

Minutes for December 15, 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	<u>(M)</u>
Gov. Robertson	<u>R</u>
Gov. Balderston	<u></u>
Gov. Shepardson	<u>[Signature]</u>
Gov. Mitchell	<u>[Signature]</u>
Gov. Daane	<u>[Signature]</u>
Gov. Maisel	<u>[Signature]</u>

Minutes of the Board of Governors of the Federal Reserve System
 on Wednesday, December 15, 1965. The Board met in the Board Room at
 9:30 a.m.

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

Mr. Sherman, Secretary
 Mr. Kenyon, Assistant Secretary
 Mr. Young, Senior Adviser to the Board and
 Director, Division of International Finance
 Mr. Holland, Adviser to the Board
 Mr. Solomon, Adviser to the Board
 Mr. Molony, Assistant to the Board
 Mr. Fauver, Assistant to the Board
 Mr. Hackley, General Counsel
 Mr. Brill, Director, Division of Research and
 Statistics
 Mr. Farrell, Director, Division of Bank Operations
 Mr. Solomon, Director, Division of Examinations
 Mr. Kakalec, Controller
 Mr. Hexter, Associate General Counsel
 Mr. O'Connell, Assistant General Counsel
 Mr. Shay, Assistant General Counsel
 Mr. Hooff, Assistant General Counsel
 Mr. Koch, Deputy Director, Division of Research
 and Statistics
 Mr. Partee, Associate Director, Division of
 Research and Statistics
 Mr. Sammons, Associate Director, Division of
 International Finance
 Mr. Leavitt, Assistant Director, Division of
 Examinations
 Mr. Thompson, Assistant Director, Division of
 Examinations
 Mr. Spencer, Staff Assistant, Office of the
 Secretary

1/ Withdrew at point indicated in minutes.

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Miss Hart and Messrs. Forrestal, Heyde, Sanders,
and Smith of the Legal Division
Mr. Dahl, Chief, Special Studies and Operations
Section, Division of International Finance
Messrs. Egertson, Goodfellow, Maguire, McClintock,
Poundstone, and Sanford of the Division of
Examinations
Mr. Waller, Supervisory Accountant, Office of the
Controller

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.

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| Letter to St. Joseph Valley Bank, Elkhart, Indiana, approving the establishment of a branch at 351 West Market Street, Nappanee. | 1 |
| Letter to Western Bancorporation International Bank, New York, New York, granting permission to (1) amend its Articles of Association and (2) purchase shares of Philippine Commercial and Industrial Bank, Manila, Philippines. | 2 |
| Letter to Robert M. Raymond, La Jolla, California, regarding the Board's statement issued in connection with its order approving the application of Union Bank, Los Angeles, California, to merge with Republic National Bank of San Diego, San Diego, California. (With a copy to the Federal Reserve Bank of San Francisco.) | 3 |
| Letter to the Federal Reserve Bank of Chicago regarding the question whether a holding company affiliate may declare a stock dividend based upon its equity in undistributed net income of subsidiary banks. (With the substance of the letter to be sent to all Reserve Banks.) | 4 |
| Letter to the Bureau of the Budget requesting an extension of time through June 30, 1966, to use a particular questionnaire in connection with the quarterly survey of bank lending practices; letter to the Presidents of all Federal Reserve Banks regarding the survey. | 5-6 |

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Item No.

Letter to Chairman Patman of the House Banking and Currency Committee regarding (1) the legal basis for the Board's section 32 interpretation with respect to First National City Bank of New York's proposed "commingled investment account" and related questions, and (2) a proposal by The Chase Manhattan Bank (National Association), New York, New York, to acquire the stock of Liberty National Bank and Trust Company of Buffalo, New York, in light of Board's responsibilities under section 7 of the Clayton Act.

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Letter to Senator Long of Missouri regarding a request that the Board consider an amendment to Regulation Q, Payment of Interest on Deposits.

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In connection with Item No. 8, Mr. Molony was authorized to inform a representative of the St. Louis Post-Dispatch, who had inquired about the matter, that the Board had responded to Senator Long's request regarding an amendment to Regulation Q.

Application of Fidelity Bank. There had been distributed a memorandum from the Division of Examinations dated December 10, 1965, and supporting papers with respect to the application of Fidelity Bank, Beverly Hills, California, to merge with South Bay Bank, Manhattan Beach, California. The Division's recommendation was favorable.

At the Board's request, Mr. Egertson reviewed the facts of the case, the competitive factor reports received from the other Federal bank supervisory agencies and the Department of Justice, and the reasons underlying the favorable recommendation of the Division of Examinations.

During the discussion that followed, members of the Board noted that Fidelity had been rated as a "problem bank" at the time of the

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1963 examination. This rating had been removed in 1964. However, when the bank was examined in June 1965, its condition was found to have deteriorated and a "problem bank" rating again was assigned. Fidelity was heavily loaned, and its liquidity position was tight. It was also noted that the bank concentrated in lending to real estate developers, brokers, and investors.

The members of the Board then presented their tentative views.

Governor Robertson observed that two small banks were seeking to merge and one of them--Fidelity--was a problem bank. When the last examination of Fidelity was conducted, its asset condition apparently had not improved but instead had deteriorated. Furthermore, Fidelity's capital was low, in addition to which the bank's operations were not broadly based. Neither, in his opinion, was the other bank involved in the merger adequately capitalized. A proposed issue of capital notes by Fidelity early in 1966 would result in a capital position of approximately 81 per cent of the requirement under the Board's formula. While that might be adequate for a bank in good condition, he did not feel it would be adequate in this case. Consequently, he would suggest that a decision be postponed. If this suggestion should be accepted, the Federal Reserve Bank of San Francisco would be requested to inform Fidelity that the Board was inclined to disapprove the proposed merger unless Fidelity wished to withdraw the application and steps then were

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taken to put the bank in such condition as to warrant approval. If that were done, the application could be resubmitted.

Governor Shepardson stated that he, too, had been bothered by the apparent condition of Fidelity Bank. The Reserve Bank seemed to feel that the management of the bank had the capacity to improve the institution, but the bank's overall record did not look good. While he was not sure of the best procedure to follow, he thought Governor Robertson's suggestion had merit.

Governor Mitchell commented that he felt much the same as Governors Shepardson and Robertson. Fidelity Bank appeared to be heavily committed in a relatively hazardous lending field. It seemingly had an overexposure in its loan portfolio. As to the proposed merger, it was difficult to take two weak banks and make a strong one. Before the proposed merger was approved, Fidelity should make a better showing than it had thus far.

Governor Maisel said that he was somewhat in agreement with the views expressed. However, he noted that the bank had acquired in late 1964 the mortgage servicing portfolio of McMillan Mortgage Company. This portfolio, carried as a nonledger asset, was valued at over \$3-1/2 million but was not assigned a value in estimating capital adequacy. Also, the bank had recently added as a director a man of stature in the savings and loan industry, who apparently must have considered the bank a sound institution. For these and other reasons, including

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certain steps toward improvement cited by the Reserve Bank in the past few months, it seemed well to be careful about reaching conclusions concerning the bank's present condition based on a reading of reports of examinations in the past.

Mr. Solomon commented that Governor Maisel had made a valid point. It was important, he added, to bear in mind that although Fidelity's operations were quite specialized, this was not necessarily a weakness. There was reason to believe that the real estate lending business had been run quite competently. The State Superintendent of Banks, for example, had indicated that he felt Fidelity was soundly managed. Recently the bank had cut back on its loans and increased its liquidity; and if Fidelity added to its capital as proposed, the bank should be in a fairly satisfactory condition.

Mr. Leavitt, responding to a question about Fidelity's "problem" rating, pointed out that it was hard for examiners to appraise a specialized institution of this kind. The loans were difficult to evaluate. While real estate loans usually involved a certain risk, Fidelity reportedly had an executive officer capable of servicing such loans and working out problems without incurring too much loss. On the basis of the most recent information supplied by the Reserve Bank, it appeared that Fidelity may well have worked its way out of the problem bank category. There probably was not too much potential loss in the loans classified as substandard, and earnings prospects appeared more favorable.

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Mr. Solomon emphasized that the bank had been responsive to the special supervisory interest shown in its case. The fact that the bank had improved its position in the past few months under the impact of an adverse examination report indicated that it was paying attention to the criticisms it had received. He felt the evaluation of the bank's assets should be viewed in the light that, while a large volume of loans had been classified substandard, this did not necessarily mean that such loans involved a significant loss.

After further discussion, Governor Robertson said it seemed to him that when there was a merger proposal before the Board and the applicant bank's condition was suspect, the bank should be thoroughly examined. Therefore, he felt that before the Board made a decision on this application, an examiner should ascertain whether the bank was in a position to expand its operations through merger. An examination of this kind should employ the best staff resources available. The Board should be certain that it took appropriate action where the record of the applicant bank raised questions.

Governor Shepardson inquired about the element of timing involved, and Mr. Leavitt responded that the applicant bank would like to consummate the merger by the end of the year. Reportedly, Fidelity had a retirement program that could only be reopened at year end.

Governor Robertson then commented that, at the least, a top examiner from the Reserve Bank could be sent to Fidelity to meet with

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the directors and officers and attempt to satisfy himself that the bank was a reasonably sound institution. Other members of the Board expressed the view that this procedural suggestion was appropriate. Accordingly, it was agreed that this procedure would be followed and that the Board would then give further consideration to the application.

Applications of United Virginia Bankshares and Williamsburg State Bank (Items 9-13). Pursuant to the decision at the meeting on October 13, 1965, there had been distributed drafts of orders and a statement reflecting approval of (1) an application by United Virginia Bankshares Incorporated, Richmond, Virginia, to acquire shares of Williamsburg State Bank, Williamsburg, Virginia, a proposed new bank, and (2) an application of Williamsburg State Bank to merge with Peninsula Bank and Trust Company, Williamsburg, Virginia, and James-York Bank, James City County (Williamsburg), Virginia. A copy of Governor Robertson's dissenting statement relating to the proposals also had been distributed.

There being no objection to certain editorial changes suggested by Mr. O'Connell, the issuance of the orders and statement was authorized. Copies of the orders and statement, as issued, are attached as Items 9-11, and a copy of Governor Robertson's dissenting statement is attached as Item No. 12. Attached as Item No. 13 is a copy of the letter sent to the Organization Committee of Williamsburg State Bank approving the application made on behalf of that bank for membership in the Federal Reserve System.

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Governor Balderston then withdrew from the meeting to attend a meeting of the interagency Coordinating Committee on Bank Regulation.

