Minutes for July 14, 1965

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	WM
Gov. Robertson	R
Gov. Balderston	CCB
Gov. Shepardson	CCS
Gov. Mitchell	GWM
Gov. Daane	JDD
Gov. Maisel	SJM

Minutes of the Board of Governors of the Federal Reserve System on Wednesday, July 14, 1965. The Board met in the Board Room at 9:30 a.m.

PRESENT: Mr. Martin, Chairman 1/
Mr. Balderston, Vice Chairman
Mr. Robertson
Mr. Shepardson
Mr. Mitchell
Mr. Daane
Mr. Maisel

Mr. Sherman, Secretary
Mr. Young, Adviser to the Board and Director, Division of International Finance
Mr. Molony, Assistant to the Board
Mr. Fauver, Assistant to the Board
Mr. Hackley, General Counsel
Mr. Farrell, Director, Division of Bank Operations
Mr. Solomon, Director, Division of Examinations
Mr. O'Connell, Assistant General Counsel
Mr. Shay, Assistant General Counsel
Mr. Hooff, Assistant General Counsel
Mr. Sammons, Adviser, Division of International Finance
Mr. Goodman, Assistant Director, Division of Examinations
Mr. Thompson, Assistant Director, Division of Examinations
Mr. Sprecher, Assistant Director, Division of Personnel Administration
Mrs. Semia, Technical Assistant, Office of the Secretary
Miss Hart and Mr. Via, Senior Attorneys, Legal Division
Messrs. Forrestal and Heyde, Attorneys, Legal Division
Mr. Smith, Senior Economist, Division of Research and Statistics
Mr. Lawrence, Economist, Division of Research and Statistics
Messrs. Egertson and McClintock, Supervisory Review Examiners, Division of Examinations
Mr. Hart, Assistant to the Director, Division of Personnel Administration

1/ Entered meeting at point indicated in minutes.

Discount rates. The establishment without change by the Federal Reserve Bank of Kansas City on July 12, 1965, of the rates on discounts and advances in its existing schedule was approved unanimously, with the understanding that appropriate advice would be sent to that Bank.

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

	Item No.
Letter to The Chase Manhattan Bank, New York, New York, granting permission to establish a branch in Georgetown, British Guiana.	1
Letter to Security Trust Company, Rochester, New York, approving the establishment of a branch at 103 Main Street East in connection with the removal of its head office from that address to One East Avenue.	2
Letter to Union County Trust Company, Elizabeth, New Jersey, approving the establishment of a branch in Cranford Township.	3
Letter to Upper Main Line Bank, Berwyn, Pennsylvania, approving the establishment of a branch in Tredyffrin Township.	4
Letter to Safe Deposit Bank and Trust Company, Springfield, Massachusetts, approving an extension of time to establish a branch in Westfield.	5
Letter to Indiana Lawrence Bank and Trust Company, North Manchester, Indiana, approving an investment in bank premises.	6
Letter to the Federal Reserve Bank of St. Louis waiving the assessment of a penalty incurred by Southwest Bank, St. Louis, Missouri, because of a deficiency in its required reserves.	7

	Item No.
Letter to Lyon County State Bank, Rock Rapids, Iowa, waiving the requirement of six months' notice of withdrawal from membership in the Federal Reserve System.	8

Application of The Bank of Virginia. At the meeting on July 12, 1965, the Board approved, Governor Robertson dissenting, the application of The Bank of Virginia, Richmond, Virginia, to merge with Farmers Bank of Boydton, Boydton, Virginia.

At today's meeting Governor Robertson stated that upon further review of the case in the light of the comments made during the Board's discussion, especially those indicating an expectation that the proposed merger would increase competition in the Boydton area, he wished to vote to approve the application.

Mr. Hackley said that, up till the date of the Board's order, there appeared to be no objection to such a change in the minority position that had been taken by a member of the Board under the Board's internal rules of procedure in holding company and merger cases; if, however, a member of the Board who had voted with the majority wished to change his position, his proper course would be to ask for reconsideration of the case.

Governor Robertson expressed the view that the Board's decision in a merger case should rest upon the positions of the members as of the date of release of the Board's order, and he felt that up to that time a member should be able to ask for reconsideration if he believed the decision had not been a good one.

There being no indication of objection, it was understood that the order reflecting the Board's decision regarding the application of The Bank of Virginia would show Governor Robertson as voting for approval.

Proposed legislation relating to foreign branches (Item No. 9). There had been distributed a memorandum dated July 8, 1965, from the Legal Division regarding requests from the Senate and House Committees on the Judiciary for reports on companion bills, S. 1907 and H. R. 6849. The proposed legislation would forbid any United States court, in an action to enforce the revenue laws, from restraining or enjoining a bank with respect to property or rights to property situated outside the United States or the performance of a contract to be performed outside the United States, except upon proof by the Government that compliance with the injunction or restraining order would not subject the bank to civil or criminal liability or penalty under the law of the country in which the property was situated or the contract was to be performed.

The legislative proposals were prompted by the decision of the United States Supreme Court in January 1965 in the case of United States v. First National City Bank (sometimes referred to as the "Omar" case). The case had been initiated by the Government's suit to enforce payment of taxes alleged to be due from Omar, S. A., a Uruguayan corporation. The Supreme Court reversed the United States Court of Appeals and upheld the issuance by the United States District Court of a preliminary injunction against First National City Bank of New York "freezing" the property of Omar wherever situated, including the deposit of Omar in the bank's Montevideo branch, pending a decision on the merits of the Government's tax claim. Omar had no property in the United States and, unlike the bank, was not present in this country and had not been personally served as a defendant in the Government's suit. In its opinion, the majority of the Supreme Court referred to a New York statute, enacted after issuance of the "freeze" order, under which they felt the Government could perfect substituted service on Omar, and noted that the District Court had indicated that the injunction would be modified upon proof by the bank that its compliance therewith would violate foreign law. Under the proposed legislation, an injunction such as the one upheld in the Omar case could not issue unless the Government sustained the heavy burden of proving that compliance by the bank would not subject it to civil or criminal liability or penalty under foreign law. Thus an effect of the proposed legislation, at least in many cases, would be to neutralize the Omar decision. Also, it would nullify the adverse effect that the Omar decision might have in discouraging foreigners to do business with overseas branches of United States banks.

Attached to the memorandum was a draft of letter to the two Judiciary Committees that would endorse the objective of the proposed legislation and would describe some of the adverse effects that could result to foreign operations of United States banks under the rule of law stemming from the Omar decision. The memorandum suggested that the Board's report on the proposed legislation also be transmitted as a reply to several banks that had urged the Board to support the bills.

Governor Mitchell, after Mr. Forrestal had summarized the considerations bearing upon the proposed legislation, questioned the extent to which the draft report favored private interests as against the public interest aspect of enabling the Government to collect revenue.

Governor Daane remarked that although he subscribed to the general position that the implications of the Omar case were inimical to the competitive position of foreign offices of U. S. banks, he did not believe that the proposed report gave sufficient recognition to the point made by Governor Mitchell, namely, the need to enable the Government to collect taxes. He would prefer that the report balance the two considerations.

