Minutes for February 17, 1964

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

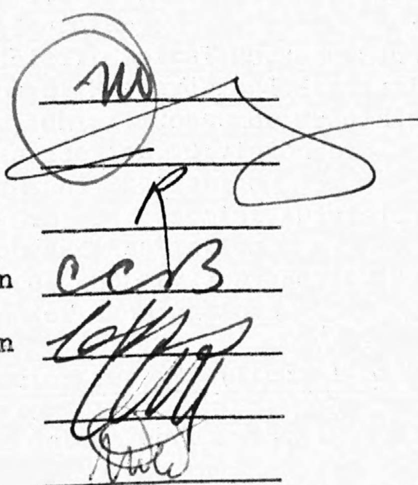
Gov. Robertson

Gov. Balderston

Gov. Shepardson

Gov. Mitchell

Gov. Daane



Minutes of the Board of Governors of the Federal Reserve System on Monday, February 17, 1964. 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. Mitchell
Mr. Daane

Mr. Sherman, Secretary
Mr. Kenyon, Assistant Secretary
Mr. Noyes, Adviser to the Board
Mr. Molony, Assistant to the Board
Mr. Cardon, Legislative Counsel
Mr. Fauver, Assistant to the Board
Mr. Hackley, General Counsel
Mr. Johnson, Director, Division of Personnel Administration
Mr. Hexter, Assistant General Counsel
Mr. Shay, Assistant General Counsel
Mr. Hooff, Assistant General Counsel
Mr. Holland, Associate Director, Division of Research and Statistics
Mr. Dembitz, Associate Adviser, Division of Research and Statistics
Mr. Sprecher, Assistant Director, Division of Personnel Administration
Mrs. Semia, Technical Assistant, Office of the Secretary
Mr. Keir, Chief, Capital Markets Section, Division of Research and Statistics
Mr. Osborne, Chief, Consumer Credit and Finances Section, Division of Research and Statistics
Mr. Smith, Senior Economist, Division of Research and Statistics
Mr. McClintock, Supervisory Review Examiner, Division of Examinations

Release of competitive factor reports (Items 1 and 2). There had been distributed a memorandum dated February 4, 1964, from the Legal Division and the Division of Examinations describing circumstances

pointing to the possibility that the Board might wish to consider whether to relax its present practice relating to the release of reports on competitive factors in bank merger cases. Two requests were pending: Oscar R. Goodman, Associate Professor of Finance, Northwestern University, had asked for the reports to the Board by the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the Department of Justice in connection with two cases decided by the Board in December 1963; and Manufacturers and Traders Trust Company, Buffalo, New York, had asked for the Department of Justice's report to the Board on that bank's application to merge with Bank of Jamestown, Jamestown, New York. (Action by the Board on that application became unnecessary following denial of the proposal by the New York State banking authorities on December 30, 1963.)

It was brought out in the memorandum that the "Internal Board Procedures with Respect to Holding Company and Merger Applications" would permit granting the pending requests if release of the reports was authorized by the agencies submitting them to the Board; however, the Board's general practice concerning the release of reports both to it and by it had been restrictive. The memorandum reviewed the position taken by the Board with respect to the general question of release of reports, along with the particular circumstances in which the Board had granted requests, and described the pertinent practices of the Comptroller and the Federal Deposit Insurance Corporation. In view of experience thus far under the Bank Merger Act, the Legal Division and the Division of Examinations recommended (1) that the two pending requests be granted;

(2) that, with respect to reports to the Board on competitive factors from each of the three other agencies, the Board adopt the practice of sending copies promptly to the applicant and supplying copies to anyone else upon request; and (3) that, with respect to reports by the Board on applications pending before either of the other two banking agencies, the Board adopt the practice of supplying copies of such a report to anyone on request following the mailing of the report to the other agency. Arguments for and against these recommendations were set out in the memorandum, and attached was a draft of letter, for use in the event the Board adopted the recommendations, that would so inform the Presidents of the Federal Reserve Banks. Also in that event, it was suggested that the substance of the recommendations be incorporated into the unpublished "Internal Board Procedures," and a draft of amendment to accomplish that purpose was attached.