Short-term promissory notes (Item No. 14). With a memorandum from the Legal Division dated December 6, 1965, there had been distributed a draft of letter to Chairman Patman of the House Banking and Currency Committee in reply to his letter of November 24 regarding the issuance of short-term promissory notes by national banks.

Chairman Patman's letter pointed out that under a 1965 ruling by the Comptroller of the Currency national banks could issue short-term promissory notes without regard to the limitations on indebtedness contained in section 5202 of the Revised Statutes. Another ruling of the Comptroller, published in 1964, was to the effect that issuance of promissory notes of any maturity by national banks did not give rise to deposits in such banks and that provisions of the Federal Reserve Act relating to reserve requirements and limitations on interest rates were not applicable. Chairman Patman expressed the view that short-term promissory notes must either represent indebtedness subject to the borrowing limitations or deposits subject to applicable legal requirements. He requested that the Banking and Currency Committee be advised of the Board's opinion regarding the status of such notes.

The proposed reply would indicate that the Board was of the opinion that such promissory note transactions gave rise either to

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indebtedness of a bank that would be subject to R.S. 5202 or to deposits that would be subject to reserve requirements and legal limitations on interest rates. The letter would also state that the Board was giving intensive consideration to the promissory note problem and that it expected to reach a decision on this matter in the near future.

Governor Robertson emphasized his feeling that the Board should act promptly to issue a proposed amendment under which short-term promissory notes issued by member banks would be classified as deposits. Consequently, he would be inclined to take a different approach in the letter to Chairman Patman and indicate that the Board contemplated publishing such an amendment in the Federal Register for comment.

Chairman Martin indicated that he felt that the proposed amendment should first be discussed with the Comptroller of the Currency as a matter of appropriate interagency coordination. He noted that Governor Balderston was even now attending a meeting of the Coordinating Committee on Bank Regulation, through which an effort was being made to resolve matters of mutual interest in the area of bank supervision.

Governor Shepardson said he was inclined to agree in principle with Governor Robertson that it was preferable to take action on a problem before there was great pressure to do so. However, he also agreed with Chairman Martin's view that it was important to coordinate with other appropriate agencies to a reasonable extent.

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At the conclusion of further discussion, the letter to Chairman Patman was approved, along lines suggested by Governor Robertson toward the end of the discussion, to indicate that the Board was attempting to work out in a satisfactory manner, in coordination with other appropriate Government agencies, a solution to the matter on which Chairman Patman had requested the Board's opinion. A copy of the letter, in the form sent, is attached as Item No. 14.

Director appointments. It was agreed to ascertain through the Chairmen of the appropriate Federal Reserve Banks whether the following persons would accept appointment, if tendered, as Federal Reserve Bank branch directors for the terms indicated, with the understanding that if it were found that they would accept, the appointments would be made:

William G. Hupfeldt, President, Schluderberg-Kurdle Company, Baltimore, Maryland, as a director of the Baltimore Branch of the Federal Reserve Bank of Richmond for the unexpired portion of the term ending December 31, 1966.

Castle W. Jordan, President, Ryder Systems, Inc., Miami, Florida, as a director of the Jacksonville Branch of the Federal Reserve Bank of Atlanta for the three-year term beginning January 1, 1966.

Frank G. Smith, Jr., Vice President, Mississippi Power and Light Company, Jackson, Mississippi, as a director of the New Orleans Branch of the Federal Reserve Bank of Atlanta for the three-year term beginning January 1, 1966.

Secretary's Note: It having been ascertained that Messrs. Jordan and Smith would accept, appointment telegrams were sent to them on December 20, 1965.

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John W. Sheldon, President of Chas. A. Stevens & Co., Chicago, Illinois, and a Class C director of the Federal Reserve Bank of Chicago, was appointed Deputy Chairman of the Bank for 1966.

By this point in the meeting, the various representatives of the Legal and Examinations Divisions who had been present for the consideration of particular legal or bank supervisory items had withdrawn from the room. Messrs. Johnson, Director, Division of Personnel Administration, Kelleher, Director, Division of Administrative Services, and Schwartz, Director, Division of Data Processing, entered the room at this point.

Board budget for 1966 (Items 15 and 16). There had been distributed to the Board with a covering memorandum from the Controller dated December 6, 1965, a proposed Board budget for the calendar year 1966 in the total amount of \$9,811,000. The proposed budget was \$941,000 (10.6 per cent) higher than the 1965 budget, and it was about \$877,000 (9.8 per cent) more than estimated expenses of \$8,934,000 for 1965.

The proposed budget reflected an increase of \$367,200 in personal services and \$553,500 in nonpersonal services. The increase in personal services reflected factors such as the full-year effect of the general pay increase for Board employees, the additional cost of new positions and positions vacant part or all of 1965, and the estimated cost of normal prospective salary adjustments. The increase in nonpersonal

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services reflected, among other things, provision for architectural expenses related to the planning of an annex building across "C" Street, the cost of certain alterations to the cafeteria facilities, and estimated costs relating to the rental of a new computer. The increases in the personal and nonpersonal accounts were partially offset by an estimated decrease in expenditures for economic and other surveys.

Mr. Kakalec pointed out that 75 per cent of the proposed budget of slightly less than \$10 million represented the cost of salaries and employee benefits. A major increase in the budget for salaries was attributable to expansion of staff, with 22 positions established thus far in 1965 and 22 more proposed in 1966. After outlining major areas of increase in nonpersonal services accounts, he noted that in the area of economic and other surveys the December 6 memorandum indicated a net decrease. However, it also showed that estimated expenditures in 1966 would exceed \$300,000, of which nearly 60 per cent (\$175,000) represented the cost of banking markets surveys.

Following Mr. Kakalec's summary, Governor Shepardson commented that as the Board would recall, early this fall he had sent a memorandum to each division head requesting information as to economies realized through elimination of nonessential activities and through improvement in manpower utilization. Each division also had been requested to provide a listing of activities that might be discontinued if it should

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be determined that a 5 per cent reduction in the budget was required. Later he had sent to the Board members a memorandum outlining certain savings that had been achieved or were being achieved by the respective divisions. Governor Shepardson also said, in this connection, that he had discussed with Mr. Young the work involved in the preparation by the Division of International Finance of papers relating to the economic position of foreign countries. Such papers were prepared principally in connection with the renewal of reciprocal foreign currency (swap) arrangements. He and Mr. Young had discussed moving to abbreviated papers, and if the Board members had any comments or reactions as to whether this would be desirable, either he or Mr. Young would be glad to receive them. There had been reports from the divisions, he added, of some relatively minor savings in several areas, along with suggestions for certain procedural changes that might result in savings. Some of the latter involved matters, such as the style of Board minutes, that the Board might want to discuss at greater length later.

Governor Shepardson concluded his comments by pointing out that it seemed generally agreed that most of the possibilities for significant savings depended upon whether or not the Board wished to curtail various program activities. In other words, there seemed to be little prospect of making substantial budget reductions without looking at the basic programs. In this regard, he observed that to

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a large extent the major costs were directly or indirectly concerned with or related to research programs or to construction and equipment programs. Accordingly, Governor Shepardson suggested that Mr. Brill review the broad outlines of the program conducted by the Division of Research and Statistics, looking toward expressions by the Board as to whether significant reductions might be made in any of the areas of activity.

Mr. Brill indicated that the current program of the Division focused on the following categories of activity: (1) basic research underlying certain economic and financial relationships; (2) improvement of statistics; (3) major studies requested by the Board; and (4) communication of staff analysis to the Board and the Federal Open Market Committee. Mr. Brill went on to discuss in some detail the categories of the Division's work that he had outlined.

Following Mr. Brill's comments, Governor Mitchell commended the research program in its broad outlines. However, he thought the staff experienced some difficulty in distinguishing between information of general interest and information vital for policy formulation at any given time. There was some tendency to issue material repetitively in a particular format and according to a prescribed schedule, thus reducing the possibilities for creative effort. He urged, among other things, substitution of tabulations for excessive verbalization in reports. He then spoke of the \$175,000 budgeted for banking markets

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surveys. While he favored the idea of such surveys in principle, he cautioned against a degree of repetition that might yield diminishing returns.

Governor Maisel observed that he, too, had been concerned about the work that was involved in certain programs in relation to their value from the standpoint of decision making. He suggested analysis of the cost of various research projects in terms of their relationship to policy decisions, with a view to allocating funds and manpower to the most vital areas in appropriate proportions.

There followed a general discussion of certain types of memoranda distributed to the Board on a continuing basis that might be submitted in summary form or on a less frequent schedule. Reference was made to the complication sometimes involved due to the reliance placed on the Board's staff by the Federal Reserve Banks and by Government departments and agencies for various kinds of information. The staff indicated that the problem of meeting diverse needs was under continuing study.

Chairman Martin then observed that the best possible research effort directed toward the decision-making process should be conducted. To him, this was the essence of the matter. The Board could, of course, find the financial resources for doing a quantity of work, but neither financial nor human resources should be wasted. The main emphasis of the Board's research program should be on quality, and he felt the program had been moving in that direction.

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Governor Shepardson summarized by saying that the program described by Mr. Brill appeared to be regarded as generally appropriate, with indication that it should be pushed forward. At the same time, continued attention should be given to locating areas where routine work could be curtailed, thus releasing manpower for more productive efforts.

Turning to the subject of the proposed annex building across "C" Street, Governor Shepardson said that the work on plans for that building had been slowed temporarily because of certain changes in the personnel of the architectural firm. He hoped, however, that within a short time a different, and more desirable, proposal would be forthcoming. Meanwhile, the firm of Raymond Loewy/William Snaith, Inc., was ready to present the second phase of its study of space utilization in the present building, but it appeared that implementation of that firm's proposals, even if they were accepted, would have to be deferred pending the availability of space in the annex building. On the matter of cafeteria facilities, Government Services, Inc., had been consulted. Through that organization a study of possible alterations to the cafeteria (not including the dining room area) was being made, particularly with a view to operating two serving lines. He suggested that the Board authorize entering into a contract with a consultant for plans for the proposed remodeling, which was expected to involve a cost of approximately \$105,000.

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Governor Mitchell noted that no final decision had yet been made as to the functions that would be performed at the proposed relocation site at Culpeper, Virginia. There was also the question of what might be done in the area of allocating responsibility for bank supervision at the Federal level, along with the possibility of delegation of certain functions by the Board to the Reserve Banks. These factors left the question of future space requirements unresolved. A related question was whether the Board desired to stay in the present building. Although the Board probably would not want to discard it, some extensive renovations would soon be necessary. All of these things suggested that further consideration should be given to probable future space requirements incident to determination of the need for an annex building.