Governor Robertson expressed the view that in a situation in which the Executive Branch of the Government had enlisted the aid of the courts in collecting taxes, in which the courts were in a position to weigh both the domestic and international aspects, and in which the State Department was in a position to furnish advice with respect to any diplomatic aspects, any legislation adopted should merely specify the extent to which private interests should be required to prove that they would be subjected to liability. It might be that in the Omar case both the Supreme Court and the District Court had given too great weight to statutory law to the detriment of considerations of civil liability, but it seemed to him that legislation should not throw the whole burden upon the Government to show that no civil or criminal liability would be incurred by a bank that complied with an injunction. Although he was not unconcerned with the implications of the Omar decision for the competitive situation of foreign branches of U. S. banks, he believed it to be the right and duty of any country to protect its revenue. Rather than report to the Committees in the terms of the draft letter, he would merely point out that there were considerations for and against the proposed legislation and give the Committees the benefit of available information with respect to the effect of the Omar decision on competition and with respect to applicable international law, but he would not go so far as strongly to urge enactment of the proposed legislation.

Governor Shepardson asked if the proposed legislation would effectively preclude the courts from taking action in the future such as they had in the Omar case. Staff responses explained that, instead of the bank having to provide the difficult proof that by complying with an injunction it would incur civil or criminal liability, the legislation in effect would shift the burden to the Government to prove that compliance would not subject a bank to civil or criminal liability. However, the legislative proposal was limited to the issuance of writs and preliminary injunctions; there was nothing to prevent the Government from collecting taxes from corporations against which it could obtain a judgment.

Governor Robertson commented that the answer to Governor Shepardson's question, in brief, was that it would be a virtual impossibility for the courts to issue an effective injunction.

Chairman Martin entered the room during the exchange of comments following Governor Shepardson's inquiry.

Governor Shepardson stated that in general he would support the approach of the draft letter, although he believed that the point of the Government's tax interest was well raised and that perhaps it should be given greater attention than was now reflected in the draft.

Governor Mitchell indicated that he leaned a little in the direction of the type of reply Governor Robertson had proposed, but he believed it would be preferable to avoid either endorsement of or objection to the bill. The letter might state that, speaking from the banking standpoint, the Board could say that it would be desirable to accomplish the results that the bill would achieve in terms of relieving foreign offices of banks from a competitive handicap, but that there were considerations from the standpoint of the national revenue as to which the Board was not competent to make a judgment.

Governor Daane remarked that, although his sympathies were with the desirability of relieving a banking handicap as expressed in the draft letter, he had been familiar with the developments in the Omar case from the beginning and believed that the draft did not give sufficient recognition to nonbanking aspects. In the circumstances, an approach such as Governor Mitchell had outlined might be the best course.

Other members of the Board having expressed agreement with the suggestions of Governors Mitchell and Daane, unanimous approval was given to a letter to Chairman Eastland of the Senate Committee on the Judiciary in the form attached as Item No. 9. A similar letter was sent to Chairman Celler of the House Committee on the Judiciary.

Mr. Noyes, Adviser to the Board, then entered the room and Mr. Forrestal withdrew.

Application of Marine Midland Trust Company. There had been distributed a memorandum from the Division of Examinations dated May 25, 1965, with other pertinent papers, relating to the application of The Marine Midland Trust Company of New York, New York, New York, to acquire the assets and assume the liabilities of Grace National Bank, also of New York City, under the charter of the Trust Company and the new name of "Marine Midland Grace Trust Company of New York." The Division recommended approval.

The summary of related facts in the memorandum of May 25 indicated, among other things, that Marine Midland Trust, an affiliate of Buffalo-based Marine Midland Corporation (a registered bank holding company), was

New York City's eighth largest commercial bank in terms of total deposits (about $950 million) and operated 13 offices. It would continue in eighth place if combined with Grace National, which ranked twelfth and had one office and total deposits of approximately $292 million. Stockholders of Grace National would receive preferred stock in Marine Midland Corporation with a book value of approximately $11.2 million in excess of the book value of Grace National, or the equivalent of about 4 per cent of Grace National's deposits and approximately 5-1/2 times its average annual net profits after taxes. Grace National, oriented in many ways toward its parent, W. R. Grace & Co. (a one-bank holding company), was a specialist in international banking. Over the years it had not solicited the "retail" trade; it discouraged small checking and savings accounts, offered no consumer loans, and had no real estate mortgage department. Marine Midland Trust, once considered an unaggressive "wholesale" bank, had recently expanded into all markets and its deposit and loan growth had been substantial in the past few years. Its parent, Marine Midland Corporation, the largest bank holding company in the State, had 11 banking subsidiaries with 201 offices and combined deposits of $3.1 billion. Of the 11 banks, only the Trust Company was located in New York City. If the proposed acquisition were effected, the deposit holdings of the 11 banks, which represented 5.4 per cent of total commercial banking deposits of New York State, would increase to 5.9 per cent.

The summary indicated also that the banking factors specified for consideration under the Bank Merger Act offered little of significance that would tend to support approval of the acquisition. The applicant contended that the acquisition would serve the convenience and needs of the various markets in which both banks presently operated, its principal arguments in support of that contention being (1) that the continuing bank would make available to Grace National's present customers an entire range of banking services through the convenience of 13 additional banking locations in New York City (as well as one in London) instead of just the present inconvenient single office offering only limited and specialized services; and (2) that the present customers of the Trust Company would have available (a) an increased lending limit (from \$6.8 million to \$9 million), (b) convenient uptown personal trust facilities, the establishment of which the Trust Company would be able to justify with the addition of Grace National's trust business, and (c) more efficient international banking services, which would result from the acquisition of the highly specialized staff at Grace National and access to the bank's many overseas contacts. After balancing these and other considerations relating to convenience and needs, the Division believed that, while a strong case could not be made for it, that factor weighed in favor of approval.

Analysis of competitive considerations led to the Division's conclusion that, although in absolute terms the two banks were "big" banks, competition between them in relation to the overall competitive situation in the unique financial center of New York City did not appear to be of significant proportions. The acquisition would, of course, eliminate one bank,but the significance of that was offset by several facts: there would remain ample alternatives to the public; there seemed little possibility of Grace National becoming an important retail bank; and the acquisition would increase competition among the city's largest banks.

There was no factor that weighed heavily in favor of or against approval. The increased competition among the large New York City banks that would result from the acquisition, the lack of any significant increase in concentration of banking resources, the existence of very limited competition between the consolidating banks, and the resultant ability of the Trust Company to provide services more comparable to those of the "big" banks were all factors that alone were of limited importance. However, when combined they more than offset any adverse effects of eliminating one of the city's relatively small wholesale banks operating but a single office.