After comments by Messrs. Hackley and Shay supplementing the memorandum, there ensued a discussion during which Governor Mills said that he saw no great urgency in adopting the steps recommended, and some benefit in setting the matter aside to be reviewed at a later date. It concerned him that the public might misinterpret the significance of the reports. They concerned the competitive factor only, as to which the Board might take a view quite different from the one it would take on the basis of all factors if the case fell within the Board's decision area. The increasing interest of the legal and banking fraternities in picking up the trend of the Board's thinking might easily lead them

to lose sight of the limited scope of the competitive factor reports. Also, the release of reports in advance of decision by the responsible agency could subject that agency to pressure. Moreover, the Federal Deposit Insurance Corporation had a new Board Chairman, with another director scheduled to take office in the near future, which suggested the possible desirability of waiting until the thinking of that agency had crystallized. If possible, the practice with respect to releasing reports should be coordinated among all three bank supervisory agencies.

Governor Robertson, while expressing himself as not objecting to release of the reports after the expiration of the thirty-day period allowed for their submission, suggested that such a practice be based on a formal written understanding with the other supervisory agencies rather than an informal staff arrangement.

Governor Balderston, with reference to the point made by Governor Mills as to the possible inclination of the public to place too broad a significance on the competitive factor reports, suggested that the format of the reports might be revised to include a prominent headline or other device to emphasize that they related only to competitive factors.

After further discussion, it was agreed, in view of the reservations expressed, that the recommendations regarding the release of competitive factor reports would be brought back to the Board for further consideration in approximately thirty days, prior to which time the views of the Office of the Comptroller of the Currency and the Federal

Deposit Insurance Corporation could be solicited informally. It was also agreed that the agencies concerned would be consulted as to whether they would have any objection to the Board's furnishing copies of their reports in response to the two pending requests and, if they had none, that the requests would be granted.

> Secretary's Note: It having been ascertained that the Department of Justice had no objection to having its competitive factor report on the proposed Manufacturers and Traders Trust-Bank of Jamestown merger furnished to Manufacturers and Traders, a letter was sent to the Federal Reserve Bank of New York on February 18, 1964, furnishing a copy of the report for transmission to the bank. A copy of the letter is attached as Item No. 1. Similarly, appropriate clearance having been obtained, the reports requested by Professor Goodman were sent to him on March 6, 1964. A copy of the letter of transmittal is attached as Item No. 2.

Payment of interest on "borrowed" funds (Item No. 3). There had been distributed a memorandum dated February 7, 1964, from the Legal Division regarding inquiries as to the legality of arrangements under which member banks transfer a portion of a customer's demand deposit account to a "borrowed money" account on which interest is paid. In recent years, several of the Reserve Banks had made such inquiries, the question ordinarily being whether such arrangements constituted payment of interest on demand deposits, prohibited by section 19 of the Federal Reserve Act. The situations also raised other questions, such as the extent to which member banks are required to maintain reserves against such accounts in accordance with section 19

and Regulation D, Reserves of Member Banks. Up to the present time, the Board had not found it necessary to express an opinion on these matters. However, Wachovia Bank and Trust Company, Winston-Salem, North Carolina, had now inquired through the Federal Reserve Bank of Richmond as to the permissibility under the Board's Regulation Q, Payment of Interest on Deposits, of arrangements for transmuting "due-to balances into bills payable overnight or for other short periods," interest being paid on the amount of such "loans." Wachovia had stated that the practice was "of enough import and widespread enough that a published ruling should be used to acquaint all banks" with the Federal Reserve position. In order to bring the problem into focus, Wachovia presented the following hypothetical case: "Bank A calls its city correspondent, Bank B, and says, 'We have on deposit with you X dollars which we would like to invest for a certain period of time.' Bank B says, 'Fine, we will borrow these funds from you at the Federal funds rate.' These funds are then transferred from due-to banks on Bank B's books to bills payable, and Bank A is paid interest on the funds. It is our understanding that there is no note, participation agreement, or other evidence of debt used."

At first glance, the memorandum continued, the answer seemed rather obvious. If deposit liabilities could be changed into loan liabilities by a simple bookkeeping transaction, the prohibition against payment of interest on demand deposits could be largely nullified, and the System's regulation of bank credit through control of the volume

of reserves could be greatly impeded. Accordingly, the immediate reaction was to regard arrangements of this kind as devices for the indirect payment of interest on demand deposits, and therefore as prohibited by section 19 and Regulation Q. However, upon analysis the Legal Division had encountered difficulties in taking that position. Those difficulties resulted principally from the absence of any realistic test (as distinguished from formal accounting-terminology tests, which were useless for this purpose) for differentiating the deposit liabilities of a bank from its loan liabilities, at least in the twilight zone of these transactions.

