FR 609

Minutes for May 16, 1966

To: Members of the Board

From: Office of the Secretary

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

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

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

Chm. Martin _____

Gov. Robertson _____

Gov. Shepardson _____

Gov. Mitchell _____

Gov. Daane _____

Gov. Maisel _____

Gov. Brimmer _____

Minutes of the Board of Governors of the Federal Reserve System on Monday, May 16, 1966. The Board met in the Board Room at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Robertson, Vice Chairman
Mr. Shepardson
Mr. Mitchell
Mr. Maisel
Mr. Brimmer

Mr. Sherman, Secretary
Mr. Kenyon, Assistant Secretary
Mr. Holland, Adviser to the Board
Mr. Molony, Assistant to the Board
Mr. Cardon, Legislative Counsel
Mr. Fauver, Assistant to the Board
Mr. Solomon, Director, Division of Examinations
Mrs. Semia, Technical Assistant, Office of the Secretary
Miss Eaton, General Assistant, Office of the Secretary

Messrs. Brill, Koch, Partee, Axilrod, Gramley, Bernard, Eckert, Ettin, Fry, Keir, and Kelty, and Mrs. Peskin of the Division of Research and Statistics

Messrs. Sammons, Hersey, Katz, Reynolds, Baker, and Gemmill of the Division of International Finance

Money market review. Mr. Axilrod commented on the Government securities market and on bank credit trends, along with the projection of bank reserve aggregates shown in a distributed table on bank reserve utilization. Mr. Baker then discussed developments in foreign exchange markets and summarized recent figures on the U.S. balance of payments.

Members of the staff not concerned with the remaining items on the agenda then withdrew and the following entered the room:

Mr. Farrell, Director, Division of Bank Operations
Mr. Hexter, Associate General Counsel
Mr. O'Connell, Assistant General Counsel
Mr. Langham, Assistant Director, Division of Data Processing
Mrs. Heller and Mr. Sanders, Senior Attorneys, Legal Division
Messrs. Egertson, Supervisory Review Examiner, and Rumbarger, Review Examiner, Division of Examinations
Mr. Veenstra, Chief, Financial Statistics Section, Division of Data Processing

Bank supervisory matters. The following letters were approved unanimously after consideration of background information that had been made available to the Board. Copies are attached under the item numbers indicated.

	Item No.
Letter to Nassau Trust Company, Glen Cove, New York, approving the establishment of a branch in Greenvale.	1
Letter to Matinecock Bank, Locust Valley, New York, approving the establishment of a branch in Bayville.	2
Letter to Farmers and Merchants Trust Company of Chambersburg, Chambersburg, Pennsylvania, waiving the requirement of six months' notice of withdrawal from membership in the Federal Reserve System.	3

With respect to Item No. 3, in response to an inquiry from Governor Robertson, Mr. Solomon recalled that at one time the Board had been averse to waiving the requirement of six months' notice of withdrawal from System membership. In recent years, however, it had been the practice to waive the requirement almost automatically. In present circumstances, it seemed to him that reluctance to waive the requirement might only intensify the problem of withdrawals from membership.

Governor Brimmer spoke of making some studies of the membership problem and said he hoped that these studies would provide a basis for a thorough review by the Board in the near future. He assented to a request that he take account of the six-month notice question in connection with his studies.

Statistics on negotiable certificates. There had been distributed a memorandum dated May 12, 1966, from the Division of Research and Statistics recommending a revision of the current negotiable certificate of deposit maturity survey and continuation, at least until the end of September, of the current ad hoc survey of interest rates on such certificates. The circumstances underlying the need for more frequent and more comprehensive data were set out in the memorandum, as well as the specific changes contemplated.

After discussion the recommendations were approved unanimously. In light of a possibility that it might be necessary to have the related systems planning and computer programming done outside the Board on a contract basis, the Board also approved any resulting budget overexpenditure.

Application of Denver U.S. Bancorporation (Items 4-6). There had been distributed drafts of an order and statement reflecting approval by the Board on April 26, 1966, of the application of Denver U.S. Bancorporation, Inc., Denver, Colorado, to acquire shares of The Mercantile Bank and Trust Company, Boulder, Colorado. A dissenting statement by Governor Robertson also had been distributed.

The issuance of the order and statement was authorized. Copies of the documents, as issued, are attached as Items 4 and 5, and a copy of the dissenting statement is attached as Item No. 6.

Mrs. Heller and Messrs. Langham, Egertson, Rumbarger, and Veenstra then withdrew from the meeting.

Float (Item No. 7). In a letter of March 24, 1966, Chairman Dawson of the House Committee on Government Operations referred to recommendations in a report by the Committee entitled "Federal Reserve System--Check Clearance Float" and requested that the Board report to the Committee any actions taken or proposed to implement the recommendations. The recommendations were that the Board:

(1) Establish quantity and time goals for float elimination through technological developments, and, if such developments did not meet expectations, consider the advisability of adopting a plan for immediate charges and credits on checks or for time schedules that would approximate actual collection times.

(2) Develop records that would indicate the proportionate use member banks made of float as reserves so that, if efforts to reduce float fell short of expectations, a study could be made to determine whether charges should be assessed against banks in proportion to the benefits they derived from float.

(3) Coordinate the System's ADP equipment planning and acquisitions with the rest of the Government, as contemplated by Public Law 89-306.

The Committee's recommendations had been discussed at a joint meeting of the Board and the Presidents of the Federal Reserve Banks on May 10, 1966, along with policy implications of the Federal Reserve's

responsibility to expedite and extend the settlement mechanism and areas in which procedural improvements were being sought. Suggestions were made as to the approach to be taken in replying to Chairman Dawson.

A draft of reply to Chairman Dawson had now been distributed advising that the System had under way several studies directed, on a long-term basis, toward minimizing float and improving the payments mechanism; that some of the studies should yield results within a year or so, while others dealt with possible changes that would take longer to put into effect. The proposed reply would then mention several actions that already had been taken as part of the studies, and would express the consensus of the recent joint discussion between the Board and the Reserve Bank Presidents to the effect that further decisions with respect to possible steps to reduce float should proceed only after the development of information from the undertakings mentioned.

At today's meeting Governor Mitchell referred further to the avenues being explored in an effort to reduce float. It seemed to him advisable, pending the availability of better information as to the results that might be accomplished, to defer a comprehensive reply to Chairman Dawson. It had been the consensus of the Presidents, he thought, that a more specific response might be possible sometime later this year, although there were differences of opinion among the Presidents as to the degree of improvement that might be expected. It was Governor Mitchell's view that with firm leadership by the Board a great deal could

be accomplished within the course of a year or so. He suggested that at some point, perhaps in June, and after consultation with the Presidents, the Board might issue a press release describing the program of the Federal Reserve System for improving the check collection machinery. The commercial banking system would be interested in such a report and might be stimulated to search for ways of assisting the program.

Mr. Cardon raised a question as to whether such a press release would contain any significant information not given in the reply to Chairman Dawson now under consideration; if it did, the Board might be placed in an unfortunate light.

Governor Brimmer expressed the view that the reply to Chairman Dawson could be improved by including, at the minimum, an indication of the beginning date of the forthcoming System float survey and the date when it was anticipated that results would be available.

Governor Mitchell agreed that the beginning date for the survey could be specified, along with some of the changes in Reserve Bank operating procedures currently being evaluated. He suggested editorial changes to that end. He counseled, however, against attempting to be too precise at this stage about how much could be accomplished in terms of float reduction, and within what periods of time.

Governor Shepardson pointed out that whereas the Committee's third recommendation spoke of coordinating the System's ADP equipment planning and acquisition with the rest of the Government, the proposed

reply to Chairman Dawson would state that the Board had cooperated with other Government agencies in this respect and would continue this practice.

Staff comments indicated that although for a number of years the Board had cooperated with the Bureau of the Budget, General Services Administration, and other agencies in various studies concerning the use of data processing equipment, these endeavors had not crossed the point where the Board would be obligated to share its equipment with other agencies through outside control of assignment and use. Nor did the cooperation contemplate that the Board would relinquish the right to make its own decisions on equipment acquisition.

Mr. Farrell reverted to the proposed press statement and indicated that the intention was to include in it certain information, of types he described, that would not be in the letter to Chairman Dawson, whereupon Chairman Martin remarked that the point raised earlier by Mr. Cardon was well taken. If the press release was to contain information not included in the present letter, Chairman Dawson should be given that information before the press statement was issued.

After further discussion the letter to Chairman Dawson was approved unanimously in the form attached as Item No. 7.