Governor Shepardson said that he thought Governor Mitchell had raised valid points. However, he also thought that they were being taken into account. The first part of the Loewy/Snaith study had indicated that all present personnel could be accommodated in the existing building, but it developed that this would involve a degree of crowding that probably would not be acceptable. On restudy, the Loewy/Snaith firm had tried to make a more realistic appraisal in light of pertinent factors, including possible expansion of certain activities and the effect upon space needs. The firm now felt, and the Board's staff agreed, that a desirable layout would permit taking

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care of only a portion of the divisions of the staff in the present building. The impact that might result from delegation of certain functions to the Reserve Banks was difficult to measure in terms of space requirements. As an example, the impact on the examinations function of delegations of authority or a restructuring of bank supervisory responsibility would obviously have a collateral effect on other areas of the Board's work, but in terms of space requirements the result might not be too significant. As to the Culpeper installation, account had been taken of present plans for activities at that location, and space was not being provided for those functions in an annex building. In sum, the space being visualized for the annex building was not believed to be excessive, even allowing for the possible divestment of certain functions, in the light of reasonable expectations of future growth.

Governor Maisel said that he had some preference for trying to contain operations in a single building. He did not feel that he knew enough about the problem to reach a conclusion at this juncture. However, he gathered that the Board, by approving the proposed budget, was not committing itself either to the construction of an annex building or remodeling of the present structure, and that further consideration could be given to the matter following the Loewy/Snaith presentation.

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Governor Shepardson replied that authorization to remodel the present cafeteria facilities was the only commitment by the Board that was being suggested at this stage.

At the conclusion of further discussion, the proposed budget for 1966 was approved unanimously. It was understood that this action included authorization for remodeling the present cafeteria facilities at a cost estimated at approximately \$105,000, as provided in the 1966 budget. Tables summarizing the approved budget are attached to these minutes as Items 15 and 16.

Secretary's Note: Under today's date a letter was sent to Clifton M. Truesdale, Springfield, Virginia, confirming arrangements for the retention of his services in developing a plan for the cafeteria expansion and modernization.

All members of the staff then withdrew from the meeting and the Board went into executive session.

The Secretary was informed later by Governor Shepardson that during the executive session the following actions were taken by the Board effective January 1, 1966:

1. Travel. The Board expressed its concurrence with the objective of the President, as stated in the Bureau of the Budget memorandum of August 23, 1965, regarding reduction of travel cost to the essential minimum. In this connection, it approved the following directives:

(a) Air transportation. In general, less than first-class accommodations will be used except in situations where first class is clearly justified as determined by guidelines to be worked out by the Controller and the Board member in charge of internal affairs.

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(b) Hotel room reimbursement. In cases where a Board employee is accompanied by his wife, reimbursement for hotel room shall be on the basis of single occupancy cost. In cases where the double occupancy rate is the same as the single rate, this fact shall be attested by attachment of a copy of the hotel rate schedule or other satisfactory evidence.

(c) Gifts to hostesses at private parties and unusually large gratuities are not to be considered reimbursable expenses.

2. Luncheons and Dinners for Official Visitors. The Board reaffirmed its approval of the present program of official luncheons and dinners as beneficial and desirable. It also approved the following specific directives in connection therewith:

(a) Cost of official group luncheons to Board employees shall be \$1.00 per person, with the difference between that amount and the normal charge for such luncheon to be charged to the budget item for official dinners, etc.

(b) Small luncheons tendered by Board members or senior officials of the Board staff to distinguished visitors shall normally be held in the Board building. Justifiable exceptions shall be cleared with the Board member in charge of internal affairs.

(c) Due to lack of evening dinner facilities in the Board building, small dinners tendered distinguished visitors by appropriate individuals may be scheduled outside the Board building and reimbursement authorized, subject to clearance with the Board member in charge of internal affairs.

3. Due to the pendency of the Board's building program, the Board directed that extensive refurbishing or refurnishing of staff offices be deferred until the building program is further advanced. This does not preclude first-class maintenance or necessary replacement of existing furniture.

4. The Board approved purchase of a suitable television set for the Board library and such sets for Board members' offices as individual members may desire.

The meeting then adjourned.

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

Telegram to the Chairman of the Federal Reserve Bank of San Francisco (copy attached as Item No. 17) authorizing the Assistant Federal Reserve Agent to produce certain currency records in connection with a tax proceeding.

Memorandum from the Division of Administrative Services recommending acceptance of the resignation of Hubert L. Steward, Messenger in that Division, effective at the close of business December 15, 1965.

On December 14, 1965, Governor Shepardson approved on behalf of the Board memoranda recommending the following actions relating to the Board's staff:

Salary increases, effective December 19, 1965

Joyce A. Matile, Stenographer, Legal Division, from \$4,641 to \$5,181 per annum, with a change in title to Secretary.

Margaret I. Ratcliffe, Clerk-Typist, Division of Research and Statistics, from \$4,149 to \$4,289 per annum.

Joyce J. Wood, Stenographer, Division of Research and Statistics, from \$4,641 to \$4,797 per annum.

Patricia L. Gannon, Secretary, Division of Examinations, from \$6,854 to \$7,046 per annum.

Millicent R. Hudnall, Stenographer, Division of Examinations, from \$4,641 to \$4,797 per annum.

Darrell Pepper, Chart Machine Operator, Division of Data Processing, from \$5,181 to \$5,352 per annum.

Mary Ann Rose, Clerk-Typist, Division of Data Processing, from \$4,149 to \$4,289 per annum.

On December 14, 1965, Governor Shepardson noted on behalf of the Board a memorandum advising that Sampson H. Bass, Assistant Controller, had filed application for retirement, effective December 31, 1965.

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

Letter to the Federal Reserve Bank of Chicago (copy attached as Item No. 18) approving the appointment of William E. Ruddy and John P. Trinklein as examiners.

Memorandum from Mr. Young, Senior Adviser to the Board and Director, Division of International Finance, dated December 15, 1965, recommending that Robert Solomon, Adviser to the Board, be designated to serve on a task force being established by the Bureau of the Budget to review the so-called "gold budget."

Memorandum from Mr. Sherman, Secretary of the Board, dated December 10, 1965, requesting approval of specified overexpenditures in two accounts of the 1965 budget of the Office of the Secretary.

Memoranda recommending the following actions relating to the Board's staff:

Salary increases, effective December 19, 1965

Bernice Bell, Stenographer, Division of Examinations, from \$4,641 to \$5,181 per annum, with a change in title to Secretary.

Susan Chapman, Personnel Clerk, Division of Personnel Administration, from \$4,289 to \$4,641 per annum.

Salary increases, effective January 2, 1966

Lucile R. MacLean, Librarian, Division of Research and Statistics, from \$8,749 to \$9,003 per annum.

Dorothy S. Projector, Economist, Division of Research and Statistics, from \$15,696 to \$16,204 per annum.

Royal Shipp, Economist, Division of Research and Statistics, from \$9,267 to \$9,573 per annum.

Linda L. Cochran, Stenographer, Division of Personnel Administration, from \$4,641 to \$4,797 per annum.

Robert Sampson, Personnel Assistant, Division of Personnel Administration, from \$8,961 to \$9,267 per annum.

Gerard E. Phillips, Messenger, Division of Administrative Services, from \$3,507 to \$3,626 per annum.

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Salary increases, effective January 2, 1966 (continued)

Irving Gedanken, Statistician, Division of Data Processing, from \$15,696 to \$16,204 per annum.

Kate G. Mogerman, Draftsman, Division of Data Processing, from \$4,641 to \$4,797 per annum.

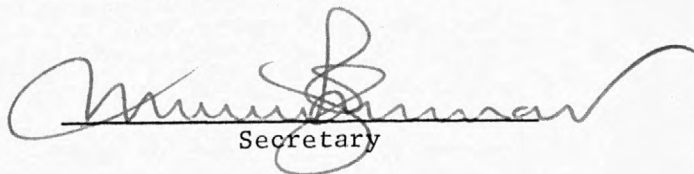
Transfers

Bonnie Brooke, from the position of Statistical Assistant in the Division of Research and Statistics to the position of Digital Computer Programmer in the Division of Data Processing, with no change in basic annual salary at the rate of \$5,181, effective December 19, 1965.

Edna J. Chavis, from the position of Stenographer in the Division of Personnel Administration to the position of Stenographer in the Division of Administrative Services, with no change in basic annual salary at the rate of \$4,797, effective December 19, 1965.

Acceptance of resignation

Kalman Schaefer, Statistician, Division of Data Processing, effective at the close of business December 24, 1965.


Secretary



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

4183
Item No. 1
12/15/65

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

December 15, 1965

Board of Directors,
St. Joseph Valley Bank,
Elkhart, Indiana.

Gentlemen:

The Board of Governors of the Federal Reserve System approves the establishment by St. Joseph Valley Bank, Elkhart, Indiana, of a branch at 351 West Market Street, Nappanee, Indiana, 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.)

Item No. 2
12/15/65

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

WASHINGTON, D. C. 20551

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

December 15, 1965.



Western Bancorporation
International Bank,
61 Broadway,
New York, New York. 10015

Gentlemen:

Reference is made to your letter dated November 1, 1965, enclosing a copy of a resolution adopted by the shareholders amending the Articles of Association of your Corporation to increase the capital stock to \$7,500,000, consisting of 750,000 shares of the par value of \$10 each. The Board of Governors approves the amendment to Article SEVENTH of your Articles of Association. Please advise the Board of Governors when the capital increase has been effected.

As requested in your letter of October 27, 1965, addressed to the Federal Reserve Bank of New York, the Board of Governors grants consent for Western Bancorporation International Bank ("WBIB"), to purchase and hold approximately 136,340 shares, par value Pesos 100 each, of Philippine Commercial and Industrial Bank ("PCIB"), Manila, Philippines, at a cost of approximately \$3,846,150, provided such shares are acquired by December 31, 1967. In this connection, the Board also approves the purchase and holding of such shares in excess of 15 per cent of WBIB's capital and surplus.

Section 211.9(b) of Regulation K, which relates to "Liabilities of one borrower," provides, in part:

"Except as the Board may otherwise specify, the total liabilities to a Corporation of any person shall at no time exceed 50 per cent of the Corporation's capital and surplus, or 10 per cent thereof if it is engaged in banking. In this paragraph 'liabilities' includes: any obligations for money borrowed and shares of stock; . . ."