Among other materials distributed was a memorandum dated June 10, 1965, from the Legal Division offering comments to assist the Board to weigh certain of the factors relevant to the application. On the basis of exploration of the validity of the applicant's two principal contentions in regard to the convenience and needs of the community, the Legal

Division was of the view that the first, namely, that the bank would make available to Grace National's present customers an entire range of banking services through the convenience of 13 additional offices, should be assigned virtually no weight in favor of approval. That belief was based, in essence, on the fact that any banking service that a customer conceivably could wish was readily available in New York City. The Division also believed that in the context of New York City, with its many full-service banking outlets, little, if any, weight should be given to the applicant's second contention, namely, that present customers of the Trust Company would have available an increased lending limit, convenient uptown personal trust facilities, and more efficient international service.

The memorandum next examined the effect of the proposed transaction in terms of competition and concentration, especially in the light of the March 1965 decision of the Federal District Court in New York upsetting the merger of Manufacturers Trust Company-Hanover Bank, in New York City, and the decision of the United States Supreme Court in the Philadelphia National Bank case in June 1963. It was noted that judgments might differ as to whether a result of the acquisition here proposed would be the elimination of significant competition between major competitors, or whether the acquisition would be, as it were, an important merger. That either of these points might be debatable, however, might well signal the necessity for stronger reasons than existed in this case under the needs and convenience factor to offset unfavorable considerations relating to competition -- existing and potential -- and concentration.

Finally, the memorandum referred to the fact that unfavorable competitive factor reports from the Comptroller of the Currency and the Department of Justice both emphasized that an effect of the proposed acquisition would be to strengthen the system of Marine Midland Corporation, which was the largest bank holding company in New York State. While the Trust Company was the holding company's only subsidiary in New York City, approval of the present application obviously would permit an expansion of the holding company's operations in New York City, which clearly would seem to be a fact to be considered in passing on applications of New York City banks to establish bank holding company systems with subsidiaries elsewhere in the State.

After Mr. McClintock had made summary comments based principally on the memorandum of May 25 from the Division of Examinations, Mr. Solomon remarked that the case had not been found easy, and that a probable first adverse impression because of the size of the holding company parent of Marine Midland Trust might be modified only after a study of the situation in depth disclosed that simple aggregate figures did not really tell the whole story. He noted that one aspect that some might consider adverse, but by no means so strongly adverse as in itself to justify denial, was that if the acquisition took place Marine Midland would have an undue advantage in pointing to what its up-State banks, through correspondent relations with the office that was now Grace National, could do for their customers with operations in Latin America. Against that should be balanced the fact that Grace National was not at present acting as correspondent for up-State banks to any noteworthy degree. Mr. Solomon also brought out that approval of the application by the Banking Department of the State of New York was more significant than was approval by the State banking authorities of proposals for mergers or holding company acquisitions in some other States, because Mr. Wille, New York State Superintendent of Banks, had demonstrated by his record that he was keenly alert to anticompetitive effects.

Chairman Martin then inquired whether there were questions regarding the presentation that had been made, and Governor Mitchell said that while he did not have questions as such, he had prepared a statement covering his analysis of this application that he would be glad to present if the other members of the Board wished.

Governor Maisel said that he would like to have the benefit of any analytical statements prior to record votes, and Governor Shepardson said that at his and Governor Mitchell's suggestion Mr. Smith of the Banking Markets Unit of the Division of Research and Statistics and Mr. McClintock of the Division of Examinations had visited New York to make a special study of the nature of Grace National's competition and of its foreign activities. He suggested that the Board hear comments on their findings at this point.

Mr. Smith then summarized the observations he and Mr. McClintock had made (which had been set forth in more detail in a distributed memorandum dated July 2, 1965). The application had indicated that about one-third of Grace National's demand deposits and loans and about 43 per cent of its savings and other time deposits were from the international market. It was not clear whether those figures were based solely on accounts with addresses outside the United States and accounts maintained for business primarily outside the United States, but if so confined the application probably understated the influence of Grace National's international activities through the omission of companies that were attracted to the bank because of its expertise in international financial transactions even though they used that service infrequently or for only a small part of their business. Upon a review of large deposit and loan accounts, it appeared that inclusion of such accounts in the figures would indicate international-oriented business of nearly 60 per cent of demand deposits of individuals, partnerships, and corporations, 85 per cent of time deposits, and 44 per cent of loans. Because of its large volume of international transactions, Grace National had always had a large amount of customers' liability on acceptances, which were essentially much the same as short-term commercial loans. If the $17.3 million of acceptances outstanding were added to commercial and industrial loans, the international portion rose to about one-half of the total. The high degree of liquidity of the bank, including its holdings of Government securities and brokers' loans, was a reflection of its lack of profitable loan outlets in the domestic market, a situation that might be expected to continue as long as the bank maintained its international orientation and did not expand into the domestic retail market.

At Chairman Martin's suggestion, Governor Mitchell then read his statement, which was substantially as follows:

> This is not an ordinary merger application. What makes it unique is the character of the Grace Bank--for many years an integral part of W. R. Grace & Co. The close affiliation with Grace Co. accounts for the nature of Grace Bank's assets, its specialized banking skills, its deposit profile, and probably in large degree its particular depositors. Over the years Grace Bank has not solicited "retail" trade, has discouraged small checking and savings accounts, offered no consumer loans and has no real estate mortgage department. It has one office in a somewhat out-of-the-way location--where it finds two tellers are ordinarily sufficient for its walk-in customer transactions. 1/

1/ The record contains various types of evidence that the Grace Bank is unlike other New York banking institutions but the most persuasive evidence of this fact to me is Grace Bank's deposit profile as revealed by the recent survey of deposits made by the F.D.I.C. It shows the Grace Bank with 7,682 I.P.C. demand deposit accounts and with 1,041 I.P.C. time deposit accounts. For a bank with $100,000,000 in demand deposits (I.P.C.) and $61,000,000 time deposits (I.P.C.) these numbers of accounts are only a fraction of what one would expect to find in the typical New York bank. And if one looks at accounts of less than $10,000 the number of such accounts at Grace is a small fraction of what might be expected. Put another way and more specifically--the New York banks that go in for retail banking, Chase, First National City, Manufacturers Hanover, etc., show an average size of demand deposit (I.P.C.) accounts under $10,000 to be between $700 and $900. Grace Bank's average sized account in this category is $2,300, even exceeding Morgan's $2,060, Empire's $2,070, and Bank of New York's $1,700. Grace Bank's business done with customers whose accounts are under $10,000 is a sport, probably arising from accommodations extended to W. R. Grace & Co.'s personnel and customers over a long period of time.

Grace Bank is a fragment of a corporate structure in which the banking business was generated as a by-product of other corporate operations. What Grace Bank developed, therefore, was primarily the technical capacity to deal with worldwide banking transactions for its parent. In its international banking activities, Grace has more than 500 correspondent relationships in 55 countries.

Grace Bank's emphasis on international banking transactions is greater than indicated by the allocations of IPC deposits and loans presented by the applicant. This allocation attributed to the international market only those accounts with addresses outside the United States and accounts maintained for business primarily outside the United States. Some companies, however, probably are attracted to Grace because they wish to have the expertise in international financial transactions available even though this service is used infrequently or for only a small part of their business. The inclusion of such accounts on the international side of Grace's business would increase the foreign share to well over one-half of the IPC deposits and about one-half of the loans outstanding.