Proposed legislation regarding certificates of deposit. In a letter of April 27, 1966, Chairman Patman of the House Committee on Banking and Currency requested the views of the Board in regard to

H.R. 14026, a bill to prohibit insured banks from issuing negotiable certificates of deposit and other similar negotiable instruments, and H.R. 14422, a bill to prohibit insured banks from issuing certificates in denominations of less than $15,000. The members of the Board also had been requested, in another letter, to testify during hearings on H.R. 14026 and related proposals.

A draft of report had been distributed, along with a staff paper reviewing the developing role of time deposits at commercial banks. A number of suggestions having been received, a revised draft reply dated May 15 was distributed. (Both drafts expressed the conclusion that the public interest would not be served by passage of either bill.)

Mr. Brill commented on the development of the alternative draft reply, which was narrower in scope and related more specifically to the two pending bills. He noted that a draft of possible statement for presentation at the hearings also had been prepared, coordinated with the proposed letter. He mentioned also that it had not been intended that the staff background paper would necessarily be transmitted to the Committee.

Governor Robertson raised the question whether both a letter report on the bills and testimony at the coming hearings seemed necessary. In the following exchange of comments it was suggested, among other things, that a letter might be prepared and presented at the hearings, but a decision as to the manner of response was held in abeyance pending discussion of the substantive issues.

Governor Shepardson commented that although he thought the proposed letter was appropriate as far as it went, it should be noted that the pending legislation had been proposed because members of Congress were concerned about what they regarded as a potentially dangerous shifting of funds. It was possible, when the findings of the current survey of interest rates paid on time deposits were available, that the Board might find disturbing elements in the situation. Therefore, it might be well to consider whether the Board should firmly oppose the two bills without suggesting alternative remedial measures to cope with any serious problem that might develop.

Governor Robertson stated that he believed the response should be confined essentially to two issues, namely, whether or not the issuance of negotiable certificates of deposit should be prohibited simply because of the feature of negotiability and whether or not there was any basis to justify discrimination between large and small savers. On the first issue he believed all of the Board members certainly would stand together. The second issue was more delicate. The letter could then go on to refer to the survey now in progress to develop current information regarding banking practices and to place the Board in a better position to determine whether any action was needed. He believed it would be proper to say that while the Board did not favor the pending bills and believed that its powers under existing law were adequate, if any legislation was called for it should be in the direction of increasing

the flexibility of the Board's powers so as to permit prescribing different maximum permissible rates of interest on any basis deemed appropriate by the Board.

Governor Brimmer commented that, since such a host of issues was involved, he thought it would be helpful to have further discussion in executive session. He believed that the transmittal of any report ought to be postponed until it was possible to achieve a better meeting of the minds on the general approach that the Board should take.

It was understood that Governor Brimmer's procedural suggestion would be followed.

Mr. Brill brought up a related question, namely, that there appeared to be limitations on the use that could be made of information regarding certificate of deposit rates that had been gathered by the Federal Reserve Bank of New York because of commitments made in requesting the data.

Discussion disclosed a consensus that it would be desirable for the Board to be able to use such information as freely as possible. It was understood that the staff would be in touch with the New York Reserve Bank with a view to seeking an understanding that would permit the widest possible latitude in the use of the data.

Messrs. Axilrod, Eckert, and Ettin then withdrew from the meeting.

Compounding of interest. Pursuant to the procedure agreed upon at the meeting on March 30, 1966, the Board requested the views of the

Comptroller of the Currency and the Federal Deposit Insurance Corporation regarding a proposed amendment to the Supplement to Regulation Q, Payment of Interest on Deposits, that would permit member banks to pay interest at the maximum permissible rate compounded on any basis a member bank might desire to adopt, and would require member banks to state the basis of compounding in every advertisement, announcement, solicitation, and agreement relating to the rate of interest paid. No response to the Board's request had been received from the Comptroller of the Currency, and it had been ascertained that none would be forthcoming. The Federal Deposit Insurance Corporation had questioned the advisability of the amendment, at least in the present circumstances.

Governor Robertson referred to the earlier discussion of this matter at the meeting on May 11 and stated that the principal purpose of bringing the matter up at this time was to determine whether the Board agreed that this item should be discussed with directors of the Corporation, and there was agreement that such a procedure would be appropriate.

Regulations Q and D (definition of deposit). On a number of occasions, most recently on March 29, 1966, the Board had discussed proposals to adopt a definition of "deposit" for purposes of Regulation Q (Payment of Interest on Deposits) and Regulation D (Reserves of Member Banks) that would bring within the scope of that term promissory notes and other forms of indebtedness of member banks, with certain

exceptions. Two successive versions of the proposed definition were published for comment, and there had now been distributed a memorandum dated May 10, 1966, in which the Legal Division summarized the comments received in response to the second publication, analyzed the suggested modifications of the Board's revised proposal, and made recommendations with respect thereto on the assumption that the Board wished to adhere to the general approach of its proposal. The memorandum also commented on the "specific" promissory note approach suggested by the New York Clearing House.

The memorandum noted, among other things, that the definition provided an exemption for indebtedness arising from a transfer of direct obligations of the United States that a bank was obligated to repurchase. Several parties had suggested expansion of the exemption to cover repurchase agreements on Federal agency obligations (others suggested even further expansion). The Legal Division, for reasons stated, recommended against such an expansion.

As to other suggested revisions of the definition, the Legal Division recommended that the exemption for Federal funds transactions be expanded to cover all one-day loans in such funds that arose out of a sale of securities on the same day; that the Board not exclude longer-term unsubordinated promissory notes from the definition of deposits; that the requirement for subordination to the claims of general creditors be eliminated; that the footnote relating to the meaning of "indebtedness"

be changed to exclude from consideration as an indebtedness for purposes of the definition of "deposit" an obligation to deliver foreign exchange sold and a liability such as arises from a foreign exchange swap transaction; and that there be eliminated the requirement under which, for an indebtedness to be covered by the exemption for interbank indebtedness, it must not be reflected on books or reports of the creditor as a bank balance.

The memorandum noted that both the Federal Deposit Insurance Corporation and the New York Clearing House had pointed out that the major purpose of the 1960 amendments to the Federal Deposit Insurance Act was to provide a simpler method of determining assessments for deposit insurance. Adoption by the Board of its proposed definition would reinstate the necessity for verifying "deposits" on a dual basis.

The Clearing House had suggested a "specific" definition of promissory notes as deposits, and had revised it somewhat after a meeting between Clearing House representatives and the Board. An alternative "specific" approach suggested by Mr. Hackley had also been circulated to the Board. The May 10 memorandum from the Legal Division expressed the view that only a comprehensive definition, as modified in accordance with recommendations in the memorandum, resolved each of the known problems, and it was as capable of appropriate interpretation as the alternatives in the event unforeseen problems should arise. Accordingly, it was recommended that the Board adhere to the comprehensive approach.

Attached was a draft of definition consistent with the conclusions of the memorandum. The Legal Division recommended that the Board use this definition as a basis for consultation with the Federal Deposit Insurance Corporation.

At the beginning of today's discussion Governor Maisel remarked that before consulting with the Federal Deposit Insurance Corporation it would be well for the Board to arrive at a policy position.

Governor Mitchell then commented that what had begun as a relatively clean-cut proposal had become so complicated that he thought it would involve the Board in many technical problems. If it was necessary to take action today, he would be inclined to discard the proposal; failing that, he would prefer the Clearing House approach.

Governor Shepardson agreed that many problems were raised and said he was not sure to what extent the current proposal would meet them. If the Board was going to move ahead with the comprehensive approach, the Legal Division's recommendations seemed appropriate. However, administrative complications seemed likely, and he always had been averse to regulations that were difficult to interpret and enforce.

Mr. Hexter observed that the Board initially had undertaken to explore the matter because of a tendency of banks to move to new mechanisms for obtaining funds in ways that were out of reach of the present regulations. Withdrawal from this effort would seem to indicate that the Board had no objection. Enforcement of the prohibition against

payment of interest on demand deposits would, of course, give rise to questions of interpretation. If the Board did not adopt a definition of the kind in question, those difficulties could be avoided, to be sure, but at the cost of not dealing with the problem that had already arisen.

Governor Maisel said his feeling from the start had been that the loophole was limited and could be dealt with if the promissory notes were defined as borrowing instruments, because then they would be covered by the statutory limitation on a bank's borrowings in relation to its capital. It seemed to him that the Comptroller of the Currency, in his letter of comment of February 23, 1966, had given some indication of willingness to adopt such a position; if so, a solution of the problem might be available.

The staff expressed doubt that the Comptroller's comments were to be so interpreted. However, Governor Maisel suggested that the letter might be given further study.

Governor Mitchell stated that he also would prefer to treat promissory notes as borrowings, because then the device would be self-limiting. As a second choice, he would take the approach suggested by the New York Clearing House and deal with evasions if and when they developed.

