess taxes for any deficiencies in accordance with the statute rather than to go through complicated adjustment procedures in an effort to avoid reserve deficiencies.

Governor Robertson expressed the view that a System operation was involved. Open market operations were entered into for System policy purposes, and as a result of those operations it was necessary to make allocations of the Open Market Account. The manner in which this was done was primarily a matter of bookkeeping. The question was whether a deficiency at any one Bank should be allowed to occur, at a

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time when other Banks had surplus reserves, simply because the existing allocation procedure led to that result.

Mr. Young commented that the fact that the Open Market Committee had gone through the process of revising its reallocation formula had become known in the market, and it was not particularly a good thing to continue to go through revisions of the formula. This went to the broad question to which Governor Mills had referred. The problem was one that could develop to an acute stage within a year or two. One approach would be to allow occasional deficiencies to occur, with announcement of any such deficiencies in the Board's Annual Report, as part of a conditioning process.

Mr. Hackley observed that if there should be deficiencies against note or deposit liabilities, a tax would be automatic. A recent letter from Chairman Martin to Chairman Douglas of the Joint Economic Committee had made that clear. The letter further pointed out, however, that until gold reserves went so low that the requirements against note liabilities could not be met by transfers from reserves against deposits, there would not be the more serious problem of adding to the discount rate. Also, until the reserve against note liabilities went below 20 per cent, technically the Board could establish some minimal rate of tax.

Mr. Farrell pointed out that a Reserve Bank could be deficient occasionally without any need to suspend reserve requirements, which would be suspended only where it appeared that a Bank would be continually

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deficient. Rather than let a suspension of reserve requirements for one or more Banks suddenly become known publicly, there might be some psychological advantage in permitting reserve deficiencies to occur occasionally and indicating to the public that there was nothing more involved than a matter of bookkeeping.

Chairman Martin noted that while there could be psychological advantages, there might also be certain disadvantages. This would raise, sooner than would necessarily be the case, the whole question of the sufficiency of gold reserves to meet statutory requirements. This was a problem that the System was going to have to consider fully over the coming months.

Mr. Sherman suggested that the Board might wish to discuss the subject at a meeting with the Presidents of the Federal Reserve Banks. The subject could be discussed at a meeting of the Open Market Committee, but that Committee did not have the responsibility for assessing a tax if a deficiency should occur, or for suspending reserve requirements. As had been indicated, the question was one of general policy: whether a reserve deficiency should be accepted in an occasional instance at some Federal Reserve Bank, or whether everything possible should be done to avoid any such deficiency.

Messrs. Young, Noyes, Daniels, Mattras, and Ring then withdrew from the meeting.

Examination of Chicago Reserve Bank. There had been circulated to the Board the report of examination and the usual accompanying papers

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relating to the examination of the Federal Reserve Bank of Chicago made by the Board's examining staff as of June 21, 1963.

At the Board's request, Mr. Smith commented on the information developed through the examination. In the course of his comments he referred, among other things, to the frequency of borrowing from the Reserve Bank on the part of one larger and two smaller member banks, along with the reasons to which the necessity for such borrowing was attributed.

Turning to the subject of member banks frequently deficient in required reserves, Mr. Smith pointed out that The Michigan Bank, National Association, Detroit, Michigan, was deficient in 20 of the 52 weekly reserve computation periods in 1962 and in 5 of the 25 periods through June 19, 1963. Nineteen of the resulting penalties were waived under paragraph C of the Board's letter S-1123, dated October 10, 1949 (FRLS #6120). The report of examination indicated that this bank's frequent deficiencies were discussed with the Reserve Bank management, which advised that since it was a policy of long standing to disregard deficiencies waived under paragraph C of the Board's letter, the matter of maintaining adequate reserves had not been discussed with the member bank. Paragraph C, Mr. Smith pointed out, provides that when a member bank is deficient in reserves during any reserve computation period, the penalty may be waived at the discretion of the Reserve Bank to the extent that the deficiency is offset by excess reserves during the immediately following reserve computation period, provided such deficiency

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does not exceed 2 per cent of the member bank's required reserves. The attitude of the Chicago Reserve Bank toward paragraph C seemed tantamount to allowing a reserve city bank to average its reserves on a bi-weekly rather than a weekly basis, and allowing a country bank to average on a quad-weekly rather than a bi-weekly basis. If so, it appeared that the Chicago Reserve Bank might be exceeding the discretion the Board intended to authorize.

Mr. Smith went on to say that if the matter was to be brought to the attention of the Federal Reserve Bank of Chicago, it would seem that there should be a general review of the Board's outstanding letter to eliminate any ambiguities. Also, a copy of any clarifying letter should be sent to all Federal Reserve Banks to let them know the Board's thinking.