After discussing legal aspects of a bank's power to borrow and the definition of "deposits," the memorandum pointed out that probably the principal mechanism for what was generally regarded as borrowing between banks (and to a lesser extent, between banks and others) was the so-called "sale" and "purchase" of deposit balances on the books of the Federal Reserve Banks, or Federal funds transactions. The existence and status of that practice, and its acceptance as giving rise to a loan rather than a deposit seemed to be at the heart of the problem. (It was noted that the Comptroller of the Currency had held in 1963 that a Federal funds transaction between banks was not a loan transaction "but is to be considered a purchase and sale of such funds"--an interpretation that the Legal Division, like the Board itself, was unable to accept.) The memorandum then presented an extensive exposition of the development and nature of Federal funds transactions, and

the extent to which they paralleled the kind of transaction about which Wachovia Bank and Trust Company had recently inquired.

It was concluded that the kind of transaction presented by Wachovia seemed to be indistinguishable, on any clearly defensible ground, from permissible Federal funds transactions. In other words, upon analysis it appeared that a member bank may lawfully designate any amount of its customers' deposits as "borrowed money" and pay interest thereon, even though the funds might constitute, in effect although not in form, demand deposits immediately available for withdrawal by check or otherwise.

Up to the present, this procedure had been followed by banks only with respect to their correspondent banks and large corporate depositors. It might be surmised that most banks would be opposed to its spreading to the deposits of individuals, partnerships, and corporations generally, since that would simply constitute an additional item of expense to the banking system. From that point of view perhaps the situation could be left undisturbed, unless and until the activities of a few aggressive banks resulted in more widespread adoption of the device of carrying demand deposits under the guise of interest-bearing borrowed money. It must be recognized, however, that the existence of the practice described by Wachovia provided a means for defeating the statutory prohibition against payment of interest on demand deposits. In the opinion of the Legal Division, it was not feasible to plug that loophole otherwise than by a ruling by all three Federal bank supervisory

agencies (if they had authority so to rule) that demand loans or one-day loans to banks actually constitute demand deposits and therefore may not bear interest. Such a position, however, would result in largely destroying the existing Federal funds market, which consisted predominantly of one-day loans and demand loans. In the circumstances, the Legal Division reluctantly concluded that, unless the Board was prepared to take steps that would significantly alter the structure of the money market (for example, by defining "demand deposits" to include all demand or one-day transactions, even though denominated "loans"; the legal authority for such a definition had not been explored), it would be necessary either to decline to answer Wachovia's inquiry on the doubtful ground that it was hypothetical, or to inform the bank that the arrangement it had described did not violate Regulation Q. Both of these alternatives were admittedly unsatisfactory. However, the Board was faced with a conflict between the statutory prohibition against payment of interest on demand deposits and the actuality of a money market mechanism - Federal funds transactions - that the Board presumably did not wish to destroy.

For reasons stated in the memorandum, the Legal Division recommended against issuing a public ruling such as suggested by Wachovia. Attached for consideration was a draft of letter to the Federal Reserve Bank of Richmond that would state, after discussion, that "The prohibition of section 19 and Regulation Q relates only to the payment of interest on demand deposits. It does not prohibit the

payment of interest on 'money borrowed' by member banks, and the System has long recognized the legality and propriety of borrowing in certain circumstances, including the situations enumerated herein. Accordingly, the Board concludes that transactions of the kind described in the letter from the member bank would not involve a violation of section 19 or of Regulation Q. You are requested to inform Wachovia Bank and Trust Company to that effect."

The memorandum concluded with the suggestion that before acting on the matter it might be advisable to discuss it with the Federal Deposit Insurance Corporation and the Office of the Comptroller of the Currency, and perhaps with the Reserve Banks.

After summary comments by Mr. Hexter, Governor Mills expressed the view that the transactions under discussion were in effect bills payable transactions. However, they constituted a device for evading the prohibition against payment of interest on demand deposits. Since the Board had authority to prescribe the physical instruments denoting a time certificate of deposit, a time deposit open account, and a savings passbook, he suggested that the draft letter be expanded to bring out forcibly that the transactions in question involved borrowings and to specify that such transactions should be formalized by an exchange of instruments between the lender and the borrower. This would place some control over the practice. The danger implicit in the laxness of handling Federal funds transactions would be multiplied if the Board were to condone the "borrowed money" practice without

giving some indication as to how the transactions should be handled. If the funds were shown on a bank's books as bills payable, the practice might be discouraged, because banks traditionally disliked to show more borrowings on their books than necessary.