Governor Brimmer said that he likewise favored the narrower approach. In his review of background material, including the minutes

of a meeting of the Board with the Presidents of the Federal Reserve Banks on January 11, 1966, he had detected what seemed to be a rather general feeling on the part of the Presidents that the focus should be rather narrowly on promissory notes, with a definition somewhat like that suggested by the New York Clearing House. If it was possible to get agreement by the Comptroller of the Currency to treat such funds as borrowings, he would support such an approach; if not, he would favor limiting the deposit definition.

Governor Robertson said that he was discouraged. This was a problem on which the Board had worked for months, and now that the time to act appeared to have arrived, there seemed to be a disposition to back down. It was his firm view that there had been no change whatsoever in the Comptroller's attitude. He believed it was absolutely wrong to condone the practice of buying money for short periods, outside the scope of the Board's regulations, merely by changing the name of the instrument; it had been recognized from the beginning that the practice constituted a violation of the prohibition against payment of interest on demand deposits. The staff had done an excellent job in adapting the proposed definition to meet as many of the complaints as possible, and had produced a formula that should be palatable. It seemed to him, therefore, that the only proper way to move was forward, by adopting the definition. If difficulties developed, corrective action could be taken, but adoption of the definition would not create problems of the magnitude of those created by refusing to act.

Governor Brimmer noted that it was still proposed to cover within the definition repurchase agreements involving Federal agency securities. It seemed to him that casting the net so widely tended to invite evasions.

Governor Robertson replied that a concession had been made in exempting repurchase agreements on direct Government obligations, the use of which was already woven into the fabric of the Government securities market. But widening the exemption to include repurchase agreements on agency securities would merely set the stage for use of this evasive device. The inclusion of the latter within the definition would not be disruptive of established market practices. Altogether, in view of the extended discussions that had occurred, and in view of the revisions of the proposed definition that had been recommended to meet objections, he believed that abandonment of the project now would be most unfortunate.

Governor Maisel commented that while Governor Robertson and others believed that a repurchase agreement created a deposit, he had never thought that this was a proper concept. Accordingly, he did not agree that the exemption provided for repurchase agreements in connection with sales of Government securities represented an exception, nor would he regard as an exception the addition of exemptions for repurchase agreements on agency securities or on municipals.

As for the argument that the Board would be in a poor posture if it abandoned the proposal, Governor Maisel said he had expressed

misgivings about publishing the proposal in the Federal Register for comment but had been assured that the purpose of publication was to send up a trial balloon and that it carried no commitment for final action.

Mr. Hexter observed that publication of a proposal for comment indicated an intent, recognizing that the comments received might lead to withdrawal of the proposal.

Governor Maisel replied that it seemed to him the comments received in this instance indicated that it would be proper to withdraw the proposed definition of deposit.

Governor Robertson then asked if Governor Maisel's objection to the definition in its present form was based primarily on the lack of an exemption for repurchase agreements covering agency securities.

Governor Maisel replied in the negative, indicating that his objections were more broadly based.

Governor Robertson next asked Governor Brimmer the same question, and the latter also responded in the negative. He did not like to see the Board pursue a policy of disrupting broad market practices that were reasonably well established. Nor was he happy with the assumption, which he thought was implicit in the memorandum, that market participants could be expected to change their practices without difficulty. The Board had set out to deal with the issuance of promissory notes by banks as a means of attracting funds. It seemed to him that in the course of the discussions the issue had escalated, largely on the basis of legal points.

Mr. Hexter observed that the matter of basic concern was to enforce the law. The prohibition in the law against payment of interest on demand deposits was strongly worded. Congress had said that no member bank should, directly or indirectly, by any device whatsoever, pay any interest on any deposit that was payable on demand, and had gone on to say that the Board should define the term "deposit" in order to prevent evasions.

Governor Brimmer reiterated the view that the Board should only adopt language specifically directed toward promissory notes; if banks should then turn to different forms of instruments to accomplish the same purpose, appropriate attention could be given to such a development.

Governor Shepardson remarked that when promissory notes were first issued they had not seemed to constitute a problem of significant magnitude, and the Board had adopted a "wait and see" attitude. Now, however, the practice had developed into a significant evasion. It seemed to him the staff had made a persuasive argument that repurchase agreements, for example, could provide an alternative avenue for evasion. He thought it was always better to foreclose such a possibility before the practice became established. He did not believe that one avoided trouble by leaving loopholes and then trying to close them later.

Governor Mitchell expressed the view that by defining deposits broadly the Board would be marking off a larger area than necessary to

deal with the original problem, and thus might be precluding the development of new practices that would be helpful to the market. He thought markets developed better when there was a little elbowroom, with corrective actions taken only as needed.

Chairman Martin then observed that the Board seemed sufficiently divided that it would be best not to push forward on this matter at the present time. He agreed with Governor Robertson that the Board's posture was not good. Discussion with the Federal Deposit Insurance Corporation might possibly result in some mutually agreeable position, but at this stage it did not appear feasible for the Board to try to take any formal step.

Accordingly, the matter was tabled.

Exchange of information with Regional Comptrollers (Item No. 8). The Board had had several discussions, most recently on March 17, 1966, regarding exchange of information between Regional Comptrollers of the Currency and the Federal Reserve Banks, and there had been an exchange of correspondence with the Comptroller on that subject.

In a letter of March 3, 1966, the Comptroller stated that "in the event our Regional Comptrollers should obtain any information which, in their judgment, would be of interest to the Federal Reserve System, they will relay such information to the appropriate Federal Reserve Bank. We assume, of course, that your various Federal Reserve Banks will be instructed to reciprocate by similarly informing our Regional Comptrollers

concerning all State Member Banks." At the March 17 meeting the Board considered a draft of reply to the Comptroller. A revised draft had now been distributed.

Mr. Solomon recalled that the Board, at the conclusion of the March 17 discussion, had decided to ask the Federal Reserve Banks to try to work out guidelines with the Regional Comptrollers for exchange of information. However, it appeared probable that such efforts would be unavailing, as they had been in the past, in the absence of support from Washington. The present draft of reply to the Comptroller was for the purpose of making a record that would give the Reserve Banks as firm a ground as possible for negotiating with the Regional Comptrollers.

There being agreement with suggestions for revised language at one point in the letter for the purpose of clarification, the letter was approved unanimously in the form attached as Item No. 8.

Messrs. O'Connell, Sammons, and Sanders then withdrew from the meeting and Miss Hart, Senior Attorney, and Mr. Shuter, Attorney, of the Legal Division entered the room.

Margin regulations. On May 9, 1966, during a discussion of stock market credit, the Board expressed itself in favor of moving forward with regulation of "purpose" credit (loans for the purpose of purchasing, carrying, or trading in securities) by lenders who were not covered by the existing regulations relating to stock market credit (Regulations T and U). The Board also expressed a desire to give early consideration

to proposals that would close previously-discussed loopholes in Regulations T and U, and a memorandum dated May 13, 1966, from the Division of Research and Statistics suggesting measures for that purpose had now been distributed.

In February 1965, pursuant to action by the Board on January 26, a preliminary draft of Regulation X, applicable to "purpose" lenders not subject to Regulations T and U, had been sent to the Federal Reserve Banks, the Securities and Exchange Commission, and the Commissioner of Internal Revenue for comment. There had now been distributed a memorandum dated May 12, 1966, from the Legal Division summarizing the comments received, attaching a second draft of regulation revised in the light of those comments, and discussing problems that seemed likely to be encountered.

The memorandum pointed out also that the Board's authority to issue such a regulation might be challenged. The Board had authority under section 7(d) of the Securities Exchange Act of 1934 to regulate purpose loans by persons other than brokers and dealers "to prevent the excessive use of credit for the purchasing or carrying of or trading in securities in circumvention of the other provisions of this section." (In 1963 the Securities and Exchange Commission had recommended that the Board exercise this authority.) The draft regulation attempted to cover this area in as broad a way as seemed practical, by subjecting to margin requirements every purpose loan made in the ordinary course of

the lender's business that was secured to any extent by a registered security, unless specifically exempted by the Act. In an attempt to meet a problem that had caused concern to the New York Reserve Bank, the draft also forbade "lenders" to make unsecured loans to brokers or dealers. A very broad definition had been given to what was in the "ordinary course" of a person's business. It had been argued in the past that those words limited the Board's authority to regulate loans by persons engaged in the business of lending or even to loans by persons engaged in the business of purpose lending. However, so-called "factors," who entered the purpose-lending field principally when margins and market activity were high, had argued that they were not subject to a provision of Regulation U that applied to persons engaged "principally, or as one of the person's important activities" in purpose lending. Moreover, loans had been made on an unsecured basis to brokers and dealers by corporations with temporarily idle funds and by tax-exempt organizations, foreign banks, and others. The Legal Division believed that a legally supportable argument could be made that all these loans were in the ordinary course of the lender's business.