Another characteristic of Grace Bank's operation is the high degree of liquidity that is maintained. Grace has attracted more deposits than it is prepared to employ in the international market (strange as it may seem) and since it has inadequate facilities for placing funds in the domestic retail credit market, it has a disproportionately large money market instrument portfolio. Grace Bank's cash and liquid asset holdings (Governments, Federal and tax-exempt, brokers' loans) amount to about 60 per cent of total assets as contrasted with ratios of 45 to 50 per cent for most large New York City banks.

The Bank's investment policy is reflected in a rate of net current operating income slightly below the average for banks of comparable size.

W. R. Grace & Co. wants to get out of the banking business because the nature of its operations have shifted in emphasis from transportation and trading to chemicals--and it does not find a banking affiliate of special usefulness.

The applicant is part of a large, aggressively managed holding company that has recently extended its operations in the international field. Acquisition of the Grace Bank would substantially accelerate its penetration of international markets by bringing to it experienced staff and established customer relationships. Thus the corporate interests of both institutions are happily served by the proposal.

The banking factors enumerated in the Merger Act are neutral in this case. The convenience and needs of the community seems only involved to the degree that the facilities of the Grace Bank might, under some other merger or a liquidation arrangement, cease to be independently available to American firms with international banking needs.

The competitive, and tendency toward monopoly, factors in this case cannot, in my judgment, adequately be appraised by looking to the size of the Marine Holding Company before and after its acquisition of Grace Bank. Overwhelmingly, in this merger proposal, the markets to be considered are those involving foreign banking relationships. Grace Bank does not compete, and is not equipped to compete, except for that specialized business. Marine would like to expand into this field. Since, in my judgment, Grace Bank cannot stand alone it must be dismembered or sold in toto to some larger institution with existing or potential international interests. Under these circumstances, it seems to me more clearly in the public interest to sell to a new entrant in this field than to an established one and for that reason I would approve the application.

Governor Maisel said that his analysis showed little or nothing to be said for the proposal on the basis of the banking factors and the convenience and needs of the community; therefore, it came down to a question of competition and where Grace could go in the future. If Grace National were going to be a competitor, it should either remain as an independent bank under different management or become part of another organization. It seemed clear that the bank as presently managed would never be a competitor in the domestic market. Given the assumption that the present ownership and management was going out, the question, then, was whether the present proposal represented the best affiliation. It seemed to him that the memorandum from the Legal Division and the stress in the reports from the Comptroller of the Currency and the Department of Justice missed the point that the Board should be more concerned with competition than with concentration. The concern with concentration was only as a measure of competition. The fact that the proposed transaction would allow the eighth largest bank in New York City to grow was the wrong stress, in his opinion; he believed that allowing the eighth largest bank to become a more active competitor might help competition generally. Thus, his analysis was that approval of this application was more likely to improve competition than was any other probable solution to the situation. Also, he disagreed with the idea that had been noted by Mr. Solomon that there might be an adverse element in enabling Marine Midland to offer through its up-State banks correspondent services of an international field specialist; Governor Maisel could not see an adverse element in allowing an institution to become a better competitor through offering improved services.

Mr. Solomon responded that he could not disagree with Governor Maisel on this point. He had merely noted that, if by this merger other up-State competitors found it more difficult to get access to the specialized international services, that could go beyond improving the services offered by this group and could be a disadvantage to banks outside the group that did not have access to similar facilities.

Governor Maisel commented that that would be true only if Grace National were the only institution expert in handling Latin American business, and this was not the case.

Governor Balderston then read a statement substantially as follows:

Since the so-called banking factors--financial history and condition, capital adequacy, earnings prospects, and management--do not argue significantly for or against the present application, the Board's task, as I can see it, is to strike a balance between the convenience and needs factor and the competitive factor. To strike such a balance involves what is tantamount to the assignment of weights to the convenience and needs factor and to the competitive factor. Since this is a merger by a bank holding company subsidiary, I will, in my analysis, use a test for competitive effect like that set forth in the Bank Holding Company Act: Would the merger expand the size or extent of the bank or the holding company system beyond limits consistent with adequate and sound banking, the public interest, and the preservation of competition?

To appraise the impact of this proposal upon the convenience and needs of the area concerned, the problem can be approached best by a series of questions: Would the deposit and borrowing needs of individual households and firms be affected adversely, if at all? My answer is that although Grace specializes in international banking and places little emphasis upon householders and small depositors, the effect upon the few that it does have would be helpful. Would firms such as U. S. Rubber, Anaconda, G. E., Westinghouse, and Chilean Nitrate receive better service if Grace were linked with Marine Midland? Those companies such as Coca Cola, Sears Roebuck, and I.T. & T. that use Grace almost entirely for domestic banking, but keep it available as an alternate in the international field, would probably be better off.

In my view, the proper approach to an analysis of convenience and needs and also of competition is that of Professor Alhadeff: to break the market down by lines of product. As a specialist in international banking, Grace's technical competence and know-how would be married to a well-run bank that would, at least, computerize the Grace operations, which are now conducted by obsolete methods. Marine Midland Trust, however, having already diversified by adding "retail" to its original "wholesale" banking, is of the usual type.

Would the proposed merger expand the Marine Midland Trust Company and its holding company beyond the limits of sound banking, the public interest, and the preservation of competition? The Marine Midland Trust Company is now eighth in size among the New York commercial banks and would remain eighth in rank if the merger were approved. It would still be less than half the size of the Irving Trust Company. It could scarcely be argued that the merger would endanger any of the seven banks that are larger in size even though the continuing bank would be a more potent contender in the international field. Nor can one conclude that Meadow Brook National, Bank of New York, and Commercial Bank of North America, the next three in rank below the continuing bank, would be injured severely.

This brings me to the question, what did Congress mean by the "public interest"? Those Congressmen who thought of a commercial bank as one located in a small town in a farming community would doubtless have in mind householders, storekeepers, and farmers in considerable number as distinct from large corporate depositors or from the banker and the other owners of the institution. But in the case before us, are large companies like G. E., whose success in foreign dealings is helpful to their country, to be taken into account when defining the public interest? My answer is in the affirmative.

A more difficult question is whether the interests of the stockholders of a bank are encompassed within the "public interest." Since both entry into and exit from the banking industry are supervised in this country, I would conclude that the rights of shareholders may be taken into account if no other portions of the public are damaged. For example, the chartering of a de novo bank may be approved if it seems likely not to fail itself, or to induce the failure of existing banks by creating an over-banked condition in the community. The odds often seem to favor approval on the ground that substantial citizens are willing to venture their own funds. What then should the supervisory agency say to these stockholders if, at a later time, they wish to sell out? In short, what should be said to the Grace Company owners, who after forty years in banking, find chemical operations more lucrative?

My answer is that if customers do not suffer an appreciable lessening of banking choices and if the acquiring bank of the holding company does not threaten to dominate other banks, approval may be granted.