Governor Daane remarked that the practice was not new by any means. The processes fell within the complex area of Federal funds transactions, and dealings in Federal funds could take such a variety of forms that it would be extremely difficult to decide which of them required an exchange of instruments and which did not. To regiment such transactions would go against the whole fabric of the Federal funds market.

Governor Mills advocated that a start be made; in his view, it would be a good move.

Governor Robertson commented that from the standpoint of logic he believed that the memorandum was correct. As he saw it, there were two alternatives: either the Board must require written instruments of some kind or it must forsake the cause of the prohibition of payment of interest on demand deposits. He felt so uncertain as to where this practice might lead that he believed the Board should at least consider the feasibility of requiring written instruments.

Governor Daane stated that, like Governors Mills and Robertson, he decried the payment of interest on demand deposits. If the Board could avoid being drawn into a position of approving the "borrowed money" transactions, perhaps the practice could be kept within bounds.

Governor Mitchell took exception to the view that the "borrowed money" constituted a demand deposit. The depositor wanted the funds invested, and he (Governor Mitchell) could not follow the reasoning through which these transactions were regarded as a way around the prohibition of interest on demand deposits. He did not believe the practice could be stopped without taking the position that a bank could not borrow from its depositors, and he doubted whether that position could be taken without specific statutory authority. He would say that if a correspondent wanted to include with its services the management of the balance of the country bank when it reached a certain level, this was a permissible banking practice. Moreover, he did not see why the issue should be swept out of sight; if the Board was going to make a ruling, everyone should know about it.

Procedural matters were then discussed, as a result of which it was agreed that on this question of broad import the first step should be to solicit the views of the Federal Reserve Banks, consultations with the other two Federal bank supervisory agencies to be deferred. A copy of the letter in which the question was submitted to the Federal Reserve Banks is attached as Item No. 3.

Messrs. Hooff, Holland, and Keir then withdrew from the meeting.

S. 750 (Item No. 4). On February 13, 1964, the Board gave preliminary consideration to a request from Chairman Robertson of the Senate Committee on Banking and Currency for a report on 83 questions regarding

S. 750, a bill to assist in the promotion of economic stabilization by requiring the disclosure of finance charges in connection with extensions of credit. There had now been distributed a memorandum dated February 14, 1964, from the Legal Division submitting a draft of letter to Chairman Robertson, to which were attached draft replies to the questions.

After discussion the letter and the replies to the questions were approved unanimously, the replies being subject to certain editorial changes. A copy of the letter is attached as Item No. 4.

Messrs. Noyes, Cardon, Fauver, Hexter, Shay, Dembitz, Osborne, Smith, and McClintock then withdrew from the meeting.

Retirement System (Item No. 5). There had been distributed a memorandum dated February 3, 1964, in which the Division of Personnel Administration recommended (1) that the Board inform the Chairman of the Board of Trustees of the Retirement System of the Federal Reserve Banks and the Chairman of the Conference of Presidents that it would interpose no objection to the adoption of the mortality tables identified as the 1951 group annuity tables using a two-year setback for women, which tables were adopted by the Retirement Committee on February 27, 1962, with an effective date left open; (2) that the Board concur in the principle that annuities of present members of the Bank Plan should not be reduced as a result of the adoption of these more conservative mortality tables; and (3) that the Board approve the recommendation of the Conference of Presidents that the regular rate of

interest for the Retirement System of the Federal Reserve Banks be increased from 3 to 3-1/2 per cent for both the purpose of valuation of liabilities and for the pricing of annuities, subject to the approval of the Board of Trustees of the Retirement System of the Federal Reserve Banks.

The memorandum summarized the developments leading to these recommendations, including consultation with Dr. Dan M. McGill of the Wharton School of Finance and Commerce, University of Pennsylvania, and Mr. George B. Buck, Consulting Actuary for the Retirement System, most recently on September 25, 1963. Memoranda from Dr. McGill and Mr. Buck and several pertinent memoranda from the Division of Personnel Administration had been furnished to the members of the Board.