The Legal Division's memorandum also discussed questions relating to the degree of restriction the Board might wish to impose. In general, the draft attempted to achieve a reasonable balance with Regulations T and U on the premise that persons similarly situated should receive equal treatment. However, it was not always possible to do this. One important

difference between Regulations X and U was that loans would not be covered by the former unless the collateral included some registered security, whereas Regulation U covered purpose loans secured by any stock, including unregistered stock.

Provisions permitting transfers of loans and permitting special subscription accounts were included in the first draft of Regulation X in accordance with the principle of putting lenders, so far as possible, on an equal basis with banks and broker-dealers. However, the New York Reserve Bank had strongly suggested deleting those sections on the ground that they would be difficult or impossible to administer.

The draft would explicitly permit same-day substitutions to be made in respect to collateral held by lenders. This privilege existed under Regulation T by virtue of the technical rules governing the "general account," and under Regulation U by interpretation. Inclusion in Regulation X of the proposed language relating to this point would avoid the necessity for a similar interpretation. If the Board wished to withhold the same-day substitution privilege under Regulation X, explicit language to that effect should probably be included in the regulation.

The memorandum stated that if the Board decided to publish a draft of Regulation X for comment, the staff would appreciate guidance as to whether the draft should include a same-day substitution privilege, permit transfers of regulated loans, and include a provision for the exercise of rights comparable to that included in Regulations T and U (special subscription account).

During introductory comments Miss Hart noted that the major question on which the staff would like to know the Board's views was the degree of restrictiveness desired: were the lenders to be treated on the same basis as banks and broker-dealers, or were they, through a really restrictive approach, to be induced to stop making purpose loans? If they did not stop, it was possible that much greater loopholes would develop under Regulation X than had developed under Regulations T and U, and therefore she advocated the restrictive approach.

Chairman Martin expressed a preference for a restrictive approach, but the possibility of court tests gave him pause. The regulation as drafted seemed to him generally appropriate, but he suggested that members of the Board's staff visit New York to discuss the matter in detail with staff of the New York Reserve Bank and perhaps also with knowledgeable parties outside the Bank.

On the question of challenge of the Board's authority, it was observed that there could be no guarantee that a court test would not be sought; the lenders to whom Regulation X would apply might seek an injunction. Neither was it possible to predict what attitude a court might take, but it was the legal staff's opinion that the proposed regulation did not exceed the Board's powers.

Chairman Martin reiterated the view that before the draft regulation was published for comment it would be desirable to consult with people who were close to the market's operations.

Mention was made of the difficulty in identifying lenders who would be subject to the regulation, and it was noted that upon publication in the Federal Register there would be an opportunity for all interested parties to submit comments. However, as in the case of the promissory note matter, questions might be raised if the Board published a notice of proposed rule making and then failed to take action.

In response to a suggestion by Governor Robertson that consultations with the New York Reserve Bank, but not with others, precede publication for comment, there was a discussion of the extent to which the present draft of regulation reflected the views of that Bank, and of further revisions that might be made in the direction of recommendations of the Bank's legal staff.

Mr. Partee referred to the three provisions specially mentioned in the Legal Division's memorandum, omission of which from Regulation X would make it more restrictive than Regulations T and U. It seemed to him that there might be fairly general acceptance of an approach in which the Board would regulate factors and other lenders on the same terms as banks and brokers, but he wondered if it would be regarded as reasonable to regulate them more strictly.

Miss Hart mentioned the exceptions taken by the New York Reserve Bank to inclusion of those privileges, and Chairman Martin remarked that this illustrated the importance of arriving at a complete agreement with the New York Reserve Bank--in fact, with all of the Reserve Banks--if possible.

During further discussion of procedures it was brought out that although the desirability of consultation with presently unregulated lenders about a measure inimical to their interests might be debatable, there were other elements of the financial community, such as the New York Stock Exchange, whose views might be helpful.

At the conclusion of the discussion it was understood that the staff would proceed with consultations with the New York Reserve Bank and with other parties to the extent deemed advisable, following which the question of the draft regulation would be resubmitted to the Board.

The discussion then turned to the memorandum in which the Division of Research and Statistics suggested means of closing loopholes in Regulations T and U.

The first question related to loans to purchase or carry listed convertible bonds. Under Regulation T such loans by brokers were subject to the same margin requirements as stocks, but commercial bank loans for the same purpose fell outside Regulation U and carried only the maintenance margins of 20 to 30 per cent required by the banks themselves. The memorandum described three alternative ways in which the treatment of such loans might be made more nearly parallel under both regulations.

Members of the Board expressed a preference for the alternative favored by the staff that would amend Regulation U by making margin requirements on bank loans to purchase or carry listed convertible bonds the same as those on stocks.

The memorandum also described reasons why it was considered desirable to reduce the liberality of the subscription account privilege in both regulations, and listed three possible alternative actions for that purpose.

Discussion of this point disclosed some sentiment in favor of the alternative of limiting the subscription account privilege to stockholders of record at the time a rights offering was announced. (However, it was brought out that such a provision had been in effect in the past, and had been abandoned because it appeared to be adverse to the flotation of equity securities.)

No views were expressed by members of the Board at this stage in regard to the other points in the memorandum, relating to extension of margin regulation to over-the-counter markets and modification of the same-day substitution privilege.

All members of the staff except Messrs. Sherman, Kenyon, Holland, and Brill then withdrew from the meeting.

Proposed legislation regarding certificates of deposit. Discussion continued of the position to be taken with respect to the bills relating to certificates of deposit that were now pending before the House Banking and Currency Committee.

Governor Mitchell suggested that the Board's spokesman say, in essence, that at the present time the Board did not have any recommendations for changes in the law, that the Board did not think any action

was indicated at this time, that the matter was under continuing study, however, and that if at some future time the Board saw a need for legislation or for action to be taken under existing legislation, appropriate steps would be taken. Within that framework, he suggested, the Board could discuss with the Committee the various issues involved; this was a minimum framework for exploration of any differences of opinion.

Governor Maisel said that he thought there were several fundamental questions. One was whether the Board was concerned about the intensity of competition between banks and other financial institutions at this point. A related question was whether the Board saw a need for additional legislation and, if such legislation was provided, whether the Board would be prepared to take action under it. Another question was whether certain markets should be insulated, in one form or another, from the impact of general monetary policy. If so, a further question was whether legislation should be sought in this regard.

Governor Robertson commented that the Secretary of the Treasury had called a meeting of the interagency Coordinating Committee on Bank Regulation for Thursday afternoon. He supposed that the purpose might be to raise the question of what should be done to make it possible for the Federal Reserve to come to the assistance of the Home Loan Bank System in the event of need. As to the Banking and Currency Committee hearings, he would not be disposed to take a position that there was need for any particular action at this particular time. Even if individual members felt there was a need to take action, the Committee was

not the proper forum for expression of such views. Instead, the position should be that the Board was watching the situation carefully, that it was making a survey, that it should be able to deal with any emerging problems under existing statutory authority, but that, if necessary, it would recommend additional legislation. Beyond that, he would want to avoid expressing any views until the Board had hammered out its own policy.

Chairman Martin expressed agreement with the view that differences should be minimized when appearing before the Banking and Currency Committee and suggested that as much as possible should be done in advance to arrive at a Board position on the various issues. He agreed with a comment by Governor Shepardson that the approach outlined by Governor Robertson seemed generally appropriate.

There followed a brief discussion of the possibilities for action under existing legislation, after which attention was directed to the draft of proposed letter on the two pending bills and a number of suggestions were made by members of the Board. It appeared from the suggestions that the letter would have to be couched in rather general terms, since there were differences of opinion on specific issues.

Governor Maisel then turned to the problem that might be posed for commercial banks around midyear in rolling over the substantial volume of maturing negotiable certificates. He suggested that work be done by the staff to appraise the dimensions of the problem, in which

connection he observed that this would be a subject appropriate for consideration by the Open Market Committee at its next meeting.

Governor Maisel referred next to the Coordinating Committee meeting Thursday afternoon and inquired when the Board had in mind a discussion of the issue that Governor Robertson had indicated was likely to be raised. He brought out that the problem, in its broader dimensions, involved the marketing of Federal agency debt instruments, thus raising the question whether the Federal Reserve had any responsibility for a more efficient market in such issues. He referred to the possibility of a disorderly market if the various agencies needed substantial amounts of cash, the possibility of assisting the agencies through providing a better market for their issues in some manner, and the question whether the agency issues should be selling at rate levels much above those for U.S. Government obligations. He saw a need for the Board to reach basic policy decisions on these matters.