Since the Grace owners wish to sell, and the Marine Midland Trust Company's increase in size and scope of activity would add to its competitiveness with larger banks without significant damage to smaller ones, I would approve the merger. In doing so, I am not overlooking the fact that the Marine Midland Trust Company belongs to the second largest holding company in the United States and the only large one now operating in New York State. But the proposal before us does not mean that the holding company is entering New York City for the first time. It already owns a bank there with thirteen banking offices (2 per cent of the total) and total deposits of nearly $950 million. The strengthening of Marine Midland in New York City proper could scarcely injure its upstate customers but might benefit those that carry on business in South America. The acquisition of Grace would make the upstate banks of the holding company more potent competitors to the other banks in their respective localities. Despite this adverse consideration, I still favor the acquisition of Grace National Bank of New York by Marine Midland Trust Company of New York.

Governor Robertson expressed the view that there seemed to be no question that the proposed acquisition would be desirable from the standpoint of the banks themselves and of their shareholders, but the Board's job was to determine the merits of the proposal on the basis of the public interest. There was no weight pro or con so far as the banking factors were concerned, but from the point of view of competition, no one could deny that one alternative source was being eliminated. A number of account holders maintained their connection with Grace National as an alternative source of credit in case of need. The mere fact that Grace National was engaged to a large extent in international banking was not sufficient in itself to justify the acquisition, in his view, because Marine Midland Trust was also in international business, and to that extent the two banks were in competition with each other. The facilitation of Marine Midland's international business that would result from the transaction had no bearing except to indicate that competition would be eliminated. The proposal involved big institutions -- not little ones; moreover, Marine Midland Trust was part of the largest bank holding company system in New York State, which was already in a position to compete effectively with any institution -- more effectively than others with institutions outside New York City. It seemed to him that this was a clear case of a large institution desiring to acquire another institution of good size, which was squarely in conflict with recent court decisions. He believed that the Department of Justice had given persuasive support for its position that the acquisition would be substantially in conflict with the public interest; also, the Comptroller of the Currency had done a good job in citing adverse considerations and had even pointed to the basis on which approval would conflict with previous decisions by the Board. Governor Robertson would disapprove.

Governor Shepardson stated that he had found it difficult to weigh the elements of this situation, especially since it involved the largest bank holding company in New York State. He had given careful study to the supplemental study of the nature of Grace National's business and the analysis of the findings of that study set forth in Governor Mitchell's statement. On balance, it seemed to Governor Shepardson that the diminution in the number of competitive institutions would be more than offset by the probable strengthening of competition with other large banks; the number of available alternatives was so great that there would be little disadvantage to anyone in reducing by one the number of independent units. He agreed with Governor Balderston that the public interest embraced all classes of bank customers, even large corporations such as were here involved. While the proposed acquisition would not add significantly to the facilities or convenience of anybody in New York, neither would it detract from their convenience, since they would not be circumscribed in their selection from the other multiple sources of service. The interests of the participant banks, including both their customers and their stockholders, would be served by this proposal. Therefore, while he found it somewhat difficult to allow absorption of a bank of nearly $300 million, in the present situation he thought it was justified and would approve the application.

The members of the Board were then asked for their formal votes, in response to which Governor Robertson voted for denial and all of the other members voted for approval of the application.

The application of The Marine Midland Trust Company of New York was thereupon approved, Governor Robertson dissenting. It was understood that an order and statement reflecting this decision would be drafted for the Board's consideration, and that a dissenting statement by Governor Robertson also would be prepared.

Messrs. Young, O'Connell, Goodman, Thompson, Sammons, Via, Smith, Lawrence, Egertson, and McClintock then withdrew from the meeting and Mr. Morgan, Staff Assistant, Board Members' Offices, entered the room.

Commingled Investment Account. There had been distributed a memorandum dated July 1, 1965, in which the Legal Division discussed a request for the Board's opinion as to whether section 32 of the Banking Act of 1933 would forbid interlocking service between First National City Bank, New York City, and a "Commingled Investment Account" that the bank proposed to establish. A related question was whether such a proposal might also involve violations of sections 20 and 21 of the Banking Act of 1933. The Board's position as to the primary and related questions took on added importance because of the possibility that, if the bank proceeded with its plan, other large State member banks might want to do likewise.

The memorandum explained that, in banking terms, the fund to be established could be described as a commingled account, to be operated under the effective control of the bank, for the collective investment of sums of money that might otherwise be handled individually by the bank as managing agent. Immediate control of the fund would be under a committee composed mostly of officers of the bank's trust department, although technically, members would be selected periodically by holders of participating interests in the fund. Counsel for the bank emphasized that the money invested in the fund would not be received "in trust" and that the fund would not be a "common trust fund" in the usual sense. However, the Comptroller of the Currency on May 10, 1965, had ruled that the fund would be an eligible operation for a national bank under his Regulation 9, "Fiduciary Powers of National Banks and Collective Investment Funds." The Securities and Exchange Commission had ruled that the fund would be a "regulated investment company" within the meaning of the Investment Company Act of 1940.

Section 32 and sections 20 and 21 were parts of the comprehensive legislation of the 1930's designed to divorce commercial banking and investment banking. Section 32, therefore, must be read in conjunction with sections 20 and 21 of the same Act. Briefly, section 21 forbade a securities firm or organization to engage in the business of receiving deposits (thus, in effect, forbidding <u>any</u> commercial bank, except in limited circumstances, to engage in the business of underwriting or issuing securities). Section 20 forbade any <u>member</u> bank to be affiliated with a securities firm or organization. Section 32 prohibited interlocking personal relationships between <u>member</u> banks and securities companies, and thus forbade connections that would tend to create indirectly, by means of personal contact, the forbidden link between commercial and investment banking.

Two basic legal questions were involved, the memorandum continued: (1) would participating interests in the fund be "securities" within the meaning of sections 32, 20, and 21, and (2) would the fund be a legal entity distinct from the bank for purposes of these sections? If the answer to the first question were negative, obviously no problem would arise under the Act. For the prohibitions of the three sections to apply there must be a person or organization that issued, distributed, etc., "securities." Counsel for the bank argued that participations in the fund would not be securities. However, the Legal Division believed that to adopt this position would be inconsistent with numerous published interpretations of the Board to the effect that shares of ordinary mutual funds were securities. Participations in the fund would be virtually indistinguishable from shares of some no-load, open-end mutual funds. It was recommended, therefore, as the better view, that such participations be regarded by the Board as "securities."

If the answer to the first question was that the participations would be securities, then the Board was faced with a difficult choice under the second question. If the fund was a separate entity, then interlocking service between the fund and the bank was forbidden by section 32, and there was a question whether a prohibited affiliation under section 20 would exist. If the fund was not a separate entity from the bank, then the bank might be "issuing securities" in violation of section 21, a criminal statute.

The Legal Division believed that, since the fund would be operated virtually as an integral part of the bank, section 32 would not forbid officers of the bank's trust department to serve as members of the committee of the fund. This position would dispose also of the section 20 question. As long as the fund was operated for the convenience of the bank's customers, without being advertised or pushed as an investment medium for its own sake, the Legal Division believed there would be no serious question of a violation of section 21 through the bank being "engaged in the business" of issuing securities. This conclusion was reinforced by the fact that a State member bank, Bank of Delaware, Wilmington, Delaware, had for many years operated a regulated investment company in its trust department. A different conclusion might be indicated if the fund here proposed were to be promoted more actively.