It was the belief of the Division, the memorandum continued, that the original recommendations of the Actuary concerning the mortality tables, which recommendations were subsequently adopted by the Retirement Committee, endorsed by the Investment Committee and the Board of Trustees, and adopted by the Conference of Presidents, were sound and should be placed in effect. That conclusion reflected, among other things, cost projections outlined in a table attached to the memorandum and in a memorandum of June 21, 1963, from the Division. Using the most conservative projections proposed, the assets of the Retirement System appeared to exceed its liabilities by approximately $9 million on a book value basis and some $49 million on a market value basis. It was believed, after taking into consideration both Mr. Buck's

and Dr. McGill's statements, that the Retirement System was in good financial condition and was clearly solvent.

While Dr. McGill would favor the GA-1951 mortality tables with a projection of 15 years, it seemed apparent that he would not object strongly to the tables proposed by Mr. Buck. Both men agreed that for at least the next eight years these mortality tables would be adequate, and it appeared that solvency could be insured if the termination-of-plan valuation suggested by Dr. McGill was made at 5-year intervals. It was noted that Mr. Deming, Chairman of the Board of Trustees of the Retirement System, had indicated in a letter of November 14, 1963, that the Retirement Committee, on October 23, 1963, proposed to recommend to the Board of Trustees that the Rules and Regulations of the Retirement System be amended to provide for an actuarial investigation into mortality, service, and compensation experience at least once in each 5-year period. Mr. Deming indicated also that the Retirement Committee reiterated its original position favoring the mortality tables proposed by Mr. Buck.

From a cost standpoint, Dr. McGill's recommendation would result in a greater increase in cost by some $575,000 over that recommended by Mr. Buck. If the GA-1951 tables with a 2-year setback were selected, as recommended, and the 3-1/2 per cent rate was thought to be sustainable, the net annual reduction in cost to the System from the present mortality tables using a 3 per cent rate would amount to about $2 million.

In regard to the rate of interest for the purpose of the valuation of liabilities and the pricing of annuities, the Division of Personnel Administration understood that the 3-1/2 per cent rate for the valuation of liabilities was thought to be a proper rate by both Mr. Buck and Dr. McGill; the only reservation was Dr. McGill's feeling that he would prefer a 3 per cent rate for the pricing of annuities. The Division believed this latter thought stemmed largely from a feeling that the System, at 3-1/2 per cent, would be closer, in effect, to guaranteeing a return at a level that might need to be reduced at some future time and that the 3 per cent rate would be a more conservative approach. In the opinion of the Division, the regular rate of interest for both the valuation of liabilities and the pricing of annuities should be the same, and the 3-1/2 per cent level would be supportable for many years to come. If it became necessary to reduce the rate, there was precedent for such action; in the 1940's the rate had been reduced from 4 to 3 per cent.

It was believed that the Board, if it adopted the mortality tables proposed by Mr. Buck, would be following a sufficiently conservative approach to keep the Retirement System in a solvent position, and the further built-in check through the 5-year termination-of-plan valuations would insure soundness and give adequate opportunity to change the mortality base if necessary.

At the Board's request, Mr. Sprecher commented on the memorandum, after which Governor Mills expressed the view that it would seem to be in order to accept the Division's recommendations, which appeared to be

consistent with the Board's review of Retirement System problems with Mr. Buck and Dr. McGill. However, he noted that the present proposals were only a prelude to others that would be forthcoming from the Conference of Presidents and the Trustees of the Retirement System. Because these coming proposals struck deep into fundamentals, he suggested that, in advance of their actual receipt, the Board give a great deal of thought to them on the basis of the information in the pertinent documents that were already available to the Board.

Governor Mills then commented further on the nature of the forthcoming proposals, some of which were based on the principle of comparability with private pension plans that were tending toward greater generosity in benefits accorded their members. Seeking to provide comparable benefits to members of the Federal Reserve Retirement System brought one into philosophical debate as to whether the Federal Reserve Banks were more nearly private or Governmental institutions and whether their financial activities and recruitment of personnel should be related more to the private or the Governmental area.