Subject to continuing observation and review, the Board suspends, until further notice, the provisions of the above-quoted portion of Section 211.9(b) to the extent that the investment by WBIB in the stock of PCIB would cause "liabilities" to exceed the percentage limitations stated therein.

Western Bancorporation
International Bank

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The foregoing consent is given with the understanding that the investment now being approved, combined with other foreign loans and investments of your Corporation and United California Bank, will not cause the total of such loans and investments to exceed the guidelines established under the voluntary foreign credit restraint effort now in effect and that due consideration is being given to the priorities contained therein.

Very truly yours,

(Signed) Karl E. Bakke

Karl E. Bakke,
Assistant Secretary.



BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

OFFICE OF THE CHAIRMAN

December 15, 1965.

Mr. Robert M. Raymond,
325 Dunemere Drive,
La Jolla, California. 92037

Dear Mr. Raymond:

This is in reply to your letter of November 24, 1965, regarding the Board's statement issued in connection with its order approving the application of Union Bank, Los Angeles, California, to merge with Republic National Bank of San Diego, San Diego, California.

When a bank submits an application presenting factors and reasoning in support of its request, and when the Board reaches a decision on the basis of its evaluation of those and other available data, it may be that the official statement of reasons for the action will prove embarrassing to some persons. Although the Board endeavors to guard against statements that would needlessly have such an effect, it is difficult to see how this can always be avoided, particularly in view of the requirements of the bank merger legislation. The Board has an obligation to make available to the public the reasons for its approval, and after reviewing this case in detail it is the Board's judgment that the statement reflected the facts before it.

The Board regrets any misunderstandings that may have arisen from its statement, including any implications that you may regard as derogatory to you personally, even if not so intended.

Sincerely yours,

(Signed) Wm. McC. Martin, Jr.

Wm. McC. Martin, Jr.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Item No. 4
12/15/65

WASHINGTON, D. C. 20551

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

December 15, 1965



Mr. Leland M. Ross, Vice President,
Federal Reserve Bank of Chicago,
Chicago, Illinois. 60690

Dear Mr. Ross:

This refers to your letter of November 15, 1965, transmitting a request for information as to whether a holding company affiliate may declare a stock dividend based upon its equity in undistributed net income of subsidiary banks.

As you know, before a holding company affiliate obtains a voting permit from the Board, it is required by section 5144(e)(4) of the Revised Statutes to agree that it will declare dividends only out of actual net earnings. The apparent purpose for this provision of law is to prevent a distribution of assets above actual net earnings. However, paragraph (7) of the application for a voting permit (Form P-1), wherein the holding company affiliate agrees to this provision of law, expressly excepts "stock dividends" as there would be no distribution of assets.

In a letter dated November 15, 1939 (S-192; FRLS 7199), the Board stated that actual net earnings generally should not be construed to include earnings of subsidiary banks which have not been distributed to the holding company affiliate. Since stock dividends do not result in a distribution of assets, it is the Board's conclusion that a holding company affiliate may pay a stock dividend from its proportionate interest in the undistributed income, or surplus from increase of equity, of its subsidiaries, provided (a) that such undistributed income or surplus is included in the capital accounts of the holding company affiliate in its annual reports to the Board and in published financial statements, and (b) that any such dividend is accounted for in accordance with generally accepted accounting principles and is not in contravention of State law.

Very truly yours,
(Signed) Merritt Sherman

Merritt Sherman,
Secretary.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Item No. 5
12/15/65

WASHINGTON, D. C. 20551

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

December 17, 1965.



Mr. Edward T. Crowder, Clearance Officer,
Office of Statistical Standards,
Bureau of the Budget,
Washington, D. C. 20503

Dear Mr. Crowder:

In September 1964, the Budget Bureau approved on an experimental basis a questionnaire to be used in connection with a quarterly survey of bank lending practices to be conducted for a period of about one year with approval expiring in December 1965. Extension of the survey in its present form, through June 30, 1966, is requested.

A System Committee has just completed a preliminary review of survey results over the past five quarters. Comments were obtained from the academic community, from about one-fourth of the respondent banks, and from users of the information within the System. The consensus was that the survey should be continued. It was found that the costs of the survey are small and it provides policy makers with an independent measure of changes in credit availability at the Nation's largest banks. The survey would be particularly useful to the System during a period when monetary policy was undergoing rapid change, particularly if this involved a change in direction.

While the Committee feels that the usefulness of the survey could be increased by changes in the reporting form and in coverage, it will not be able to complete its work on these proposed changes for several months. Pending receipt of its final recommendations, the Board has approved continuation of the survey in its present form through the middle of next year.

As indicated in the supporting statement submitted with our request of August 24, 1964, the reporting is not burdensome on respondents--the 81 large banks in major cities throughout the country that regularly report quarterly figures on interest rates

Mr. Edward T. Crowder

-2-

on business loans. Completing the lending practices questionnaire requires only about 15 minutes of a senior bank officer's time. The cost to the Federal Reserve of compiling and summarizing the data is nominal.

The survey is presently conducted as of the 15th of March, June, September, and December and coincides with the quarterly interest rate survey. Plans are underway, however, to shift the timing of the latter survey to the first 15 days of February, May, August, and November. When this occurs, the timing of the lending practices survey will be changed accordingly.

Enclosed are three copies of Form 83. Your prompt attention to this request will be appreciated.

Very truly yours,



Merritt Sherman,
Secretary.

Enclosures.



BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

WASHINGTON, D. C. 20551

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Item No. 6
12/15/65

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

December 16, 1965.

Dear Sir:

In the summer of 1964, the System Research Advisory Committee and the Presidents' Conference recommended and the Board authorized a quarterly survey of changes in bank lending practices to be conducted on an experimental basis for a period of about one year. The survey was designed to complement the quarterly interest rate survey and give the System a better knowledge of the extent of changes in nonrate terms of bank lending about which little information is available from other sources.

A System Committee has just completed a preliminary review of survey results. The consensus of the Committee and of those users of the information from whom comments were solicited is that the survey should be continued. While the Committee feels that the survey can be improved by some changes in the reporting form and in coverage, it will not be able to complete its work on the proposed changes for several months. Pending receipt of its final recommendations, the Board has approved continuation of the survey in its present form through the middle of next year.

The next lending practices survey will be conducted as of December 15, 1965, using the present questionnaire, Budget Bureau approval for which expires at the end of this year. The Budget Bureau has been asked to authorize the use of this form through the middle of next year. Plans are underway to shift the timing of the quarterly interest rate survey to the first 15 days of February, May, August, and November. When this occurs, the timing of the lending practices survey will be changed accordingly.

Very truly yours,

Merritt Sherman,
Secretary.

TO THE PRESIDENTS OF ALL FEDERAL RESERVE BANKS.



BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

OFFICE OF THE CHAIRMAN

December 15, 1965

The Honorable Wright Patman, Chairman,
Committee on Banking and Currency,
House of Representatives,
Washington, D. C. 20515

Dear Mr. Chairman:

This is in response to your letters of October 26 and November 24, 1965, asking that you be furnished with (1) a legal memorandum with respect to a recent interpretation of the Board as to the applicability of section 32 of the Banking Act of 1933 to a proposal by the First National City Bank of New York to establish a "commingled investment account", (2) an analysis of a proposal by The Chase Manhattan Bank, National Association, to acquire the stock of Liberty Bank and Trust Company of Buffalo, New York, in the light of the Board's responsibilities under section 7 of the Clayton Antitrust Act, and (3) a consideration of the legality under section 32 of the acquisition by a national bank of the controlling stock of a securities business primarily engaged in activities of the kind described in that section.

In accordance with your request, I enclose a memorandum prepared in the Board's Legal Division with respect to the legal considerations under section 32 of the Banking Act of 1933 in connection with First National City Bank's proposed commingled investment account. However, it appears that there is a misunderstanding as to the time sequence involved in publication of the Board's interpretation on this matter. While First National City Bank had asked the Board for an interpretation on this point last March, the Board did not respond until July 22, 1965, when it wrote a letter expressing its views. When a general interest in this interpretation became apparent, and requests for copies of the interpretation were received, the Board, following the usual practice, authorized formal publication of the interpretation under date of September 29, 1965. That the Board's views on the question were not "suppressed" is evident from the news stories concerning the matter prior to that date.

Concerning the possible applicability of section 21 to the proposal by First National City Bank, the Board for many years has

followed the policy of not expressing views as to whether a certain activity would violate a criminal statute, and it continues to believe this policy a sound one. The Board is not a criminal court, and the implications of expressing the view that certain action would be criminal might be very serious indeed. This does not mean, however, that the Board refrains from issuing warnings in appropriate cases, as is evident from its interpretation in this matter. Indeed, in the present instance, the Board suggested in its letter of July 22, 1965, that First National City Bank consult the Department of Justice on whether section 21 of the Banking Act of 1933 would apply to the bank's proposal to establish and operate a commingled investment account, and was informed subsequently that the bank had done so.

With respect to Chase Manhattan Bank's proposal to acquire the stock of Liberty National Bank of Buffalo, Chase has requested the Board to determine that consummation of that proposal would not cause it to become engaged "as a business in holding the stock of, or managing or controlling banks", and would therefore not cause Chase to be a "holding company affiliate" under section 2(c) of the Banking Act of 1933, or, if the Board should determine otherwise, that the Board grant Chase a voting permit entitling it to vote the stock of Liberty National Bank and Trust Company that would be held by Chase upon consummation of the proposed transaction. These requests are now under active consideration by the Board, and we will be glad to advise you of the Board's decisions with respect thereto.

Whether consummation of Chase's proposed acquisition of the stock of Liberty National Bank and Trust Company would violate section 7 of the Clayton Act could, of course, be determined only on the basis of a full investigation that would assemble all data relevant to the competitive effect of the transaction. As you know, the Board may institute proceedings under the Clayton Act with respect to the acquisition of stock of a bank only if the Board has reason to believe that the acquiring corporation "is violating or has violated the provisions of section 7 of that Act" (15 U.S.C. 21). The Board's authority in this respect is in contrast to that of the several United States District Attorneys, who are authorized, under the direction of the Attorney General, to institute proceedings under the Clayton Act "to prevent and restrain" violations (15 U.S.C. 25). You may be assured, however, that, to the extent that it may become necessary, the Board will carefully consider the proposed transaction in the light of its responsibilities under the Clayton Act.