Governor Mills commented that a broad issue was involved. Here a reserve city bank was attempting to enjoy the privilege of a country bank to average its reserves over two weekly computation periods. The Reserve Bank apparently was extending to the national bank in Detroit a privilege not enjoyed generally by member banks throughout the country.

Mr. Farrell said that in the year 1960 about 700 penalties were waived under paragraph C; of these, 450 were waived by the Chicago Reserve Bank. This had been a practice of long standing at Chicago. The inconsistency between the Chicago Bank's attitude and the attitude of the other Reserve Banks was somewhat disturbing.

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Mr. Holland said that available statistics suggested that a good many larger reserve city banks around the country were using this privilege occasionally. In 1963, through the middle of November, a small group of the larger banks tended to use this privilege in about one-eighth of the weeks. In the Atlanta District, one bank used the privilege nearly half the time. It appeared that the practice may have spread in recent years. It was a privilege available to country banks also, thus enabling them to spread adjustments over a four-week settlement period. A case could be made that this was a useful kind of device in the sense of not driving the banks to the last nickel of adjustment, especially on Wednesdays.

Chairman Martin raised the question whether definite harm was seen in the practice, and Governor Mills commented that in the computation of reserve requirements a deficiency may be partially offset in the next reserve computation period. However, a bank could not have a surplus in one reserve week and use it to cover a deficiency in the succeeding week. Mr. Smith said that, as he saw it, the only harm was that there was a rule in existence, and if such a rule was not lived up to on a consistent basis, it was of questionable value.

Chairman Martin then asked whether a change in the rule should be considered, and Mr. Holland commented that on various occasions this privilege alleviated the kinds of pressure that banks of all sizes could get caught in on the last day of reserve computation periods.

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He thought that something could be said for making the privilege symmetrical and allowing a small excess of reserves to be carried forward.

Governor Mills again commented that a broad question was involved; that is, whether there should be a gradual breakdown in the discipline applied to member banks at a time when such banks should be keenly aware of their obligations of membership.

Governor Robertson said that, as he saw it, the main problem was whether or not favoritism was evident on behalf of a certain member bank or banks as against other banks. It appeared to him that favoritism was indicated. The Chicago Reserve Bank had been more free in extending this privilege than any other Reserve Bank, and some member banks had used it more than others.

Mr. Conkling commented on the origin of the limited privilege extended through paragraph C and expressed the view that the Chicago Reserve Bank was living up to the rules as it understood them. The Board's letter stipulated that certain penalties might be waived at the discretion of a Federal Reserve Bank. In its discretion, another Reserve Bank might take an attitude different from that of the Chicago Bank.

Mr. Solomon commented that the Atlanta Bank had been concerned about the development of the practice in its District. One member bank in that District seemed to be doing this rather frequently. The Atlanta Bank had been inclined to waive the penalties up to now, but

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it was becoming somewhat concerned as to whether it was following the proper practice. He had told the Atlanta Bank that the question was one that had come up elsewhere and was under review.

Question was raised as to whether the issue might be taken up by Mr. Holland at a meeting of the Reserve Bank discount officers, but Mr. Holland expressed the view that the issue was a broader one than would be appropriate for discussion in that forum.

Chairman Martin then suggested that Mr. Farrell prepare a memorandum on the subject preparatory to thorough review by the Board.

Mr. Sherman suggested that the Board also might want to have in mind discussing the matter with the Conference of Presidents once the Board had interpreted the meaning of its S-letter.

Governor Mills then referred to a collateral subject that he considered fundamental and important. Federal funds originally had been used primarily to make up deficiencies in reserve accounts, but now they were being used in a widespread manner to support the asset structure of banks. The Comptroller of the Currency had ruled that Federal funds transactions involved purchases and sales, and did not have to be reflected as loans and borrowings, while the Board more properly regarded them as loans and borrowings.

Governor Mills recalled that he had raised the question of risk some years ago with the Board's former General Counsel, who was satisfied that there was no great risk involved at that time. If a bank should fail, however, and if it had borrowed Federal funds in

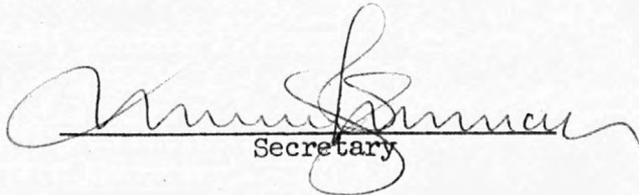
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substantial amount, the lender of those funds would have established a credit substantially in excess of the borrowing bank's deposit insurance protection. The lending bank would have a claim, but it would be vital to determine whether it was a general claim or a preferred claim. This, he thought, the Board ought to investigate. If a borrowing bank failed, and if the lending bank's claim was not a preferred claim, the lending bank could be in real trouble.