Some years ago, Governor Mills continued, it had been suggested that the Federal Reserve Banks consider what would be tantamount to a stock benefit or profit-sharing plan. Such an arrangement had been found impracticable, but in the proposals that were expected to be submitted there was a recurrent idea that more generous equity benefits would in a sense be a substitute for a profit-sharing plan. This would

ally the Federal Reserve Banks more closely with the practices of industry and commerce. An expanded benefit in the package of proposals related to the current provision that upon death in active service an employee's estate receives an amount equal to his current annual salary, but with a maximum of $25,000. It was to be proposed that there be no ceiling -- a substantial relaxation so far as the Presidents of the Federal Reserve Banks were concerned. Retirement System decisions were not a matter of today only, but reached far into the future, and questions of ethics were involved, such as whether it was proper for the beneficiaries of a pension fund to manage that fund or whether self-interest, even with the best of motives, was bound to be a factor.

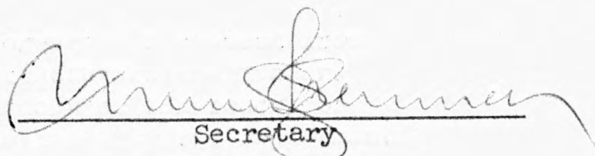
In the ensuing discussion various technical questions were considered, particularly whether adoption of the recommendations before the Board today would in any way prejudice consideration of the questions (to which Governor Mills had referred) that had not yet come before the Board. This question was resolved in the negative.

Comment was made by Chairman Martin that in the course of events the Board might find it desirable to arrange further meetings with Dr. McGill and Mr. Buck.

Governor Balderston suggested that the record show clearly that one of the principal concerns of the Board, namely, the financial soundness of the Retirement System as of this moment, had been satisfied through the work done by Dr. McGill and Mr. Buck.

At the conclusion of the discussion, the three recommendations contained in the memorandum from the Division of Personnel Administration were approved unanimously. A copy of the letter informing Mr. Irons, Chairman of the Conference of Presidents, of this decision is attached as Item No. 5. Copies of the letter were sent to Mr. Deming, Chairman of the Board of Trustees of the Retirement System, and to Mr. Harris, Chairman of the Retirement Committee.

The meeting then adjourned.



Secretary

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

Item No. 1
2/17/64

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

February 18, 1964.

Mr. Howard D. Crosse,
Vice President,
Federal Reserve Bank of New York,
New York, New York. 10045

Dear Mr. Crosse:

Under date of January 6 you forwarded a request from Charles W. Millard, Jr., President, Manufacturers and Traders Trust Company, Buffalo, New York, for a copy of the report on the competitive factors submitted to the Board by the Department of Justice in connection with that bank's application to merge with Bank of Jamestown, Jamestown, New York. As you know, the proposed merger was disapproved by the Superintendent of Banks of the State of New York, December 30, 1963.

This is to advise that the Board has granted the request of Manufacturers and Traders Trust Company. Accordingly, a copy of the report on competitive factors in question is enclosed. It will be appreciated if you would transmit such copy to Manufacturers and Traders Trust Company, which has not been advised of the Board's action concerning the matter.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.

Enclosure

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

Item No. 2
2/17/64

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

March 6, 1964.

Mr. Oscar R. Goodman,
Associate Professor of Finance,
Graduate School of Business Administration,
Northwestern University,
339 East Chicago Avenue,
Chicago 11, Illinois.

Dear Professor Goodman:

This is in further reference to our letter of December 31, 1963, concerning your earlier requests for copies of the reports on competitive factors received by the Board from the Department of Justice, the Federal Deposit Insurance Corporation, and the Comptroller of the Currency in connection with the application of The Lorain County Savings & Trust Company, Elyria, Ohio, to merge with The Central Bank Company, Lorain, Ohio, and the application of Fidelity-Philadelphia Trust Company, Philadelphia, Pennsylvania, to merge with Liberty Real Estate Bank and Trust Company, Philadelphia, Pennsylvania. Copies of the competitive factors reports requested by you are enclosed.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.

Enclosures

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

Item No. 3
2/17/64

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

February 17, 1964.

Dear Sir:

A member State bank has inquired whether it is permissible for a member bank to "borrow" at an agreed rate of interest, from correspondent banks and other depositors, by means of transfers from "Deposits" to "Bills payable", "Borrowed money", or other similar liability account.

The inquiry may have important implications with respect to sound banking practice, the statutory prohibition against payment of interest on demand deposits, the applicability of reserve requirements, and the Federal funds market. To assist in its further consideration of this matter, the Board would appreciate receiving the comments of your Bank, including its views as to the nature and magnitude of the problems presented, and your recommendations as to procedures for dealing with those problems.

As background for your study of the question presented, there are enclosed copies of a memorandum prepared by the Board's Legal Division, together with a draft of possible response.