You also ask for the Board's views "on the legality under section 32 of the acquisition by a national bank of the controlling stock of a securities business engaged in dealing in, underwriting, purchasing

and selling securities" in a fashion not permitted by the provisions of 12 U.S.C. section 24, that is to say, broadly speaking, engaged in the securities business as principal, rather than as agent on behalf of others.

Section 32 provides in relevant part that

"No officer, director, or employee of any corporation or unincorporated association, no partner or employee of any partnership, and no individual, primarily engaged in the issue, flotation, underwriting, public sale, or distribution, at wholesale or retail, or through syndicate participation, of stocks, bonds, or other similar securities, shall serve the same time [sic] as an officer, director, or employee of any member bank. . . ."

The Board has always attempted to interpret this section in accordance with the mandate of the Supreme Court in the Board of Governors of the Federal Reserve System v. Agnew case, that the statute is a "preventive or prophylactic measure" (339 U.S. 441, 449 (1947)). However, it is difficult to develop any theory, from the language of the section itself, or in the light of its legislative history, under which the ownership of stock, without more, would bring the section's prohibition into play. Section 32 is directed at certain specific individual interlocking relationships, as "officer", "director", "employee", or "partner", and at business activities of an "individual". Ownership of stock is nowhere mentioned.

However, it seems probable that the situation you have in mind would come within the purview of another section of the Banking Act of 1933, section 20 (12 U.S.C. § 377), which forbids any member bank to be "affiliated in any manner described in section 2(b) hereof" with any securities business engaged in activities of the kinds described in that section. Among the types of affiliation covered in section 2(b) is the ownership or control, by a member bank, of a majority of the voting shares of a corporation or of more than 50 per cent of the shares voted for the election of the corporation's directors.

In addition, of course, paragraph Seventh of 12 U.S.C. section 24 (section 5136 of the Revised Statutes) would seem clearly to forbid acquisition of such shares by a member bank. That paragraph states that "Except as hereinafter provided or otherwise permitted by law, nothing herein contained shall authorize the purchase by the association [national bank] for its own account of any shares of stock of any corporation." The Board is not aware of any other provision of law which would override this prohibition.

Sincerely yours,

(Signed) Wm. McC. Martin, Jr.

Wm. McC. Martin, Jr.

Enclosure

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

OFFICE OF THE CHAIRMAN

December 15, 1965



The Honorable Edward V. Long,
United States Senate,
Washington, D. C. 20510

Dear Senator Long:

This will acknowledge your letter of December 10, 1965, and accompanying memorandum, in which you requested the Board of Governors to consider issuing an amendment to the December 6, 1965, Supplement to Regulation Q, to provide that in those States where the rate of interest payable by banking institutions on time deposits of State moneys is set by statute at the maximum rate prescribed by Regulation Q, the maximum rate of interest payable on such funds shall remain the same as set forth in the Supplement to Regulation Q immediately prior to the issuance of said Supplement. The memorandum accompanying your letter suggests adding the following new paragraph (c) to the Regulation Q Supplement:

"(c) Where, by the provisions of any state statute, the rate of interest payable by banking institutions on time deposits of state moneys shall be the maximum rate of interest which by federal law or regulation a member bank of the Federal Reserve System may from time to time pay on time deposits, the maximum rate set forth in paragraph (a) above shall not apply to such time deposits of state moneys and the maximum rate of interest payable by member banks of the Federal Reserve System on such time deposits of state moneys shall be the same as that which was applicable to such deposits immediately prior to the issuance of this Supplement. This amendment shall be retroactive to December 6, 1965."

The Board is of the opinion that it does not possess legal authority to amend Regulation Q in the manner suggested. The Board also doubts whether it would be proper for it to amend the Regulation by any means that might be legally available in order to deal with this situation.

The authority of the Board to prescribe maximum interest rates on deposits is derived from the thirteenth paragraph of section 19 of the Federal Reserve Act (12 U.S.C. 371b), which provides that the Board

The Honorable Edward V. Long -2-

". . . shall prescribe different rates for such payment on time and savings deposits having different maturities, or subject to different conditions respecting withdrawal or repayment, or subject to different conditions by reason of different locations, or according to the varying discount rates of member banks in the several Federal Reserve districts."

As this provision of the Act indicates, the Board is required to fix different rates of interest on time and savings deposits according to one or more of the criteria enumerated in the statute. The amendment that you suggest would fix a different rate of interest on the basis of the nature of the depositor, a criterion which is not one of the four specified in the statute. Consequently, the Board would have no legal authority to effect such a change in the Regulation.

Under the provision of law above quoted, the Board may prescribe different rates based on "different conditions by reason of different locations". If the Board were to prescribe a different maximum rate of interest on this basis, however, the new rate would necessarily be applicable to all time deposits, and could not apply solely to deposits of State funds. It is considered unlikely that an amendment of this kind would afford satisfactory relief to member banks in Missouri since corporate and individual time deposits might be withdrawn from Missouri banks and redeposited elsewhere.

The Board is also of the view that even if the amendment proposed in your letter were legally permissible and would be sufficient to satisfy the requirements of section 30.260(3) of the Missouri Revised Statutes, it would be inappropriate for the Board to issue an amendment to an administrative regulation for the purpose of interfering with a provision of State law.

For these reasons, the Board has concluded that it would not be advisable for it to make any change in the Supplement to Regulation Q in order to deal with this matter.

We appreciate receiving the expression of your views regarding this matter, and I wish to assure you that the Board took into account all aspects of the problem before reaching its decision.

Sincerely yours,

(Signed) Wm. McC. Martin, Jr.

Wm. McC. Martin, Jr.

UNITED STATES OF AMERICA

BEFORE THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

WASHINGTON, D. C.

In the Matter of the Application of
 UNITED VIRGINIA BANKSHARES INCORPORATED,
 RICHMOND, VIRGINIA,
 for approval of the acquisition of voting
 shares of Williamsburg State Bank,
 Williamsburg, Virginia.

ORDER APPROVING APPLICATION UNDER
BANK HOLDING COMPANY ACT

There has come before the Board of Governors, pursuant to section 3(a)(2) of the Bank Holding Company Act of 1956 (12 U.S.C. 1842(a)(2)) and section 222.4(a)(2) of Federal Reserve Regulation Y (12 CFR 222.4(a)(2)), an application by United Virginia Bankshares Incorporated, Richmond, Virginia, a registered bank holding company, for the Board's prior approval of the acquisition by Applicant of at least 90 per cent of the voting shares of Williamsburg State Bank, Williamsburg, Virginia, a proposed new bank into which would be merged Peninsula Bank and Trust Company and James-York Bank, both of Williamsburg, Virginia.

In accordance with section 3(b) of the Act, the Board notified the Commissioner of Banking for the Commonwealth of Virginia of receipt

of the application and requested his views and recommendation thereon. The Commissioner expressed no objection to approval of the application.

Notice of receipt of the application was published in the Federal Register on July 2, 1965 (30 Federal Register 8500), providing an opportunity for interested persons to submit comments and views with respect to the proposed acquisition. The time for filing such comments and views has expired, and all those received have been considered by the Board.

IT IS HEREBY ORDERED, for the reasons set forth in the Board's Statement of this date, that said application be and hereby is approved, provided that the acquisition so approved shall not be consummated (a) within seven calendar days after the date of this Order or (b) later than three months after said date, and that the Williamsburg Bank shall be opened for business not later than ^{three}~~six~~ months after said date.

Dated at Washington, D. C., this 15th day of December, 1965.

By order of the Board of Governors.

Voting for this action: Chairman Martin, and Governors Balderston, Shepardson, Mitchell, and Daane.

Voting against this action: Governor Robertson.

Present but not voting: Governor Maisel.

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.

(SEAL)

UNITED STATES OF AMERICA

BEFORE THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

WASHINGTON, D. C.

In the Matter of the Application of
 WILLIAMSBURG STATE BANK
 for approval of merger with
 Peninsula Bank and Trust Company
 and James-York Bank.

ORDER APPROVING MERGER OF BANKS

There has come before the Board of Governors, pursuant to the Bank Merger Act of 1960 (12 U.S.C. 1828(c)), an application by Williamsburg State Bank, Williamsburg, Virginia, a proposed new bank, for the Board's prior approval of the merger of that bank and Peninsula Bank and Trust Company, Williamsburg, Virginia, a State member bank of the Federal Reserve System, and James-York Bank, James City County (post office address Williamsburg), Virginia, under the charter and title of the Peninsula Bank and Trust Company. As an incident to the merger, the two offices of Peninsula Bank and Trust Company and the sole office of James-York Bank would become the offices of the resulting bank. Notice of the proposed merger, in form approved by the Board, has been published pursuant to said Act.

Upon consideration of all relevant material in the light of the factors set forth in said Act, including reports furnished by the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the Attorney General on the competitive factors involved in the proposed merger,

IT IS HEREBY ORDERED, for reasons included in the Board's Statement accompanying its Order of this date concerning the acquisition of Williamsburg State Bank by United Virginia Bankshares Incorporated, Richmond, Virginia, that said application be and hereby is approved, provided that said merger shall not be consummated (a) within seven calendar days after the date of this Order or (b) later than three months after said date.

Dated at Washington, D. C., this 15th day of December, 1965.

By order of the Board of Governors.

Voting for this action: Chairman Martin, and
Governors Balderston, Shepardson, Mitchell,
Daane, and Maisel.

Voting against this action: Governor Robertson.

(SEAL)

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

APPLICATIONS FOR THE ACQUISITION OF WILLIAMSBURG STATE BANK
BY UNITED VIRGINIA BANKSHARES INCORPORATED AND FOR THE
MERGER OF WILLIAMSBURG STATE BANK WITH PENINSULA
BANK AND TRUST COMPANY AND JAMES-YORK BANK

STATEMENT

United Virginia Bankshares Incorporated, Richmond, Virginia ("Applicant"), a registered bank holding company, has filed with the Board, pursuant to section 3(a)(2) of the Bank Holding Company Act of 1956 ("the Holding Company Act"), an application for approval of the acquisition of at least 90 per cent of the voting shares of Williamsburg State Bank, Williamsburg, Virginia ("Williamsburg Bank"), a proposed new bank. Applicant also has applied for the admission of Williamsburg Bank to membership in the Federal Reserve System, and proposes to merge into Williamsburg Bank the Peninsula Bank and Trust Company ("Peninsula Bank") and James-York Bank, both of Williamsburg, Virginia.^{1/} Incident to the merger proposal, Williamsburg Bank has applied, pursuant to the Bank Merger Act of 1960 ("the Merger Act") (12 U.S.C. 1828(c)), for the Board's prior approval of the proposed merger under the charter and title of Peninsula Bank. Applicant intends to operate the existing main office and one branch of Peninsula Bank and main office of James-York Bank, respectively, as the main office and branches of the resulting merged institution.