The meeting then adjourned.

Secretary's Note: Pursuant to the procedure approved by the Board on October 12, 1960, relating to examinations of Edge Act and agreement corporations by examiners for the Federal Reserve Banks of New York and Philadelphia, acting as examiners for the Board of Governors, a letter was sent today to the Federal Reserve Bank of San Francisco authorizing a similar arrangement in that District for examinations of International Bank of Commerce, Seattle, Washington, and Wells Fargo Bank International Corporation, San Francisco, California.


Secretary

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Item No. 1
11/29/63

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

WASHINGTON, D. C. 20551

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

November 29, 1963



Board of Directors,
The Marine Trust Company of Western New York,
Buffalo, New York.

Gentlemen:

The Board of Governors of the Federal Reserve System approves the establishment by The Marine Trust Company of Western New York, Buffalo, New York, of a branch approximately 100 feet north of the junction of Orchard Park Road and Union Road, Town of Orchard Park, (Unincorporated Area), Erie County, New York, provided the branch is established within one year from the date of this letter.

Very truly yours,

(Signed) Kenneth A. Kenyon

Kenneth A. Kenyon,
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.)

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

Item No. 2
11/29/63

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

November 29, 1963

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 at 1501 Avenue M, Borough of Brooklyn, Kings County, 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) Kenneth A. Kenyon

Kenneth A. Kenyon,
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 GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

WASHINGTON 25, D. C.

Item No. 3
11/29/63

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

November 29, 1963



Board of Directors,
Princeton Bank and Trust Company,
Princeton Township, New Jersey.

Gentlemen:

The Board of Governors of the Federal Reserve System approves the establishment by Princeton Bank and Trust Company, Princeton Township, New Jersey, of a branch at the southeast corner of the intersection of U. S. Route 206 and Mt. Rose-Rocky Hill Road (also known as Cherry Valley Road), Princeton Township, New Jersey, provided the branch is established within one year from the date of this letter.

Very truly yours,

(Signed) Kenneth A. Kenyon

Kenneth A. Kenyon,
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.)

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BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

Item No. 4
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ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

November 29, 1963

Board of Directors,
City Trust Company,
Bridgeport, Connecticut.

Gentlemen:

The Board of Governors of the Federal Reserve System approves the operation of branches by City Trust Company, Bridgeport, Connecticut, at 2366 Main Street and 3226 Main Street, Stratford, Connecticut, providing the proposed merger of City Trust Company, Bridgeport, Connecticut and The Stratford Trust Company, Stratford, Connecticut, is approved and consummated.

Very truly yours,

(Signed) Kenneth A. Kenyon

Kenneth A. Kenyon,
Assistant Secretary.

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

Item No. 5
11/29/63



ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

November 29, 1963

Board of Directors,
The Guaranty National Bank
of Oklahoma City,
Oklahoma City, Oklahoma.

Gentlemen:

With reference to your request submitted through the Federal Reserve Bank of Kansas City, the Board of Governors, acting under the provisions of Section 19 of the Federal Reserve Act, grants permission to The Guaranty National Bank of Oklahoma City to maintain the same reserves against deposits as are required to be maintained by nonreserve city banks, effective as of the date it opens for business.

Your attention is called to the fact that such permission is subject to revocation by the Board of Governors.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Item No. 6
11/29/63

WASHINGTON 25, D. C.

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

November 29, 1963



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

Gentlemen:

The Board of Governors of the Federal Reserve System approves the establishment of a branch by United California Bank in the vicinity of the intersection of Brookhurst Street and Chapman Avenue, Garden Grove, Orange County, California, provided the branch is established within one year from the date of this letter.

Very truly yours,

(Signed) Kenneth A. Kenyon

Kenneth A. Kenyon,
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.)

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Item No. 7
11/29/63

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



ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

November 29, 1963

Board of Directors,
The Sterling State Bank,
Mount Sterling, Ohio.

Gentlemen:

The Board of Governors has received from the Federal Reserve Bank of Cleveland a copy of President R. G. Webber's letter dated November 6, 1963, in which he requests permission for the declaration of a dividend by The Sterling State Bank of \$2,400 payable December 31, 1963.

After consideration of the facts, the Board approves the declaration of the above-mentioned dividend. This letter does not authorize the declaration of any other dividend in 1963 or later.

Very truly yours,

(Signed) Kenneth A. Kenyon

Kenneth A. Kenyon,
Assistant Secretary.