After some discussion of these points, Chairman Martin commented that they were quite appropriate for consideration but that they implied reconstituting the entire market structure.

In reply to a question by Governor Robertson, Mr. Holland reviewed preliminary staff thinking on the matter of amending the Treasury's direct borrowing authority from the Federal Reserve to provide funds with which to assist the Home Loan Bank System, and he described a type of amendment that seemed to the staff preferable to other possibilities.

Governor Brimmer commented that he felt this was the sort of thing to be kept in reserve and that he doubted whether the Board should take any position publicly at this point.

Chairman Martin expressed the view that the Board should take its lead from the Treasury. If the Board were to express any position, it might well be misinterpreted. If the Treasury advocated some measure, the Board would of course have to indicate whether it agreed or not.

Chairman Martin then said that there appeared to be no need, in view of the discussion today and the suggestions made by members of the Board, to bring back to the Board another draft of the letter to Chairman Patman regarding the two pending bills. Accordingly, it was understood that the letter was authorized for transmittal in a form reflecting the various suggestions that had been agreed upon. It was also understood that the statement to be presented to the Committee by the Vice Chairman, on behalf of the Board, would be redrafted to harmonize with the revised form of letter.

Foreign travel. The Board authorized Ruth Logue, Economist in the Division of International Finance, to visit the Netherlands Bank and the National Bank of Belgium for consultation in connection with the current study of the discount mechanism, with the understanding that Miss Logue would make these visits in the course of a forthcoming personal trip to Europe, that the total duration of her official travel would be about five days, that the Board would pay the additional transportation cost

involved in the visits, and that she would receive per diem in accordance with the Standardized Government Travel Regulations while on official business.

The meeting then adjourned.

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

Letter to the Civil Service Commission advising that the Board had designated Merritt Sherman, Secretary of the Board, to serve as Equal Employment Opportunity Officer.

Memorandum from the Division of Administrative Services dated May 12, 1966, recommending that an order be placed with Westinghouse Corporation for certain repair work on the C Street elevators in the Federal Reserve Building at a cost of $5,880 and requesting authorization for any resulting budget overexpenditure.

Memorandum (copy attached as Item No. 9) from the Division of Examinations and the Office of the Controller dated May 11, 1966, relating to reimbursement of travel expenses incurred by Reserve Bank employees borrowed to assist the Board's examining staff.

Memorandum from Mr. Holland, Adviser to the Board, dated May 13, 1966, recommending, in connection with the current study of the discount mechanism, that Bernard Shull be designated as Director of Research Projects; that Priscilla Ormsby be designated to succeed Mr. Shull as Secretary of the Secretariat; that appropriate provisions be made, as needed, to borrow personnel from the Reserve Banks on a rotating basis; and that full-time secretarial assistance be provided for Mr. Shull through the establishment, if necessary, of an additional secretarial or clerk-typist position at Grade FR-5 in the Division of Research and Statistics.

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

Appointment

Rowena A. L. Lipscomb as Statistical Clerk, Division of Research and Statistics, with basic annual salary at the rate of $4,641, effective the date of entrance upon duty.

Salary increase

William R. Howell, Supply Clerk, Division of Administrative Services, from $3,507 to $3,814 per annum, effective May 22, 1966.

Secretary

1716

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

Item No. 1
5/16/66

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

May 16, 1966

Board of Directors,
Nassau Trust Company,
Glen Cove, New York.

Gentlemen:

The Board of Governors of the Federal Reserve System approves the establishment by Nassau Trust Company, Glen Cove, New York, of a branch on the north side of Northern Boulevard approximately 120 feet west of the intersection of Glen Cove Road and Northern Boulevard, Greenvale (unincorporated area), Town of North Hempstead, Nassau County, New York, provided the branch is established within one year from the date of this letter.

Very truly yours,

(Signed) Karl E. Bakke

Karl E. Bakke,
Assistant Secretary.

(The letter to the Reserve Bank stated that the Board also had approved a six-month extension of the period allowed to establish the branch; and that if an extension should be requested, the procedure prescribed in the Board's letter of November 9, 1962 (S-1846), should be followed.)

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

Item No. 2
5/16/66

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

May 16, 1966

Board of Directors,
Matinecock Bank,
Locust Valley, New York.

Gentlemen:

The Board of Governors of the Federal Reserve System approves the establishment by Matinecock Bank, Locust Valley, New York, of a branch at the southwest corner of Perry and Bayville Avenues, Bayville, New York, provided the branch is established within six months from the date of this letter.

Very truly yours,

(Signed) Karl E. Bakke

Karl E. Bakke,
Assistant Secretary.

(The letter to the Reserve Bank stated that the Board also had approved a six-month extension of the period allowed to establish the branch; and that if an extension should be requested, the procedure prescribed in the Board's letter of November 9, 1962 (S-1846), should be followed.)

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

1718
Item No. 3
5/16/66

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

May 16, 1966

Board of Directors,
Farmers and Merchants Trust
Company of Chambersburg,
Chambersburg, Pennsylvania.

Gentlemen:

The Federal Reserve Bank of Philadelphia has forwarded to the Board of Governors a letter dated May 6, 1966, signed by President J. Glenn Benedict, together with the accompanying resolution, signifying your intention to withdraw from membership in the Federal Reserve System and requesting waiver of the six months' notice of such withdrawal.

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

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

Very truly yours,

(Signed) Karl E. Bakke

Karl E. Bakke,
Assistant Secretary.

Item No. 4
5/16/66

UNITED STATES OF AMERICA

BEFORE THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

WASHINGTON, D. C.

In the Matter of the Application of DENVER U. S. BANCORPORATION, INC., Denver, Colorado, for approval of the acquisition of voting shares of The Mercantile Bank and Trust Company, Boulder, Colorado.	DOCKET NO. BHC-73

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 Denver U. S. Bancorporation, Inc., Denver, Colorado, a registered bank holding company, for the Board's prior approval of the acquisition of 50 per cent or more of the outstanding voting shares of The Mercantile Bank and Trust Company, Boulder, Colorado.

In accordance with section 3(b) of the Act, the Board gave written notice to the State Bank Commissioner of Colorado of receipt of the application and requested his views and recommendation thereon. The Comptroller of the Currency and the Antitrust Division of the Department of Justice were notified of receipt of the application. None of the

aforementioned governmental authorities disapproved the application in writing within 30 days of notice of the application. At a later date, however, the State Bank Commissioner, on behalf of himself and the Colorado State Banking Board, opposed the application. The notice of the filing of the application, published in the Federal Register of July 22, 1965 (30 Federal Register 9189), included a statement that comments and views regarding the proposed acquisition could be filed with the Board within 30 days thereafter. By letter dated August 17, 1965, the president of The First National Bank of Denver commented adversely on the proposal. By letter dated August 18, 1965, The Central Bank and Trust Company, Denver, Colorado, submitted to the Board an opposition to the proposal and requested an opportunity to participate in a hearing on the matter. On September 9, 1965, at the discretion of the Board and in accordance with the provisions of section 222.7(a) of the Board's Regulation Y (12 CFR 222.7(a)), the Board ordered a public hearing in connection with the application. Said Order was published in the Federal Register on September 16, 1965 (30 Federal Register 11887). A public hearing was held in Denver, Colorado, on October 19-22, 1965, before a duly selected Hearing Examiner. Appearances at the hearing were made on behalf of Applicant as proponent; The Central Bank and Trust Company and the Colorado State Banking Board and Bank Commissioner as opponents; and counsel for the Board of Governors in a nonadversary capacity. After the hearing, proposed findings of fact, conclusions of law, and briefs were submitted by the aforesaid adversary parties. On March 4, 1966,

the Hearing Examiner filed with the Board a Report and Recommended Decision, recommending approval of the application. The opposing bank filed exceptions to the Hearing Examiner's Report and Recommended Decision, together with a supporting brief and a request for oral argument before the Board. Applicant responded with a brief in opposition to the opposing bank's exceptions and request for oral argument. The Colorado State Banking Board and Commissioner filed no exceptions but requested that their abstention be construed, not as agreement with the Hearing Examiner's conclusions, but rather as a reliance upon the record itself. All of the aforementioned documents were received as part of the record and have been considered by the Board.

IT IS HEREBY ORDERED, for the reasons set forth in the Board's Statement of this date, that the request for oral argument be and hereby is denied; and that said application for acquisition 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.

Dated at Washington, D. C., this 16th day of May, 1966.

By order of the Board of Governors.

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

Voting against this action: Governor Robertson.

Absent and not voting: Chairman Martin and Governor Brimmer.

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.