^{1/} The James-York Bank is located in James City County but has a Williamsburg post office address. Herein, the bank is considered as being located in Williamsburg.

Views and recommendation of State supervisory authority. - As required by section 3(b) of the Holding Company Act, the Board notified the Virginia Commissioner of Banking of receipt of the application under the Act and requested his views and recommendation thereon. The Commissioner offered no objection to approval of the application. Subsequently, the Chairman of the State Corporation Commission submitted a letter on behalf of the Commission recommending that the application be approved.

Statutory factors. - Section 3(c) of the Holding Company Act requires the Board to take into consideration the following five factors: (1) the financial history and condition of the holding company and the banks concerned, (2) their prospects, (3) the character of their management, (4) the convenience, needs, and welfare of the communities and the area concerned, and (5) whether or not the effect of the proposed acquisition would be to expand the size or extent of the bank holding company system involved beyond limits consistent with adequate and sound banking, the public interest, and the preservation of competition in the field of banking.

Under the Merger Act, the Board is required to consider, as to each of the banks involved, (1) its financial history and condition, (2) the adequacy of its capital structure, (3) its future earnings prospects, (4) the general character of its management, (5) whether its corporate powers are consistent with the purposes of 12 U.S.C., Ch. 16 (the Federal Deposit Insurance Act), (6) the convenience and needs of

the community to be served, and (7) the effect of the transaction on competition (including any tendency toward monopoly). The Board may not approve the proposed merger unless, after considering all the factors, it finds the transaction to be in the public interest.

To the extent that the statutory criteria embodied in the respective statutes are substantially similar, the facts pertinent to both the holding company proposal and the merger proposal are discussed in common in order to avoid repetition.

Substance of the proposal. - The aforementioned proposed merger - part of Applicant's over-all plan - will not be pursued unless Applicant's acquisition of the Williamsburg Bank is approved. In these circumstances, although consideration has been given to the facts in relation to the statutory criteria embodied in both acts, the Board's Statement herein reflects principally its consideration of the application filed pursuant to the Holding Company Act. This application involves, in effect, the proposed acquisition by Applicant of the two existing banks, the Peninsula Bank, having deposits^{2/} of approximately \$20 million, and the James-York Bank, with deposits of \$2.6 million.

James-York Bank was established as an affiliate, or "satellite", of Peninsula Bank in 1956 when, under State law, banks were not permitted to establish de novo branches beyond the limits of their home office city.

^{2/} Deposits at December 31, 1964. Unless otherwise indicated, all banking data noted are as of this date.

The two institutions are presently affiliated by reason of ownership of a majority of James-York Bank's voting shares by James City Investment Corporation, a holding company which is, in turn, owned by shareholders holding a majority of the shares of Peninsula Bank. The president and executive vice president of Peninsula Bank are, respectively, the president and vice president of James-York Bank, and three of James-York Bank's seven directors are directors of Peninsula Bank. Because of the aforementioned existing affiliation, further evidence of which is contained in the record before the Board, James-York Bank may be regarded, for certain purposes, as merely a third office of Peninsula Bank, and it is so treated in various parts of this Statement, the two institutions being sometimes referred to collectively as "the Banks".

Financial history, condition, prospects, and management of Applicant and the Banks, and other applicable banking factors. - Applicant, which commenced operation as a bank holding company in January 1963, has six subsidiary banks which, at December 31, 1964, operated 47 offices and held total deposits in the aggregate amount of \$499 million. Its brief financial history is satisfactory. Similarly satisfactory are its financial condition and prospects, due primarily to the satisfactory condition and prospects of its subsidiary banks. Applicant's management, which is drawn largely from its subsidiary banks, is regarded as well qualified and experienced.

Peninsula Bank and James-York Bank were organized, respectively, in 1917 and 1956. Peninsula Bank and a newly organized national bank,

which opened for business on December 8, 1965, are the only banks within the city limits of Williamsburg, and they and James-York Bank are the only banks in the combined primary service area of the Banks.^{3/} The financial history, condition, prospects, and management of the Banks are considered satisfactory. However, Applicant foresees that, because of the rapid population growth and increasing tourist trade occurring and anticipated in the Williamsburg area, the present aggregate capital of the merging banks will be inadequate to support anticipated future deposit growth of the resulting bank. Applicant therefore proposes to inject approximately \$600,000 of new capital into the resulting bank to meet foreseeable needs, and to supply in the more distant future additional capital funds as required. Under Applicant's proposal, the Board finds the projected capital structure of Williamsburg Bank to be adequate. While the Banks as now constituted could, in the Board's opinion, successfully meet additional capital needs, their future financial condition and prospects, as a merged institution under Applicant's ownership, appear more favorable in the light of Applicant's proposed capital program.

The proposed management of Williamsburg Bank is found to be satisfactory, since it will be composed of the Banks' present managements.

On the basis of the foregoing, the Board concludes that those aspects of Applicant's proposal that relate to the banking factors

^{3/} The area from which Applicant indicates 84 per cent of the amount of the Banks' combined deposits of individuals, partnerships, and corporations ("IPC deposits") originate.

discussed are consistent with the purposes of both the Holding Company Act and the Merger Act, and weigh in favor of approval under both acts.

Convenience, needs, and welfare of the communities and area concerned. - Both offices of Peninsula Bank are within the limits of Williamsburg, an independent city, and James-York's one office is in James City County, just outside Williamsburg. The Banks' designated combined primary service area, which is also the primary service area projected for Williamsburg Bank, consists of the corporate limits of Williamsburg and the surrounding suburban area in York and James City Counties within an approximate five-mile radius of Williamsburg. The estimated population of the area is 16,000.

In the period 1950-1960, the population of Williamsburg and the adjoining magisterial districts of York and James City Counties increased at an annual rate which was substantially greater than that of the State or the Nation. Tourists, numbering more than 500,000 annually, are the most important factor in the economy. Tourism has been a primary objective of the more than \$72 million expenditure for restoration and capital improvements in Williamsburg. The total employment at three area enterprises - The College of William and Mary, Dow Chemical Company, and the State's largest mental health institution - contributes significantly to the maintenance of the local economy. Less substantial but similar contribution is made by four military facilities located within 12 miles of Williamsburg.

There is no evidence in the record, nor does Applicant contend, that basic banking needs in the Williamsburg area are going unserved. However, Applicant claims, on the basis of its experience, that where a useful service is offered, it will be used even though the public had not previously been aware of a need therefor. Applicant asserts that the need for such service must be anticipated, made apparent, and thereafter served, and that, by so doing, a bank can help promote the social and economic welfare of its service area. Services that Applicant proposes to introduce or improve upon in the Williamsburg area include a broad and convenient source for mortgage, floor plan, and college tuition loans, apartment and motel financing, a revolving credit plan for individuals, and expanded trust services.

The record reflects that there exists a rather heavy local demand for mortgage loans. Of the services proffered by Applicant, the proposed assistance with respect to mortgage credit appears most pertinent. The two banks together have a relatively high ratio of loans to deposits, and are heavily loaned in the mortgage category. While Applicant's subsidiary banks also may at times be heavily loaned and unable to participate extensively in assisting the Banks in handling mortgage credit demands, arrangements have been completed for the sale by Applicant's banks of mortgage loans to five insurance companies and a savings and loan association. Under this arrangement, the subsidiary bank originating a loan will continue to service the loan on a fee basis, and will thus retain direct contact with the borrowers.

The Board concludes that considerations bearing on the convenience, needs, and welfare of the area concerned are consistent with approval of the transaction proposed, and offer some weight for approval.

Effect of the proposed transactions on adequate and sound banking, the public interest, and banking competition. - Applicant's holding company system, the largest banking system in the State, would have 7.2 per cent of the offices and 11.9 per cent of the deposits of all Virginia banks if the proposal were consummated, representing increases from 6.8 per cent and 11.4 per cent, respectively.^{4/} The four bank holding companies operating in Virginia (one of which is not registered under the Holding Company Act) would control 24.3 per cent of the offices and 27.0 per cent of the deposits of all banks, representing increases of .4 per cent and .5 per cent, respectively. In the Board's judgment, such concentration is not so excessive, in either the Applicant's system or in all holding companies, as to preclude the further expansion here proposed. Significant in the assessment of the effect on the banking market of existing concentration is the fact that, in terms of total deposits, the second, third, and fourth in size of the seven largest banking "systems" in Virginia^{5/} are independent banks, and those three independent institutions together hold 25.8 per cent of the deposits of all banks in the State.

^{4/} Data reflected in this paragraph are as follows: Banking offices as of October 31, 1965, and deposits as of December 31, 1964, adjusted to include all mergers consummated and, for bank holding companies, all acquisitions either consummated or approved by the Board as of October 31, 1965.

^{5/} The bank which is fourth in size is practically the same size, in terms of deposits, as the fifth largest banking system, which is the second largest bank holding company in the State.

For purposes of determining the competitive effects of Applicant's proposal, the Board has concluded that the Williamsburg area constitutes the market area most directly affected by Applicant's proposal. In this regard, the Board's attention was directed to the so-called Lower Peninsula Area, consisting of James City and York Counties and the independent cities of Williamsburg, Newport News, and Hampton, bounded by the York River on the north, the Chesapeake Bay on the east, and the James River on the south. However, in the Board's judgment, the Lower Peninsula Area is not a relevant or realistic market area for purposes of the present analysis for the reason that Williamsburg, viewed either in terms of its political or natural boundaries, is isolated from other portions of the so-called Lower Peninsula Area, resulting in its being relatively free from the force of banking competition from and with that area.

Inasmuch as the newly opened national bank is the only other banking institution operating in the Banks' combined primary service area, consummation of Applicant's proposal would result in its control of three of four offices and substantially all of the deposits in the Williamsburg area. This result has significance with respect to its effect on competition both between Peninsula Bank and James-York Bank, and between the Banks and the new national bank. The long-established affiliation between the Banks, by virtue of common majority ownership and common executive managements, effectively negatives the existence

of any significant actual competition between them and makes unlikely measurable future competition. The latter conclusion appears all the more valid in view of the lack of any evidence in the record that the existing affiliation is likely to terminate. With respect to the Board's conclusion regarding the lack of present or likely future competition between the Banks, the Board concurs in the view expressed by the State Corporation Commission that the Banks are "virtually one institution". It may be reasonably concluded that the competitive situation in the Williamsburg area will not be changed measurably by consummation of Applicant's proposal.