Very truly yours,

Merritt Sherman,
Secretary.

Enclosures 2.

TO THE PRESIDENTS OF ALL FEDERAL RESERVE BANKS

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

Item No. 4
2/17/64

OFFICE OF THE CHAIRMAN

February 17, 1964

The Honorable A. Willis Robertson, Chairman,
Committee on Banking and Currency,
United States Senate,
Washington, D. C. 20510

Dear Mr. Chairman:

This refers to your letter of February 6, 1964, which enclosed a list of questions relating to S. 750, Senator Douglas' bill, "To assist in the promotion of economic stabilization by requiring the disclosure of finance charges in connection with extensions of credit."

Because of the rather technical and detailed nature of most of the 83 questions on the list, it was submitted to the Board's staff for study. In response to your letter, there is enclosed a memorandum which the staff has prepared commenting on the various questions. It is hoped that the memorandum will be useful in connection with further considerations of the bill.

In this connection, the Board would like to point out again that it is in full accord with the purpose of requiring creditors to disclose their finance charges. There is no doubt that the more information borrowers and credit purchasers have about the prices they are paying for credit, the more efficiently they can choose among the alternatives available to them. The Board expressed the same view in its report of February 20, 1963, to you on S. 750 and also in its reports on similar bills introduced in 1960 and 1961.

However, as these reports have stated, the Board believes that administration of such legislation would not constitute an appropriate activity for the Federal Reserve System. The regulation of trade disclosure practices would be foreign to the Board's present responsibilities. As noted in its report to you of February 20, 1963, the Presidential message of May 15, 1962, concerning consumer protection stated that: "Inasmuch as the specific credit practices which such a bill would be designed to correct are closely related to and often combined with other types of misleading trade practices which

the Federal Trade Commission is already regulating, I recommend that enforcement of the new authority be assigned to the Commission."

Accordingly, as stated in its earlier reports, the Board endorses the objective of requiring creditors to disclose their finance charges, but believes that it would be inappropriate for the Board to administer such a bill.

Sincerely yours,

(Signed) Wm. McC. Martin, Jr.

Wm. McC. Martin, Jr.

Enclosure

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

Item No. 5
2/17/64

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

February 17, 1964.

Mr. Watrous H. Irons,
Chairman, Conference of Presidents
of the Federal Reserve Banks,
c/o Federal Reserve Bank of Dallas,
Dallas, Texas. 75222

Dear Mr. Irons:

As you know, the Board of Governors has had under study and review certain aspects of the Retirement System of the Federal Reserve Banks relating particularly to mortality tables and interest rates. For this purpose, the Board retained the services of Dr. Dan M. McGill, and the Board has had joint sessions with both Dr. McGill and Mr. George B. Buck, the Consulting Actuary of the Retirement System.

As a result of these considerations, the Board has arrived at the following conclusions:

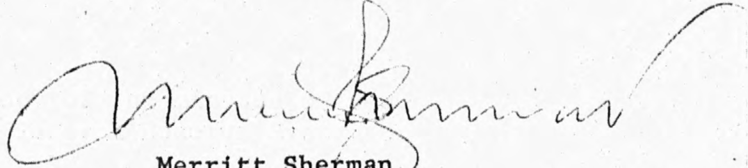
(1) That the Board will interpose no objection to the adoption of the mortality tables identified as the 1951 group annuity tables using a 2-year setback for women, which tables were adopted by the Retirement Committee on February 27, 1962.

(2) That the Board concurs in the principle as expressed by the Conference of Presidents at its meeting on May 28, 1962, that annuities of present members of the Bank Plan should not be reduced as a result of the adoption of these more conservative mortality tables.

(3) That the Board approves the recommendation of the Conference of Presidents that the regular rate of interest for the Retirement System of the Federal Reserve Banks be increased from 3 to 3-1/2 per cent for both the purpose of valuation of liabilities and for the pricing of annuities, subject to the approval of the Board of Trustees of the Retirement System of the Federal Reserve Banks.

Dr. McGill in his study recommended that a termination-of-plan valuation be made about every five years. The Board believes that such a provision should be incorporated in the Rules and Regulations of the Retirement System of the Federal Reserve Banks as a periodic check to insure the maintenance of the System in a sound financial condition.

Very truly yours,



Merritt Sherman,
Secretary.

cc: Mr. Frederick L. Deming,
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