(SEAL)

Item No. 5
5/16/66

BOARD OF GOVERNORS

OF THE

FEDERAL RESERVE SYSTEM

APPLICATION BY DENVER U. S. BANCORPORATION, INC., DENVER, COLORADO, FOR APPROVAL OF ACQUISITION OF VOTING SHARES OF THE MERCANTILE BANK AND TRUST COMPANY, BOULDER, COLORADO

STATEMENT

Denver U. S. Bancorporation, Inc., Denver, Colorado ("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 Act"), an application for approval of the acquisition of 50 per cent or more of the outstanding voting shares of The Mercantile Bank and Trust Company, Boulder, Colorado ("Mercantile").

Views and recommendation of supervisory authority. - As required by section 3(b) of the Act, notice of receipt of the application was given to, and views and recommendation requested of, the Colorado State Bank Commissioner. Notice of receipt of the application was transmitted in writing to the Comptroller of the Currency and to the United States Department of Justice, and was published in the Federal Register on July 22, 1965 (30 Federal Register 9189). None of the aforementioned governmental authorities disapproved the application in writing within 30 days of notice of the application. Subsequently, however, the State Bank Commissioner, on behalf of himself and the State Banking Board, opposed the application on the grounds

that the formation and extension of bank holding company systems are devices aimed at circumvention of the State's anti-branch banking policy.

As observed by the Hearing Examiner, the argument presented by the State banking authorities in opposition to the proposal is substantially the same argument that was made to, and rejected by, the Board in the proceedings that resulted in the formation of Applicant (49 Federal Reserve Bulletin 1518) and those involving the application of First Colorado Bankshares, Inc., to acquire Security National Bank, Denver (49 Federal Reserve Bulletin 1646, 1651). The Board is of the view that, for the reasons stated in its earlier statements relative to this argument, proposed holding company formations, operations, and acquisitions are not to be subjected to statutory limitations that may be imposed on branch banking. For the same reasons, the Board is unable to accept the rationale urged by the Colorado State banking authorities in this case.

Public hearing. - Following expiration of the period allowed in the published notice for receipt of comments on Applicant's proposal, the Board ordered a public hearing to be conducted in Denver before a Hearing Examiner selected for the purpose by the United States Civil Service Commission. This hearing was not required by law, but was ordered by the Board pursuant to the provisions of section 222.7(a) of the Board's Regulation Y (12 CFR 222.7(a)), upon the Board's finding that such hearing would be in the public interest.

Participants in the hearing were the Applicant as proponent; The Central Bank and Trust Company, Denver, Colorado ("Central"), and the State Bank Commissioner on behalf of himself and the State Banking Board as opponents; and counsel for the Board of Governors in a non-adversary capacity. The adversary parties presented evidence, and all parties were afforded full opportunity for cross-examination of persons appearing as witnesses. Subsequent to the hearing, the parties were afforded the opportunity to file, and the adversary parties did file, proposed findings of fact, conclusions of law, and supporting briefs.

On March 4, 1966, the Report and Recommended Decision of the Hearing Examiner was filed with the Board wherein he recommended that the application be approved. Exceptions to the Hearing Examiner's Report and Recommended Decision, with brief and a request for oral argument before the Board, were filed by Central. Applicant filed a responding brief and an opposition to oral argument.

Request for oral argument. - As evidenced by the foregoing chronology of occurrences with respect to this application, ample opportunity for comments was afforded to all interested persons, an extensive public hearing was held at which a number of witnesses testified and were cross-examined over a period of several days, a transcript of nearly seven hundred pages provides a record of the hearing, and counsel for the adversary parties have submitted full briefs and written arguments. In the light of these facts and upon review of the entire record, it is concluded that the request by

Central for oral argument before the Board should be denied on the grounds that (a) the parties have had ample opportunity to present their views, (b) there has been no showing that the Board would be better informed as a result of oral argument, and (c) such argument would further delay decision on the application herein. Accordingly, the Board deems it appropriate that the matter be decided at this time on the basis of the record now before it.

Statutory factors. - Section 3(c) of the Act requires the Board to take into consideration the following five factors in acting on this application: (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.

Financial history and condition, and prospects of Applicant and banks concerned. - Applicant became a bank holding company on February 5, 1964. Its holding company system is composed of four banks with approximately $380 million in total deposits at December 31, 1964.[2/] Denver United States National Bank ("Denver U. S. National"),

2/ Unless otherwise indicated, all banking data are as of this date. At June 30, 1965, total deposits of the system were $394 million.

with deposits of approximately $349 million,[3/] is located in Denver; two of the banks in the system, Arapahoe Bank, Littleton (formerly Arapahoe County Bank), and First Bank of Aurora, with deposits of approximately $6 million and $9 million, respectively, are located in suburban communities near Denver. Weld County Bank, located in Greeley, Colorado, about 60 miles north of Denver, was acquired by Applicant in July 1965. It has deposits of approximately $16 million.

The Hearing Examiner found "that the financial history and condition and prospects of Applicant and all of its presently controlled subsidiary banks are satisfactory." The record supports and the Board concurs in these findings.

Mercantile, with approximately $15 million of deposits,[4/] is located in Boulder, Colorado, approximately 30 miles northwest of Denver, and was organized over 60 years ago. The evidence presented shows that Mercantile has experienced a substantial growth in deposits and income, particularly during the period from 1955-1964. Between year-end 1955 and 1964, its deposits increased from about $5 million to almost $15 million; and between 1960 and 1964, the increase was from almost $9 million to nearly $15 million, or 67 per cent. The Board concurs in the Hearing Examiner's finding that Mercantile's financial history and current condition are satisfactory.

3/ At June 30, 1965, its deposits were $364 million.

4/ As of year-end 1965, its deposits exceeded $17 million.

The data of record show that the area served by Mercantile has experienced a steady economic development, and its prospects for continued and substantial economic growth appear favorable. It is reasonable to expect additional growth in Mercantile's deposits and, with such growth, a need for additional capital. While the record reflects previous successful endeavors by Mercantile in marketing its shares, the conclusion appears reasonable that affiliation with Applicant would afford an easier, more assured method for meeting Mercantile's future capital requirements, a fact that, in the Board's judgment, enhances Mercantile's prospects and offers some slight weight in favor of approval of the application.

Management. - Applicant's directors are considered persons of leadership in the regional economy. Its executive officers, drawn from among the executives of Denver U. S. National, have provided satisfactory management for the holding company and its leading subsidiary. Applicant's other three subsidiary banks are also considered to be capably managed.

Mercantile's directors are regarded as experienced and capable. Its president and executive vice-president have provided the bank with successful management. The record shows, however, that the president, who is in his 70's, has entered into an agreement with the bank providing for his retirement as president and for succession of the executive vice-president to the position of president.[5/] While this succession would provide Mercantile with a capable and competent

5/ The former executive vice-president is now president of Mercantile.

chief executive, Applicant states that the remainder of the staff is relatively young and inexperienced in the banking business, and there is no employee on Mercantile's staff considered experienced or capable enough to assume the duties of executive vice-president. It appears that, during the seven or eight years prior to the application herein, three vice-presidents resigned for the purpose of assuming the presidencies of three other Colorado financial institutions and another vice-president chose early retirement. Applicant claims that the proposed affiliation would make available to Mercantile, through the holding company system, a program for recruitment and training, for promotion throughout the system's banks, and for pension plan coverage and other fringe benefits, a program which could facilitate for Mercantile the acquisition, training, and retention of capable management as needed. However, in the light of the favorable prospects for the City of Boulder, its closeness to the City of Denver, and the past experience of Mercantile in attracting capable executive management, the Board is of the opinion that Applicant's proposal is not the only solution to Mercantile's management succession problem. Thus, the assurance offered by Applicant's proposal for an immediate and apparently certain solution to Mercantile's management succession problem affords but little weight toward approval of the application.

Convenience, needs, and welfare of the communities and the area concerned. - The proposed affiliation may be expected to have little, if any, effect on the convenience, needs, and welfare of the communities and the area served by Applicant's present subsidiaries. Rather, the principal effect would be in the area served by Mercantile, of which the City of Boulder is considered to be the primary service area.6/

Between 1950 and 1965, the City of Boulder experienced a substantial population growth - 20,000 to an estimated 48,000 - as well as a significant economic expansion. The University of Colorado, located in Boulder, apparently has grown rapidly in recent years and is changing from a predominantly undergraduate institution to one oriented toward graduate studies, particularly in the areas of physical science and engineering. The record reflects that the City and County of Boulder have acquired, in recent years, numerous industrial plants employing several thousand people, specializing mainly in research and development in the fields of atomic energy, aerospace, electronics, and, to a lesser degree, manufacturing. It is reasonable to expect continued growth in this area. At the end of 1959, there were three commercial banks in Boulder, and in 1965 there were six, among which Mercantile ranks third in deposits. The banking needs of the communities and the area concerned appear to be served adequately.