The recently opened national bank in Williamsburg may be expected to increase banking competition in the area, measured either as offered by the Banks as presently constituted, or under the proposed ownership and control of Applicant. While an accurate appraisal of the potential competitive effect of consummation of Applicant's proposal on the new national bank is difficult, the Board believes it unlikely that the competitive impact of either the proposed merger or of Applicant's subsequent control of the merged institution will be significantly different or greater than that which would be realized from the Banks' operation as presently constituted. With respect to this conclusion, it may be noted that the Comptroller of the Currency, with knowledge of Applicant's proposed acquisition, expressed the view that the proposed merger of the Banks would not have a significant or substantial adverse effect on competition. In conclusion, the Board assumes that the fact

of the Banks' affiliation was known to the organizers of the national bank at the time they sought its charter, and that Applicant's present proposal regarding the Banks was brought to their attention. The Board notes that no objection to Applicant's proposal has been filed by those organizers.

Turning to the effect of this proposal on existing or potential competition between the Banks and Applicant's existing subsidiaries, Citizens and Marine Bank in Newport News, Applicant's subsidiary, operates 4 offices in Newport News, 4 offices in Hampton, the downtown sections of which are, respectively, 30 and 37 miles from Williamsburg, and 1 office in York County, which appears to be about midway between Williamsburg and Hampton, though not on the principal connecting route. Some 13 miles separate Williamsburg and the nearest office of Citizens and Marine Bank. The next nearest office of any other of Applicant's subsidiaries is in the Richmond area, about 50 miles west of Williamsburg. Since, on the basis of Applicant's analysis, less than two per cent of the amount of the Banks' IPC deposits and less than five per cent of the amount of their commercial, industrial, farm, and consumer loans were derived from the service areas of those two nearest subsidiaries, and since a similar proportion of demand IPC deposits and an even smaller percentage of loans of those subsidiaries, in relation to such loans and deposits of the Banks, were derived from the Williamsburg service area, the Board concludes that no significant existing or potential competition would be eliminated or foreclosed by the proposed holding company acquisition.

The nearest bank to Williamsburg is The First National Bank, located in Yorktown, about eleven miles to the southeast. This bank operates but one office with deposits of about \$5 million. Its business, generally, would appear to be local in nature. Further distant, in the southeastern section of the Lower Peninsula Area, are offices of ten other banks, excluding Applicant's subsidiary. The political and geographical considerations earlier mentioned as separating Williamsburg from the latter area warrant, in the Board's view, the conclusion that no measurable effect on the banks in this area will follow consummation of Applicant's proposal.

In the light of the foregoing considerations and all the facts in the record, the Board concludes that consummation of the subject proposal would not increase Applicant's size or extent beyond limits consistent with adequate and sound banking, the public interest, and the preservation of competition in the field of banking.

On the basis of the relevant facts as contained in the record before the Board, and in light of the factors set forth in the Holding Company and Merger Acts, it is the Board's judgment that the proposal is in the public interest and that the applications regarding the merger of the Banks as proposed and the acquisition by Applicant of the Williamsburg Bank should, therefore, be approved.

December 15, 1965.

DISSENTING STATEMENT OF GOVERNOR ROBERTSON

I am opposed both to the proposed merger of Peninsula Bank and Trust Company and the James-York Bank, and to the acquisition by United Virginia Bankshares Incorporated of control of the merged banking institution for the reason that consummation of both proposals is contrary to the legislative directives embodied in the Bank Merger and Bank Holding Company Acts. As set forth in the Board's Statement, Peninsula Bank and the James-York Bank have been affiliated for some time through their majority control by common stockholders. Because of this affiliation, little or no existing competition between these banks would be eliminated by consummation of the proposed merger. However, in the course of time and changing circumstances, the existing basis of affiliation could terminate, resulting in the growth of healthy competition between the banks. The possibility of this occurrence, with its attending advantages to the public, is precluded, regrettably, by the Board's approval of the proposed merger.

In approving Bankshares' acquisition of the Williamsburg Bank - in actuality, the simultaneous acquisition of two existing banks - the Board found Williamsburg and the immediately adjoining areas to be the significant geographic area within which to appraise the competitive impact of these proposals. My view of the record in this matter makes abundantly clear that a far more relevant market area for analyzing the effect on banking competition to follow consummation of the merger and holding company

proposals approved by the Board is the entire Lower Peninsula Area, which encompasses, in addition to Williamsburg and York and James City Counties, the cities of Hampton and Newport News. The Board's use of the greater Williamsburg area as the relevant market within which to gauge the impact of Applicant's proposals ignores the realities of existing and foreseeable circumstances. Williamsburg is experiencing rapid physical growth and a dynamic economic expansion. Hampton and Newport News each lie but some 30 odd miles southeast of Williamsburg. One of the offices of Applicant's bank headquartered in Newport News is but 13 miles from Williamsburg. In an age of super highways and rapid travel, the cities of Hampton and Newport News are but minutes from Williamsburg - minutes that will be lessened as the geographic limits of Williamsburg continue to expand.

The foregoing compels me to conclude that the Board has erred in two respects. First, its action reflects a miscalculation of the potential competition between the two Williamsburg banks to be acquired (with total deposits of \$23 million) and Applicant's Newport News subsidiary, Citizens and Marine Bank (total deposits of \$47 million). The sizes of these institutions - their closest respective offices separated by but 13 miles - and the likelihood that the two areas concerned will become increasingly geographically and economically integrated, make clear to me the potential for future competition that is precluded by approval of Applicant's bank holding company proposal. A second finding by the Board in which I am unable to concur is that consummation of

Applicant's proposed acquisition would not result in an undue concentration of banking resources under Applicant's control. Applicant, the State's largest banking system, now controls nearly 25 per cent and 21 per cent, respectively, of the banking offices and deposits of the 14 banks operating in the Lower Peninsula Area. Apart from the virtual monopoly that would be given Applicant in the Williamsburg area upon its acquiring the Williamsburg Bank, in the whole Lower Peninsula Area, its control of both offices and deposits would be increased to about 32 per cent. Even were there presented banking factors considerations arguing for approval of Applicant's acquisition of Williamsburg Bank, Bankshares' resulting control of banking offices and resources in the Lower Peninsula Area compels denial of its application. More so is denial compelled where, as here, the record clearly reflects that the banking needs of the Williamsburg area and, as far as I can determine, those of the entire Lower Peninsula Area are being met adequately by the banks in those areas.

In my opinion, the sole significant benefit possibly to flow from consummation of Applicant's acquisition of the Williamsburg Bank is the provision that Applicant asserts it would make for expanded mortgage loans in the Williamsburg area. On analysis, I find that this phase of Applicant's proposal carries little weight toward approval. Even assuming a future need for increased mortgage credit in the Williamsburg area, I am unable to conclude that the demand for such cannot be met either through a restructuring of the Williamsburg banks' loan portfolios, aided, perhaps, by the entry in this field of the newly established national bank, or

through the utilization by the Williamsburg banks of normal correspondent bank relationships.

On the whole, I am unable to find that the relatively insignificant public benefits that may flow from Applicant's acquisition of the Williamsburg Bank are sufficient in any respect to outweigh substantially adverse competitive consequences that are inherent in this proposal. Consequently, I would deny both the merger and bank holding company applications.

December 15, 1965.



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

4216
Item No. 13
12/15/65

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

December 15, 1965

Organization Committee,
Williamsburg State Bank,
Williamsburg, Virginia.

Gentlemen:

The Board of Governors of the Federal Reserve System approves the application made on behalf of Williamsburg State Bank, Williamsburg, Virginia, for stock in the Federal Reserve Bank of Richmond, effective if and when the bank opens for business under appropriate State authorization, subject to the numbered conditions hereinafter set forth:

- (1) Such bank at all times shall conduct its business and exercise its powers with due regard to the safety of its depositors, and, except with the permission of the Board of Governors of the Federal Reserve System, such bank shall not cause or permit any change to be made in the general character of its business or in the scope of the corporate powers exercised by it at the time of admission to membership.
- (2) The net capital and surplus funds of such bank shall be adequate in relation to the character and condition of its assets and to its deposit liabilities and other corporate powers.

Williamsburg State Bank

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- (3) At the time of admission to membership, such bank shall have paid-in and unimpaired capital stock of not less than \$150,000 in order to comply with Federal statutes.
- (4) That Peninsula Bank and Trust Company, Williamsburg, Virginia, and James-York Bank, Williamsburg, Virginia, shall have been merged into subject bank.

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

If at any time a change in or amendment to the bank's charter is made, the bank should advise the Federal Reserve Bank, furnishing copies of any documents involved, in order that it may be determined whether such change affects in any way the bank's status as a member of the Federal Reserve System.

Acceptance of the conditions of membership contained in this letter should be evidenced by a resolution adopted by the board of directors after the bank's Certificate of Authority to Commence Business has been issued. A certified copy of such resolution, together with advice of compliance with the provisions of conditions numbered 3 and 4, should be transmitted to the Federal Reserve Bank of Richmond.

The time within which admission to membership in the Federal Reserve System in the manner described may be accomplished is limited to 90 days from the date of this letter, unless the bank applies to the Board and obtains an extension of time. When the Board is advised that all of the requirements have been complied with and that the appropriate amount of Federal Reserve Bank stock has been issued to the bank, the Board will forward to the bank a formal certificate of membership in the Federal Reserve System.

Since the Williamsburg State Bank will be operating under the charter and title of Peninsula Bank and Trust Company, a State member bank, and, essentially under the same management, it is assumed

Williamsburg State Bank

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that you are acquainted with the officers of the Federal Reserve Bank and the services offered by the System. The Board of Governors sincerely hopes that you will continue to find membership in the System beneficial and your relations with the Reserve Bank pleasant.

Very truly yours,

(Signed) Karl E. Bakke

Karl E. Bakke,
Assistant Secretary.

Enclosure.



BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

OFFICE OF THE CHAIRMAN

December 15, 1965

The Honorable Wright Patman, Chairman,
Committee on Banking and Currency,
House of Representatives,
Washington, D. C. 20515

Dear Mr. Chairman:

This is in response to your letter of November 24 with respect to short-term promissory notes issued by national banks. The occasion for your concern is the 1965 ruling of the Comptroller of the Currency that such notes issued by national banks are not subject to the statutory limitation on the extent to which a national bank may "at any time be indebted, or in any way liable". Revised Statutes, section 5202; 12 U.S.C. 82. As you point out, another ruling of the Comptroller, published in 1964, is to the effect that issuance of "promissory notes of any maturity" by national banks does not give rise to deposits in such banks and that provisions of the Federal Reserve Act relating to reserve requirements and limitations on interest rates do not apply to such promissory note transactions.