A detailed discussion of the mechanics of the plan and of its various legal aspects was set out in the memorandum, and attached was a draft of letter to the Federal Reserve Bank of New York reflecting the Legal Division's conclusions.

After summary comments by Miss Hart, Governor Robertson observed that the proposed fund would enter into contracts with First National City Bank, and that participants in the fund would have legal rights against the fund. He asked, in the light of those facts, if the Legal Division's conclusion that the fund and the bank were not separate entities was based on the language of the statute or on other grounds. The Legal staff responded that the committee being set up to manage the fund was tantamount to a division within the bank's trust department. It was a group under the control of the trust officers of the bank, and if one were required to identify the committee as an entity, it would be difficult to do so against the background of situations that the Board had held to involve only one corporate organization even though they included more definite characteristics of separation than were here presented. There followed an extended discussion of the point raised by Governor Robertson and the tenability of the position recommended by the Legal Division.

Governor Maisel commented that the reasoning that the participations in the proposed fund must be regarded as "securities" but that the fund and the bank were not separate entities seemed to say that the bank could underwrite securities, despite statutory prohibitions of that activity, as long as it did so in its own name, and he asked what would be the limit to the bank's underwriting activity under this theory. In the ensuing discussion the staff emphasized that the question raised by Governor Maisel was a close one, on which judgments could go either way, and it was uncertain how a court might determine the question if it were tested in litigation. A complicating fact was that the Comptroller of the Currency had approved the proposed plan, although he must be presumed to be fully aware of the possible bearing upon it of sections 20 and 21 of the Banking Act of 1933.

Governor Robertson commented that regardless of the implications of interagency relations the Board had the responsibility of administering the law regarding interlocking service between member banks and securities organizations. He could accept the reasoning that for purposes of section 20 the bank and its proposed fund were a single entity, but it appeared to him that the only circumstance that might determine that the plan would not violate section 21 was that the bank would not advertise the availability of the fund.

Governor Daane expressed the view that, since the absence of advertising apparently rested only on assurances by the bank, the plan amounted to the operation of a mutual fund and thereby contravened the intent of section 21. The question was close only in the sense of degree and not in the sense of principle, and if the Board expressed no objection the door would be opened to other similar plans.

Further discussion brought out that there were no available interpretations of section 21 by the Department of Justice, and that the Board's position in regard to situations involving the section had been not to interpret the law but to bring questionable circumstances to the attention of the Department. It was again observed that there was only a thin line between plans that had been permitted for many years, such as that operated by the Bank of Delaware, and the one proposed by First National City Bank. There was also discussion of the diminishing distinctions between common trust funds and mutual investment funds, and of the attitude taken by the Securities and Exchange Commission in regard to mutual investment funds.

The discussion developed tentative acceptance by the members of the Board of an approach that would find that the plan did not involve relationships such as were prohibited by section 32, would regard First National City Bank and its proposed fund as a single entity, but would point out the possibility that the plan might involve a violation of section 21. It was understood that a draft of letter along those lines would be submitted for the Board's consideration.

Messrs. Shay, Hooff, and Heyde, and Miss Hart then withdrew from the meeting.

Evaluation of Directors Day. There had been distributed a memorandum from Mr. Morgan dated June 25, 1965, commenting on reactions to the organization and conduct of the program presented on March 24-25, 1965, for newly-appointed directors of the Federal Reserve Banks and branches, and making certain suggestions for future similar meetings in the light of experience with this year's program.

After a brief discussion it was understood that any member of the Board who wished to offer additional comments or suggestions would convey them to Mr. Morgan.

Salary guidelines for Reserve Bank officers (Item No. 10). There had been distributed a memorandum dated July 6, 1965, from the Board's Committee on Organization, Compensation, and Building Plans, regarding salary guidelines for Reserve Bank officers. Current guidelines for officers other than Presidents and First Vice Presidents called for an annual review of officers' salaries, careful selectivity, and limitation of increases, based strictly on merit, to not more than 40 per cent of the officer staff at each Reserve Bank, exclusive of those officers granted promotional increases and increases to officers whose salaries were below the minimum of certain designated grades.

The memorandum commented on experience during the several years such guidelines had been in effect, and stated the recommendation of the Committee that the guidelines be reestablished for the year 1966 with no exclusions other than promotions and increases from below minimum of the lowest range. Attached to the memorandum was a draft of letter to the Chairmen and Presidents of all Federal Reserve Banks reflecting the Committee's recommendation.

After discussion the letter was approved unanimously. A copy is attached as Item No. 10.

The meeting then adjourned.

Secretary's Notes: On July 13, 1965, Governor Shepardson approved on behalf of the Board the following items:

Memorandum from the Division of Data Processing dated July 2, 1965, recommending that Helen K. Black be appointed on a temporary contractual basis effective to December 31, 1965, with compensation at the rate of $19 per day for each day worked, to assist in the work of the Financial Statistics Section of that Division.

Memorandum from the Division of Data Processing dated July 12, 1965, recommending that Dr. Martin Greenberger, Associate Professor at the Sloan School of Management, Massachusetts Institute of Technology, be appointed as Consultant to that Division effective to December 31, 1965, on a temporary contractual basis with compensation at the rate of $75 per day for each day worked and with transportation expenses and per diem when in travel status to be paid in accordance with the Board's travel regulations. This action included approval of the resulting over-expenditure in the pertinent account of the 1965 budget of the Division.

Memorandum from the Division of Data Processing dated July 9, 1965, requesting authorization for dual occupancy of a draftsman position in the Economic Graphics Section of that Division for a temporary period.

Governor Shepardson today approved on behalf of the Board memoranda recommending the following actions relating to the Board's staff:

Appointments

Mary Ellen Stroupe as Research Assistant, Division of Research and Statistics, with basic annual salary at the rate of $6,050, effective the date of entrance upon duty.

Frederick C. McGrady as Budget and Planning Assistant, Office of the Controller, with basic annual salary at the rate of $5,690, effective July 19, 1965.

Kalmann Schaefer as Statistician, Division of Data Processing, with basic annual salary at the rate of $6,450, effective the date of entrance upon duty.

Salary increases, effective July 18, 1965

Name and title	Division	Basic annual salary From	To
	Research and Statistics		
Linda S. Blumberg, Editorial Clerk		$ 5,000	$ 5,165
Suzanne D. Courtright, Statistical Assistant		5,330	5,495
Erling T. Thoresen, Economist		10,250	10,605

Salary increases, effective July 18, 1965 (continued)

Name and title	Division	Basic annual salary From	To
	Examinations		
Jerry B. Riley, Senior Federal Reserve Examiner		$12,495	$12,915
Louis William Zidek, Senior Federal Reserve Examiner		12,495	12,915
	Administrative Services		
Wilbert J. Hart, Supply Clerk		3,680	3,805
Mildred C. Harris, Charwoman		3,385	3,500
Betty Howard, Charwoman		3,385	3,500

Acceptance of resignation

Frances L. Hornbeck, Substitute Charwoman, Division of Administrative Services, effective at the close of business July 12, 1965.