6/ The area from which it is estimated that Mercantile received 76 per cent of its total individual, partnership, and corporation (IPC) deposits.

Applicant urges, in favor of approval, that it can and is ready to assist Mercantile with respect to audit and accounting procedures, future building programs, bond portfolio management, trust services, marketing operations, and real estate loan activity. The Board is satisfied that Applicant's rendition of assistance with respect to the said services would prove beneficial, not only to Mercantile but also, in certain respects, to the residents and businesses in its primary service area, by virtue of an improvement in the scope and nature of banking services available to them. While the prospects of Applicant's assistance in these respects are consistent with and weigh toward approval, the affirmative weight to be accorded them is somewhat lessened by the absence in the record of evidence indicating that any of the area's major banking needs are presently unserved, or if such unserved need should arise, that it could not be met adequately either through Mercantile's own efforts or with the assistance of its correspondent banks. Accordingly, with respect to the convenience, needs, and welfare of the communities and area concerned, it is the probability of greater speed and certainty with which assistance would be provided Mercantile through the proposed affiliation that offers some weight toward approval of the application.

Effect of proposed acquisition on adequate and sound banking, the public interest, and banking competition. - The Hearing Examiner found, and the record supports his finding, that the aggregate deposits of $380 million held by Applicant's four banks would, by the addition of Mercantile to Applicant's system, be

increased to $395 million, an increase from 14.1 to 14.7 per cent in Applicant's control of the deposits of all insured banks in Colorado. Applicant and the other two registered bank holding companies with subsidiary banks in Colorado currently control 21.6 per cent of the deposits of all insured banks in the State. Applicant's acquisition of Mercantile would increase this concentration to 22.2 per cent. In the Denver Standard Metropolitan Statistical Area,[7/] Applicant's control would be increased from 20 per cent to 21 per cent. In Boulder County, the affiliation would give Applicant control of approximately 9 per cent of the offices of the 11 insured banks and 14 per cent of the deposits of those banks. In the City of Boulder, Applicant would acquire 16.7 per cent of the offices of insured banks and 20 per cent of the deposits of those banks. Mercantile would be the only bank holding company subsidiary in Boulder.

At the time of the Board's approval in November 1963 of Applicant's formation, the Board concluded that, while a sizable portion of the total deposits and loans of all banks in the State of Colorado was concentrated in a relatively few banks, the largest five of which were in Denver and included Applicant's largest subsidiary (Denver U. S. National), it did not appear to the Board that any single banking institution was dominant in the Denver area or in the State as a whole. At that time, as now, Denver U. S. National was the second

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7/ This includes the Counties of Adams, Arapahoe, Boulder, Denver, and Jefferson. Applicant presently has no subsidiary in Adams, Boulder, or Jefferson Counties.

largest bank in Denver and in the State. Applicant's rank as second in control of bank deposits in both areas would continue after the proposed acquisition. The Board concurs in the Hearing Examiner's conclusion that the increase in the concentration of banking resources that would result from consummation of the proposal herein does not represent a consideration adverse to approval of the application.

Considering next the extent to which Applicant's ownership of stock of Mercantile would eliminate existing competition or foreclose future competition between Mercantile and Applicant's subsidiaries, the Board agrees with the Hearing Examiner that these considerations present no bar to approval of the application. The record shows that Mercantile, located 30 miles from Denver U.S. National, is not in competition with it, and that Denver U.S. National does not solicit deposits or loans in Boulder. All the bankers who testified agreed that no Denver bank solicits business in Boulder. About $2.5 million of Denver U.S. National's deposits, amounting to less than one per cent of all its deposits, appear to have originated in Boulder. They represented almost entirely correspondent bank deposits from two Boulder correspondents. About $478,000 of Denver U.S. National's loans, or .3 per cent of its total loans, were shown as originating in Boulder. Virtually all arose through participation with Boulder banks.

Mercantile is located approximately 38, 40, and 56 miles from Applicant's three subsidiaries other than Denver U.S. National. These three relatively small institutions serve primarily their immediate vicinities. The Hearing Examiner's finding that none of

Applicant's subsidiary banks competes in Mercantile's primary service area is supported in the record and is adopted by the Board. The record shows also that Mercantile does not compete, to any significant degree, in the primary service areas of any of Applicant's subsidiaries.

Applicant asserts and the evidence shows that the six Boulder banks compete vigorously with each other. Mercantile (with nearly $15 million of deposits) ranks third in size of the Boulder banks. First National Bank in Boulder, the largest bank in the city (with over $30 million of deposits), together with its affiliate, the Arapahoe National Bank of Boulder (deposits of approximately $3 million), controls over 45 per cent of all commercial bank deposits in Boulder. National State Bank of Boulder (deposits of nearly $22 million) controls about 30 per cent, and Mercantile about 20 per cent of the total deposits. The remaining five per cent are controlled by the two smallest banks in Boulder (deposits of approximately $1.5 million and $2 million, respectively). The acquisition herein proposed would not diminish the number of offices servicing Boulder. In addition, the evidence shows that there are offices of four savings and loan institutions in Boulder, three of which each have total savings in excess of the total deposits of any of the banks there. One of these institutions, with its head office in Denver, has savings funds exceeding $114 million. In Boulder County, there are five additional banks, three of which have deposits of $2.5 million or less. None of the five banks derives more than a minimal amount of business

from Boulder, Mercantile's primary service area. It is reasonable to conclude from the record, as has the Hearing Examiner, that the proposed acquisition would not significantly diminish existing competition in Boulder or any of the areas involved, nor preclude potential competition there. Rather, it appears that the businesses and residents in Boulder will be the beneficiaries of more vigorous competition to be offered to the two larger banks in the area.

In opposition to the proposal herein, Central further argues that the subject acquisition, coupled with other acquisitions to date by Applicant, will restrict competition in correspondent banking. While the proposal herein may result, as Central argues, in its loss of Mercantile as a correspondent bank (with a $1 million account) to the gain of Denver U.S. National, Applicant points out that the affiliation may result, on the other hand, in Denver U.S. National losing as much or more of its correspondent bank business to the gain of Central or other Denver correspondents.

It appears that the correspondent banking business of Colorado is concentrated in Denver. The five largest banks in the State, all located in Denver, account for 88 per cent of the deposits made by banks. First National Bank of Denver ranks first with approximately 31 per cent of the total of correspondent bank deposits, amounting to about 11 per cent of its total deposits. Central ranks second with about 22 per cent of the total of such correspondent bank deposits, amounting to 20 per cent of its total deposits; and Denver U.S.

National ranks third with about 17 per cent of such deposits, amounting to 7 per cent of its total deposits. It is evident that the shifting of Mercantile's relatively small account would not have a significant effect on the correspondent bank business in the relevant markets, nor cause the position of Applicant's subsidiaries with respect to competition for correspondent accounts to be enhanced in any significant measure at the expense of their competitors. Nor, in view of the relative ease of access to a number of alternative Denver bank correspondents that will continue to be available to the businesses and residents of Boulder, would Mercantile's affiliation with Denver U.S. National represent an undue deprivation of access to correspondent bank services.

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.

The possibility that Applicant, in the future, may seek approval of additional acquisitions as part of a plan for "continuing expansion through the holding company device" - as suggested by the opposing bank in its exceptions to the Hearing Examiner's Report and Recommended Decision - is not considered to be a significant factor adverse to the proposal herein. The Board consistently has taken the position that each application must be considered on the pertinent

facts presented, and a decision by the Board in a given matter does not constitute any commitment on future applications.

To the extent that the findings and conclusions of the Hearing Examiner are consistent with those contained herein, they are adopted. Opposing bank's exceptions to the Hearing Examiner's Report and Recommended Decision have been fully considered, and the Board's findings and conclusions reflect the Board's judgment of the merits of those exceptions.

On the basis of all the relevant facts contained in the record before the Board, and in the light of the factors set forth in section 3(c) of the Act, it is the Board's judgment that the proposed acquisition would be consistent with the public interest and that the application should therefore be approved.

May 16, 1966.

Item No. 6
5/16/66

DISSENTING STATEMENT OF GOVERNOR ROBERTSON

I have voted to deny this application essentially for the reasons set forth in my statement of dissent from the Board's action approving Applicant's formation in November 1963. At that time I expressed the opinion that the Congress, in enacting the Bank Holding Company Act, never intended that the statute be used as a vehicle for altering the banking structure of a State over the expressed objection of that State, particularly where there was no satisfactory showing that any benefit would likely inure to the public from a proposed holding company formation.