For historical reasons and because of changes in banking practices, it has been difficult to develop acceptable criteria that would draw a definite and workable distinction, in all situations, between loans and borrowings on the one hand and deposits on the other. However, it seems clear to the Board of Governors, as it does to you, that promissory note transactions must fall within one category or the other - that is, they necessarily give rise either to indebtedness of the bank that is subject to R. S. 5202 or to deposits that are subject to reserve requirements and legal limitations on interest rates.

In his 1964 ruling, the Comptroller stated that "The proceeds from the sale of such notes do not constitute deposits. . . ." No reason was given for this view, but the ruling did indicate that "Such borrowings are . . . limited by 12 U.S.C. 82." In changing his ruling on the latter point in the September 1965 National Banking Review, the Comptroller stated only that "unsubordinated promissory notes of comparatively short term . . . are issued in the ordinary course of banking business as a means of obtaining funds to be used in making loans and the performance of other banking functions" It is difficult for the Board to see how this statement can serve as a basis for the

The Honorable Wright Patman

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Comptroller's conclusion that the statutory limitations on national banks' indebtedness are inapplicable to these obligations of national banks.

When the practice of issuing unsecured promissory notes in the ordinary course of business developed in 1964, the Board held that "since such notes constitute borrowings, they are not subject, under present law and regulation, to the interest rate limitations or reserve requirements prescribed for deposits by the Board." 1964 Federal Reserve Bulletin 1137; 12 C.F.R. 217.138. Developments since that time have given rise to the question whether it would be advisable to amend Federal Reserve Regulations D and Q to provide that the reserve requirements and interest rate limitations prescribed in those regulations, and the statutory prohibition on the payment of interest on demand deposits, would apply to promissory notes of the kinds that are issued by national banks and member State banks in the ordinary course of their business.

The recent ruling by the Comptroller, to which you refer, has made this problem more complicated (as well as more pressing), but the Board hopes that the supervisory agencies may be able to work out a satisfactory solution in the near future.

Sincerely yours,

(Signed) Wm. McC. Martin, Jr.

Wm. McC. Martin, Jr.

1966 Budget
Summary by Divisions

Schedule A

Division	1965		1966 Budget	Over (Under) 1965 Expenses
	Budget	Expenses (Estimated)		
Offices of Members of the Board	\$ 508,392	\$ 527,765	\$ 562,731	\$ 34,966
Office of the Secretary	385,319	380,688	413,497	32,809
Legal Division				
Regular	308,018	308,114	356,035	47,921
Special:				
Printing F.R. Act	-	-	15,500	15,500
Division of Research and Statistics				
Regular	2,025,676	2,040,070	2,164,029	123,959
Special:				
Academic Consultants	12,410	8,190	12,325	4,135
Division of International Finance	601,485	576,941	649,290	72,349
Division of Examinations	927,210	917,644	1,053,008	135,364
Division of Bank Operations	290,094	279,544	299,896	20,352
Division of Personnel Administration	219,486	225,118	239,406	14,288
Division of Administrative Services				
Regular	1,622,526	1,618,759	1,672,880	54,121
Special:				
Furniture Replacement Program	13,500	12,174	20,350	8,176
Supplements - Banking and Monetary Statistics	15,498	10,566	3,409	(7,157)
Replacement - Venetian Blinds	11,000	-	11,000	11,000
Special Mailing Equipment	-	-	13,300	13,300
Repairs - Retaining Walls, etc.	17,544	20,807	13,036	(7,771)
Youth Opportunity Program	-	2,379	5,250	2,871
Printing 2nd System Booklet	20,000	-	-	-
Office of the Controller	111,551	108,523	113,773	5,250
Office of Defense Planning	59,704	62,228	45,024	(17,204)
Division of Data Processing				
Regular	551,816	549,536	798,075	248,539
Special:				
Charting Machine and Projection Equipment	62,500	2,500	65,305	62,805
Remote Computer Facility	-	-	25,000	25,000
Advanced Calculator	-	-	8,000	8,000
Employee Retirement and Insurance Benefits	839,460	1,232,602	955,817	(276,785)
Total Operating Budget	8,603,189	8,884,148	9,515,936	631,788
Construction and Alterations				
Annex Building	257,680	(3,989)	189,793	193,782
Main Building	8,625	53,894	105,000	51,106
Grand Total	\$8,869,494	\$8,934,053	\$9,810,729	\$ 876,676

1966 Budget
Summary of Account ClassificationsSchedule B
Page 1

Classification of Expenses	Positions Provided		Amount			Over (Under) 1965 Expenses
	1965 Budget	1966 Budget	1965		1966 Budget	
			Budget	Expenses (Estimated)		
PERSONAL SERVICES						
Salaries:						
Offices of Members of the Board	31	34	\$ 472,492	\$ 469,976	\$ 522,211	\$ 52,235
Office of the Secretary	50	51	381,134	376,373	406,252	29,879
Legal Division	31	33	290,798	289,364	335,965	46,601
Division of Research and Statistics	172	183	1,558,331	1,591,067	1,730,429	139,362
Division of International Finance	54	57	545,368	519,190	586,840	67,650
Division of Examinations	74	79	702,851	690,361	805,076	114,715
Division of Bank Operations	29	28	276,969	267,162	285,871	18,709
Division of Personnel Administration	30	30	186,754	187,854	200,823	12,969
Division of Administrative Services	145	153	706,064	701,089	741,028	39,939
Office of the Controller	12	12	104,382	101,624	109,485	7,861
Office of Defense Planning	3	2	50,504	50,463	33,574	(16,889)
Division of Data Processing	60	73	444,569	426,204	543,596	117,392
Total - Positions and Salaries	691	735	\$5,720,216	\$5,670,727	\$6,301,150	\$630,423
Fees			\$ 67,030	\$ 69,739	\$ 87,080	\$ 17,341
Retirement Contributions			789,625	1,182,296	901,815	(280,481)
Employee Insurance			49,045	49,198	52,894	3,696
Total Personal Services			\$6,625,916	\$6,971,960	\$7,342,939	\$370,979

1/ Includes 10 stenographic recruit positions.
2/ Includes Youth Opportunity Program; excludes Cafeteria salaries.

Classification of Expenses	1965		1966 Budget	Over (Under) 1965 Expenses
	Budget	Expenses (Estimated)		
NONPERSONAL SERVICES				
Traveling Expenses	\$ 321,409	\$ 326,473	\$ 352,783	\$ 26,310
Postage and Expressage	107,943	102,204	103,940	1,736
Telephone and Telegraph	101,829	113,030	114,321	1,291
Printing and Binding	395,074	375,818	425,234	49,416
Stationery and Supplies	72,181	82,636	86,553	3,917
Furniture and Equipment	126,137	63,279	148,580	85,301
Rentals	144,130	140,143	237,985	97,842
Books and Subscriptions	25,150	25,349	26,800	1,451
Heat, Light and Power	56,500	51,849	53,500	1,651
Repairs and Alterations (Building and Grounds)	52,029	35,337	40,236	4,899
Repairs and Maintenance (Furniture and Equipment)	27,372	26,384	31,101	4,717
Insurance	1,839	1,671	1,608	(63)
Contractual Professional Services	409,781	405,214	358,020	(47,194)
Consumer Finances Surveys	270,000	285,000	25,000	(260,000)
Consumer Credit Surveys	50,000	6,000	63,000	57,000
Banking Markets Surveys	15,000	5,000	175,000	170,000
Other Surveys	32,000	56,000	45,000	(11,000)
Security Clearance Investigations	13,260	19,870	18,450	(1,420)
Review of Examinations Procedures	13,000	13,000	13,000	-
Legal, Consultant and Other Services	11,246	16,894	37,995	(3,899)
Auditing Books of Board	2,500	2,500	2,500	-
Translating, Transcripts and Reporting Service	2,775	950	3,075	2,125
All Other	135,899	162,801	192,336	29,535
Cafeteria (net)	48,262	51,415	54,250	2,835
Special Statistical Services	39,600	61,703	79,500	17,797
CEMLA Membership Fee	18,000	18,000	27,000	9,000
Official Dinners, Receptions, etc.	5,450	6,941	7,470	529
Tuition and Registration	9,392	9,586	9,326	(260)
Meals for Official Guests	3,800	4,545	4,500	(45)
News Ticker Service	3,690	3,690	3,690	-
Miscellaneous	7,705	6,921	6,600	(321)
Total Nonpersonal Services	\$1,977,273	\$1,912,188	\$2,172,997	\$ 260,809
Total Personal Services	6,625,916	6,971,960	7,342,939	370,979
Total Operating Budget	8,603,189	8,884,148	9,515,936	631,788
Construction and Alterations	266,305	49,905	294,793	244,888
Grand Total	\$8,869,494	\$8,934,053	\$9,810,729	\$ 876,676

T E L E G R A M
LEASED WIRE SERVICEItem No. 17
12/15/65BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON

December 14, 1965.

Whitman - San Francisco
Swan - San Francisco

This refers letter of December 8, 1965, from Mr. Cooper, Assistant General Counsel of your Bank, regarding summons served upon Mr. Pascual, Assistant Federal Reserve Agent, to appear before Donald H. O'Hare, Special Agent of the Internal Revenue Service, in connection with tax proceeding against Antoine B. Rinieri to produce records relating to dates of issuance and recipient of certain designated fifty (50) and one hundred (100) dollar currencies.

It is understood that information requested is in records of office of Federal Reserve Agent and is desired to prove that bills in question were in this country at time when Mr. Rinieri claims they were in Switzerland. You are advised that pursuant to section 261.2(b) of its Rules of Organization, Board authorizes Mr. Pascual to appear and produce information requested and testify in connection therewith.

(Signed) Merritt Sherman

Sherman

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

Item No. 18
12/15/65

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

December 15, 1965

Mr. Leland M. Ross, Vice President,
Federal Reserve Bank of Chicago,
Chicago, Illinois. 60690

Dear Mr. Ross:

In accordance with the requests contained in your letters of December 8, 1965, the Board approves the appointments of William E. Ruddy and John P. Trinklein, at present assistant examiners, as examiners for the Federal Reserve Bank of Chicago, effective January 10, 1966.

Very truly yours,

(Signed) Elizabeth L. Carmichael

Elizabeth L. Carmichael,
Assistant Secretary.