Merritt Sherman

Secretary

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

Item No. 1
7/14/65

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

July 14, 1965.

The Chase Manhattan Bank,
1 Chase Manhattan Plaza,
New York, New York. 10005

Gentlemen:

The Board of Governors of the Federal Reserve System grants its permission to The Chase Manhattan Bank, pursuant to the provisions of Sections 9 and 25 of the Federal Reserve Act, to establish a branch in Georgetown, British Guiana, to be located at 47 Water Street, Georgetown, and to operate and maintain such branch subject to the provisions of such Sections.

Unless the branch is actually established and opened for business on or before July 1, 1966, all rights granted hereby shall be deemed to have been abandoned and the authority hereby granted will automatically terminate on that date.

It is noted that estimated expenditure for furniture, fixtures and equipment will not exceed $135,000 (of which approximately $54,000 will be expended in the United States), plus an allowance for contingencies of $25,000. With respect to foreign branches, funds provided by home office (whether in the form of allocated capital, advances, or otherwise) should be regarded as foreign assets for purposes of the voluntary foreign credit restraint effort.

Please inform the Board of Governors, through the Federal Reserve Bank of New York, when the branch is opened for business. The Board should also be promptly informed of any future change in location of the branch within the City of Georgetown.

Very truly yours,

(Signed) Karl E. Bakke

Karl E. Bakke,
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, D. C. 20551

Item No. 2
7/14/65

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

July 14, 1965

Board of Directors,
Security Trust Company,
Rochester, New York.

Gentlemen:

The Board of Governors of the Federal Reserve System approves the establishment of an in-town branch by Security Trust Company at 103 Main Street East, in connection with the removal of its head office from that address to One East Avenue, Rochester, New York.

Very truly yours,

(Signed) Karl E. Bakke

Karl E. Bakke,
Assistant Secretary.

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

Item No. 3
7/14/65

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

July 14, 1965

Board of Directors,
Union County Trust Company,
Elizabeth, New Jersey.

Gentlemen:

The Board of Governors of the Federal Reserve System approves the establishment by Union County Trust Company, Elizabeth, New Jersey, of a branch at the southeast corner of Walnut Avenue and Chestnut Street, Cranford Township, Union County, New Jersey, provided the branch is established within one year from the date of this letter.

Very truly yours,

(Signed) Karl E. Bakke

Karl E. Bakke,
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, D. C. 20551

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

Item No. 4
7/14/65

July 14, 1965

Board of Directors,
Upper Main Line Bank,
Berwyn, Pennsylvania.

Gentlemen:

The Board of Governors of the Federal Reserve System approves the establishment by Upper Main Line Bank, Berwyn, Pennsylvania, of a branch at the northeast corner of the intersection of Routes 202 and 363 in Tredyffrin Township, Chester County, Pennsylvania, provided the branch is established within one year from the date of this letter.

Very truly yours,

(Signed) Karl E. Bakke

Karl E. Bakke,
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, D. C. 20551

Item No. 5
7/14/65

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

July 14, 1965

Board of Directors,
Safe Deposit Bank and Trust Company,
Springfield, Massachusetts.

Gentlemen:

The Board of Governors of the Federal Reserve System extends to January 21, 1966, the time within which Safe Deposit Bank and Trust Company, Springfield, Massachusetts, may establish a branch in the 300 block of East Main Street, Westfield, Massachusetts.

Very truly yours,

(Signed) Karl E. Bakke

Karl E. Bakke,
Assistant Secretary.

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

Item No. 6
7/14/65

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

July 14, 1965

Board of Directors,
Indiana Lawrence Bank and
Trust Company,
North Manchester, Indiana.

Gentlemen:

The Board of Governors of the Federal Reserve System approves, under the provisions of Section 24A of the Federal Reserve Act, an additional investment in bank premises of $8,500 by Indiana Lawrence Bank and Trust Company, North Manchester, Indiana, for the purpose of establishing additional parking facilities.

Very truly yours,

(Signed) Karl E. Bakke

Karl E. Bakke,
Assistant Secretary.

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

Item No. 7
7/14/65

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

July 14, 1965

Mr. Joseph C. Wotawa,
Vice President,
Federal Reserve Bank of St. Louis,
P.O. Box 442,
St. Louis, Missouri. 63166

Dear Mr. Wotawa:

This refers to your letter of June 25, 1965, regarding the penalty of $351.58 incurred by the Southwest Bank, St. Louis, Missouri, on a deficiency in its required reserves for the biweekly computation period ended June 23, 1965.

It is noted that (1) the deficiency resulted from an incorrect treatment of purchased certificates of deposit in the computation and reporting of net demand deposits, which caused an understatement of the latter; (2) the error was called to your Bank's attention by the member bank; and (3) the Southwest Bank previously has had an excellent record in maintaining its required reserves over the past 13 years.

In the circumstances, the Board authorizes your Bank to waive the assessment of the penalty of $351.58 for the period ended June 23, 1965.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.

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

Item No. 8
7/14/65

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

July 14, 1965

Board of Directors,
Lyon County State Bank,
Rock Rapids, Iowa.

Gentlemen:

The Federal Reserve Bank of Chicago has forwarded to the Board of Governors President Leahy's letter dated June 24, 1965, together with the accompanying resolutions dated June 15, 1965, signifying your intention to withdraw from membership in the Federal Reserve System and requesting waiver of the six months' notice of such withdrawal.

The Board of Governors waives the requirement of six months' notice of withdrawal. Under the provisions of Section 208.10(c) of the Board's Regulation H, your institution may accomplish termination of its membership at any time within eight months from the date that notice of intention to withdraw from membership was given. Upon surrender to the Federal Reserve Bank of Chicago of the Federal Reserve stock issued to your institution, such stock will be canceled and appropriate refund will be made thereon.

It is requested that the certificate of membership be returned to the Federal Reserve Bank of Chicago.

Very truly yours,

(Signed) Karl E. Bakke

Karl E. Bakke,
Assistant Secretary.

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BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

Item No. 9
7/14/65

OFFICE OF THE CHAIRMAN

July 16, 1965

The Honorable James O. Eastland, Chairman,
Committee on the Judiciary,
United States Senate,
Washington, D. C. 20510

Dear Mr. Chairman:

This is in reply to your letter of June 3, 1965, requesting the views of the Board of Governors on a bill, S. 1907, "To amend chapter 161 of title 28 of the United States Code by adding a new section with respect to certain restraining writs or orders issued by United States district courts that affect property situated outside the United States."

The overseas operations of member banks of the Federal Reserve System are of direct concern to the Board by virtue of the authority vested in it by section 9, paragraph 3, and sections 25 and 25(a) of the Federal Reserve Act. Member banks may establish foreign branches only with the consent of the Board, and the operation of foreign branches of member banks is subject to the Board's Regulation M.