Similarly, in the present case, the evidence of record clearly establishes that the major banking needs of the Boulder area are now being served and that no cognizable public benefit will result from consummation of this proposal. On the contrary, it seems clear to me that the further concentration of the banking resources in the State under Applicant's control that will follow upon its acquisition of The Mercantile Bank and Trust Company represents a circumstance inimical to the public and directly contrary to the expressed policy of the State of Colorado favoring independent unit banks.

The record in this case reflects the pride that the community of Boulder has in its status as an independent, growing community. In my opinion, the continued economic independence of Boulder becomes less

certain by the very real possibility that Applicant's ownership of the Mercantile Bank will result in a draining off of that bank's deposits, now presumably remaining in and primarily serving the Boulder area, to serve the regional requirements of Denver U. S. National Bank. While access to these Boulder funds will afford little competitive advantage to Denver U. S. National, removal of such funds from Boulder could have a significantly adverse effect on the medium and small size business credit needs that Applicant asserts would be served by this proposal.

Finally, Applicant's acquisition of Mercantile will further the existing concentration of banking resources in a few large Denver banks and will constitute, as at the time of Applicant's formation, an open invitation to increase that concentration. The State's expressed opposition to such a resulting banking structure, when combined with the other adverse features of this proposal, leaves, in my judgment, no alternative to denial of the application.

May 16, 1966.

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

Item No. 7
5/16/66

OFFICE OF THE CHAIRMAN

May 16, 1966.

The Honorable William L. Dawson,
Chairman, Committee on Government Operations,
House of Representatives,
Washington, D. C. 20515.

Dear Mr. Chairman:

This is in response to your letter of March 24, 1966, concerning the Twenty-Second Report by the Committee on Government Operations, entitled "Federal Reserve System--Check Clearance Float." Your letter noted that this report contains three recommendations, and requested any comments the Board might care to make in regard to these recommendations and in particular in regard to any action which has been taken or proposed to implement them.

The subject report recommends in substance that the Board:

(1) Establish quantity and time goals for float elimination through technological developments, and, if such developments do not meet expectations, consider the advisability of adopting a plan for immediate charges and credits on checks or for time schedules which approximate actual collection times.

(2) Develop records that would indicate the proportionate use member banks make of float as reserves so that, if efforts to reduce float fall short of expectations, a study can be made to determine whether charges should be assessed against banks in proportion to the benefits they derive from float.

(3) Coordinate the System's ADP equipment planning and acquisitions with the rest of the Government, as contemplated by Public Law 89-306.

Prior to the receipt of your letter of March 24, 1966, the System had started several studies, which on a long-term basis, are directed toward minimizing float and improving the payments mechanism. Some should yield results within a year or so, while others deal with possible changes that would take longer to put into effect.

The following actions have already been taken as part of these studies:

(1) Procedures are now under way for a new and much more elaborate float survey at each of the 36 Federal Reserve offices. The purpose is to identify and quantify the components of total float for each day during the month of September. This is the earliest possible survey date in light of the magnitude of the job and the float characteristics to be studied.

(2) Plans are being developed to determine the possible areas throughout the country in which regional clearing facilities might be expanded or established, along with the cost and benefits of such undertakings. This is a longer range undertaking for which it is now impracticable to set a time table.

(3) Several suggestions for changes in Reserve Bank operating procedures to reduce float are now being evaluated. Some of these--such as increased use of trucks for deliveries of checks, and arrangements for automatic payments therefor--are being adopted on a limited scale but will be pushed more vigorously. Other possibilities--such as special handling for items not encoded--hold future promise.

The Board recently discussed your letter of March 24, 1966, with the Presidents of the various Federal Reserve Banks. It was the consensus of this discussion that further decisions with respect to possible steps to reduce float should proceed after the development of information from the undertakings mentioned above.

The Board has cooperated with other Government Agencies on matters concerning equipment planning and acquisitions, and will continue this practice.

Sincerely yours,

(Signed) Wm. McC. Martin, Jr.

Wm. McC. Martin, Jr.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

Item No. 8
5/16/66

OFFICE OF THE CHAIRMAN

May 16, 1966

The Honorable James J. Saxon,
Comptroller of the Currency,
Treasury Department,
Washington, D. C. 20220

Dear Jim:

This is with further regard to the exchange of information regarding National banks.

I can assure you that the Federal Reserve Banks will continue the practice, which they have followed for many years, of fully and promptly advising the Regional Comptrollers of the Currency (and their predecessors, the District Chief National Bank Examiners) of any information coming to the Reserve Bank regarding a State member bank that might affect a National Bank. One example of this is a kiting operation involving both a State member bank and a National bank. Another example is the fact that a State member bank under common ownership or control with a National bank is receiving more than usual supervisory attention.

In addition to needing to be advised of information regarding a National bank which might affect a State member bank, the System has responsibility for administering the Federal Reserve discount function in the public interest as to all member banks, both State and National, and the System is under the following directive in the Federal Reserve Act:

> "...Each Federal reserve bank shall keep itself informed of the general character and amount of the loans and investments of its member banks with a view to ascertaining whether undue use is being made of bank credit for the speculative carrying of or trading in securities, real estate, or commodities, or for any other purpose inconsistent with the maintenance of sound credit conditions; and, in determining whether to grant or refuse advances, rediscounts or other credit accommodations, the Federal reserve bank shall give consideration to such information."

These responsibilities make it essential that the System have full current information regarding National banks, particularly the name of, and any developments with respect to, any National bank receiving more than usual supervisory attention.

I understand that this subject is being considered by the Subcommittee (Problem Banks) of the Coordinating Committee on Bank Regulation, and I earnestly hope that further implementing arrangements can be promptly worked out to assure that the System will obtain necessary information. In the meantime, I am sending the Reserve Banks copies of this letter and your letter of March 3, 1966, for their guidance, as I have also sent them copies of our earlier correspondence on the subject.

Sincerely yours,

(Signed) Wm. McC. Martin, Jr.

Wm. McC. Martin, Jr.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Item No. 9
5/16/66

Office Correspondence

Date May 11, 1966.

To Board of Governors

From Division of Examinations
Office of the Controller

Subject: Reimbursement of travel expenses incurred by Reserve Bank employees borrowed to assist Board's examining staff.

Prompted in part by a question raised by one of the Reserve Banks regarding the adequacy of the per diem paid in lieu of subsistence to Reserve Bank employees borrowed by the Division of Examinations to assist in examinations of Federal Reserve Banks other than their own, views on the subject were exchanged between Examinations and the Controller's Office. In the discussion, a suggestion was made that the travel expenses of employees loaned by a Reserve Bank be paid by the employer Reserve Bank on the same basis as would have been allowed to the employees if they were traveling on bank business, rather than according to the Board's travel regulations as heretofore. Also, to simplify the processing of claims for reimbursement, it was suggested that each travel voucher and overtime claim submitted by a Reserve Bank employee be audited and paid by the employing Reserve Bank, and that such Bank in turn submit a claim to the Board that would supply essential information but without supporting documents.

The proposal that such an arrangement be substituted for that currently in effect was forwarded on April 29 to all Federal Reserve Banks except the Federal Reserve Bank of San Francisco (from which personnel is not normally borrowed because of its distant location) with a request for their views.

Replies have been received from ten of the eleven Banks, all of whom expressed concurrence with the proposal. Accordingly, approval of the Board is requested for the proposed arrangement as outlined above and described in the enclosure accompanying the attached proposed letter to the Reserve Banks affirming the arrangement previously suggested to them.

Attachment.

EXPENSES REIMBURSABLE TO A FEDERAL RESERVE BANK IN CONNECTION WITH SERVICES OF ITS EMPLOYEES IN ASSISTING THE BOARD'S EXAMINING STAFF IN EXAMINATIONS OF OTHER FEDERAL RESERVE BANKS

(1) Travel Expenses

Transportation and subsistence expenses paid to the designated employees by the employer Federal Reserve Bank in accordance with such Bank's current rules and regulations applicable to such employees for travel on bank business.

(2) Overtime

The actual amount of overtime compensation, if any, applicable to the specific examination and paid by the Reserve Bank in accordance with its prevailing policy for overtime payments.

Note: It is requested that the claim forwarded by a Federal Reserve Bank to the Board of Governors for reimbursement of expenses incurred by the Bank's employees assisting in an examination of another Federal Reserve Bank (1) identify the Reserve Bank examined and (2) list the names of the employees who participated in the examination, showing for each (a) the dates his services were used; (b) the amount of overtime paid, if any; and (c) the amount of his travel expenses distributed among transportation and other major subclassifications, (i.e., subsistence, hotels, etc.) normally reported under the Bank's internal procedures. Copies of expense vouchers or other supporting documents need not be submitted.