The proposed legislation was introduced as a result of the decision of the United States Supreme Court in the case of United States v. First National City Bank, 379 U. S. 378 (1965), the so-called Omar case. As you know, in that case the Supreme Court held that a United States district court has the power, in an action to enforce the revenue laws, to enjoin or restrain a United States bank from transferring or disposing of any property or rights to property, whether or not located in the United States, held for the account of an alleged delinquent taxpayer. Specifically, it affirmed the issuance by the United States District Court for the Southern District of New York of a preliminary injunction issued against First National City Bank ("Bank") ordering it to "freeze" the deposits of Omar, S. A., a Uruguayan corporation, held by the Bank in its Montevideo branch pending a decision of the Government's claim against the corporation for alleged unpaid taxes.

It is the Board's view that a rule of law permitting United States courts to "freeze" deposits in the foreign branches of American banks could cause serious harm to United States banks operating abroad. Some of the adverse effects which could result from the application of the principle established by this case are as follows:

(1) There is the possibility that as a result of this decision a United States bank would be subjected to multiple liability if it honors the injunction of a United States court and is sued by the depositor for breach of the deposit contract in the country in which the account is located.

Under well-recognized principles of private international law, a contract of deposit is governed by the law of the country in which the branch operates, and the fact that a United States court has purported to restrain performance of a bank's contractual obligation would, in most instances, be no valid defense in an action for damages brought by a depositor in the courts of the host country. It is a further rule of international law, accepted and enforced in the United States, that the courts of one country will not enforce or give effect to the tax claims of another. Thus, such a decree by a United States court would not be entitled either to comity among nations or to full faith and credit. As a matter of actual practice, almost no foreign country where American banks do business would allow the injunction of an American court to keep a local depositor from drawing on his account.

In addition to the civil damages for which a bank might be liable in a situation of this kind, criminal penalties could be imposed by a government on a bank which refuses to honor its deposit obligations, including revocation of the bank's license to do business in that particular country. To the extent that criminal or civil liability would attach as a result of the extraterritorial reach of a restraining order, it is, of course, the bank and not the delinquent taxpayer which would be penalized.

In the Omar case, the disadvantage of multiple liability was somewhat lessened by the district court's offer to modify the freeze order if the Bank shows that the order conflicts with Uruguayan law. This provision, however, would not remove the danger of civil liability as it would seem to be applicable only to violation of a statute. Moreover, it places the heavy burden on the Bank of discovering foreign law which may well be unclear until the matter is litigated in a foreign court. In any event, there is no guarantee that in future cases the order of a district court will contain such an offer to modify the decree upon a showing that liability will attach under foreign law. The proposed legislation would essentially have the desirable effect of shifting to the party seeking the injunction the burden of establishing that no liability would exist under the laws of the foreign country in which the bank operates.

(2) Foreign branches of American banks would be handicapped to the extent that they would not be competing abroad on an equal basis with indigenous and foreign banks.

(3) The decision could prompt the withdrawal of local and foreign currency deposits from American banks abroad by those who suspect they might be subject to an American court order, thus impeding the ability of American banks to finance foreign commerce with the resultant adverse effects on the United States balance of payments.

(4) The position of American banks in countries which already resent the intrusion of American corporations into their financial communities could be made even more difficult by the suggestion embodied in the Omar decision that ex parte orders of United States courts are to override the obligations of the guest bank in the foreign country.

(5) A logical extension of the holding in the Omar case would seem to be that foreign courts would, in turn, be able to issue injunctions against American branch banks which would affect accounts or activities of the head office in the United States. As the court of appeals said in the Omar case "The untoward difficulties and potential conflict between the laws of different nations that such a doctrine would produce militate against giving it support here", 321 F. 2d 14, 24.

Against these potential disadvantages to the foreign banking system of the United States, there is, of course, the public interest to be considered in the efforts of the Government to enforce the revenue laws and to collect unpaid taxes from delinquent taxpayers, be they citizens of the United States or nonresident aliens. The Board is not in a position to determine to what extent the proposed legislation would militate against the proper discharge of the responsibilities of the Internal Revenue Service under the tax statutes.

The Board does feel, however, that the proposed legislation would effectively negate the potential harm to our overseas banking system implicit in the Omar decision; and from this standpoint, the Board favors the objective of S. 1907.

Sincerely yours,

(Signed) Wm. McC. Martin, Jr.

Wm. McC. Martin, Jr.

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

Item No. 10
7/14/65

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

July 14, 1965.

Dear Sir:

In recent years, the Board's responsibility for reviewing and approving salaries of Reserve Bank officers, other than Presidents and First Vice Presidents, has been partially implemented by the establishment of general guidelines for use by the Directors in requesting approval of the Board of Governors for proposed changes in officers' salaries.

From the viewpoint of the Board, the guidelines have had a constructive effect on salary administration throughout the System, and have materially assisted the Board in its responsibility for approving officer compensation. The Board believes that the guidelines have assisted the Banks by focusing their attention on the need to plan and schedule merit and promotional advances over a reasonable period of time. The Banks have tended to be more selective in granting adjustments as the quality and quantity of existing and potential officer resources have come under review.

In the light of this experience, the Board has reestablished guidelines for the year 1966 as follows:

1. Annual Review. Except for increases incident to promotions, requests for approval of salary changes should be made at the time of the annual review; at other times, only under unanticipated circumstances.

2. Basis of Increase and Rate of Progression. Increases should not be automatic; in frequency and amount they should reflect relative merit and competitive conditions.

3. Selectivity. To maintain selectivity, and subject to exceptions below, the Board will not ordinarily approve, in any given year, increases for more than 40 per cent of the officer staff at each Reserve Bank. The merit basis for increases should not be avoided by automatic increases in larger amounts at two or three year intervals.

4. Exceptions.

   a. Increases to officers whose salaries are below the minimum of Group D (Groups D and E at New York) are excluded from the 40 per cent limitation. In determining the 40 per cent, the officers in these grades who have been given below-minimum increases will not be included in either the numerator (number of officers' salaries increased) or the denominator (total number of officers).

   b. The exclusion of promotional increases from the 40 per cent calculation will continue, with the same stipulation as in the past, i.e., to be eligible, a promotion must include a concurrent change in title and level of responsibilities.

Salaries of officers proposed for the year beginning January 1, 1966, should be submitted to the Board of Governors not later than November 15, 1965. The Board's Committee on Organization, Compensation, and Building Plans (comprised of Governor Mitchell as Committee Chairman and Governors Balderston and Shepardson) believes that, as in the past, it would be mutually helpful if a preliminary, informal list of proposed salaries is forwarded. The Committee will be available to discuss this with the President of your Bank when in Washington.

The Committee would also like to be advised, at that time, of any plans your Bank may have for building projects of a major nature during the next five years.

This letter is being sent to the Chairman and the President of each Federal Reserve Bank.

Very truly yours,

Merritt Sherman,
Secretary.

TO THE CHAIRMEN AND PRESIDENTS OF ALL FEDERAL RESERVE BANKS.