FR 609

Minutes for June 23, 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 Thursday, June 23, 1966. The Board met in the Board Room at 10:00 a.m.

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

Mr. Sherman, Secretary
Mr. Bakke, Assistant Secretary
Mr. Hackley, General Counsel
Mr. Solomon, Director, Division of Examinations
Mr. Hexter, Associate General Counsel
Mr. Hooff, Assistant General Counsel
Mr. Daniels, Assistant Director, Division of Bank Operations
Mr. Leavitt, Assistant Director, Division of Examinations
Miss Wolcott, Technical Assistant, Office of the Secretary
Miss Hart and Mr. Shuter of the Legal Division
Mr. Poundstone, Review Examiner, Division of Examinations

Approved items. The following items were approved unanimously after consideration of background information that had been made available to the Board. Copies are attached under the respective item numbers indicated.

	Item No.
Letter to Puritan Bank and Trust Company, Meriden, Connecticut, approving the establishment of an in-town branch.	1
Letter to Hempstead Bank, Hempstead, New York, interposing no objection to the continuation of safe deposit facilities at the bank's Levittown branch while conducting other branch operations in nearby temporary quarters.	2

	Item No.
Letter to Bankers International Corporation, New York, New York, granting permission to acquire shares of Petroquimica del Atlantico, S.A., Barranquilla, Colombia.	3
Letter to the Bureau of the Budget regarding enrolled bill H.R. 7371, to amend the Bank Holding Company Act of 1956.	4

Currency of $2 denomination (Item No. 5). In a letter dated February 28, 1966, the Secretary of the Treasury had sought the views of the Board on alternative proposals of abandoning the $2 denomination of United States notes or the issuance of $2 Federal Reserve notes. The question was raised because of the elimination from the 1967 Federal budget of funds for the printing of United States notes, and the possibility that existing stocks would not be sufficient to meet demand during that fiscal year. On April 21, 1966, the Board replied to the effect that, with few exceptions, the public would not be significantly inconvenienced by the elimination of $2 bills, and neither the Board nor the Reserve Banks favored the printing of $2 Federal Reserve notes at this time. Also, it was suggested that if the $2 bill was discontinued, the Reserve Banks and the Treasury should stop paying out notes at the same time and the existing stocks should be destroyed.

It now appeared that in the near future it would be impracticable for the Federal Reserve Banks to continue to meet requests for $2 notes without new supplies. The stock of new $2 bills in Washington had been

exhausted, and the total supply at Reserve Banks would soon become so small as to make continuation of the current procedure of shipments between Federal Reserve offices to meet regional demands unfeasible. Accordingly, the Division of Bank Operations, in a draft letter to the Secretary of the Treasury that had been circulated to the Board, proposed that the Federal Reserve Banks discontinue paying out $2 bills and that outstanding notes be returned to custody of the Treasurer of the United States until such time as the Treasury could supply additional quantities of $2 United States notes. In this connection, it was understood that funds for printing $2 United States notes were included in the Treasury's proposed budget for the fiscal year 1968, although the Department would not be averse to having the proposal deleted by the Bureau of the Budget.

During remarks supplementing the circulated material, Mr. Daniels noted that the stock of $2 bills had become depleted faster than anticipated. He observed that no reply to the Board's letter of April 21 had been received from the Treasury, and, from informal talks with members of the Treasury staff, it was his belief that no reply would be forthcoming before September, at which time the budget proposal for printing $2 United States notes during fiscal 1968 would have been acted upon by the Budget Bureau.

Following consideration of questions raised by members of the Board that pointed up the limited use of the $2 denomination as a

circulating medium, the letter to the Secretary of the Treasury was approved unanimously. A copy is attached as Item No. 5.

Interpretation of Regulation T (Item No. 6). In a letter dated April 22, 1966, the National Association of Securities Dealers requested the opinion of the Board as to whether a violation of section 220.4(f)(6) of Regulation T (Credit by Brokers, Dealers, and Members of National Securities Exchanges) had occurred in a transaction involving the transfer of credit by a broker from a customer's margin account into a special miscellaneous account. An appeal by the customer, from a decision adverse to him rendered by the Philadelphia branch of the National Association of Securities Dealers, was pending before the Association.

In summary, it appeared that on November 1, 1963, the customer ordered the closing of several margin accounts in which were held positions in certain securities, all registered on a national securities exchange. The customer paid the broker the total amount of the debit balances in cash, and the broker initiated steps to have the securities transferred to the customer's name. On November 6, margin requirements were raised from 50 per cent to 70 per cent. On November 8, before transfer of shares to the customer's name had been completed, the customer decided to buy over-the-counter securities. The broker informed the customer that the shares would have to be purchased for cash, but that a loan, in the amount of 50 per cent of the current market value of the registered securities still held by the broker, could be made available for this purpose.

Thereafter, a dispute arose over management of the account, and the customer charged the broker with a violation of Regulation T in having extended credit on the basis of 50 per cent, rather than 30 per cent, of the value of his securities, since on the date the credit was extended the margin requirement was 70 per cent. The broker countered that on November 4, incident to closing out the margin accounts, a routine bookkeeping transfer of 50 per cent of the current market value of the registered shares in the customer's margin accounts had been made to his special miscellaneous account. He argued that it was customary trade practice for a broker to withdraw excess funds from customers' margin accounts into their special miscellaneous accounts, thereby making these funds available for unrestricted use, and that since this particular transfer had taken place before margin requirements were raised, the full 50 per cent was therefore available for extension of credit to the customer.

The question before the Board was whether the broker had the authority to make the transfer into the special miscellaneous account after the customer had indicated he wanted to close his margin accounts. There had been distributed a memorandum from the Legal Division dated June 21, 1966, in which it was concluded that, on the basis of the record submitted to the Board, the transfer was in violation of Regulation T. This conclusion was based on the premise that a broker's authority to effect withdrawals from overmargined accounts for deposit

in special miscellaneous accounts arises from his contract with the customer, subject to applicable regulations and laws. Since, in this particular case, the customer had ordered his accounts closed, had paid in full the debit balance, and directed that the securities be delivered to him, the contractual authorization for transactions with respect to the customer's accounts, other than to have the securities issued out in the customer's name, had terminated, and could not be revived absent a specific request from the customer that his accounts be reopened.

Various aspects of the matter were discussed, in the light of the distributed material and supplementary remarks by Miss Hart, directed toward clarifying the issue before the Board. Certain suggestions for modifications in the draft reply were made by Governor Brimmer, after which unanimous approval was given to a letter to the National Association of Securities Dealers in the form attached as Item No. 6.

The meeting then adjourned.

Secretary's Note: Acting in the absence of Governor Shepardson, Governor Robertson today approved on behalf of the Board memoranda recommending the following actions relating to the Board's staff:

Salary increases, effective July 3, 1966

Name and title	Division	Basic annual salary From	To
	Research and Statistics		
Mary Jane Harrington, Economist		$10,491	$10,797
William Paul Smith, Economist		11,355	11,723
Judith A. Ziobro, Research Assistant		7,097	7,304

Salary increases, effective July 3, 1966 (continued)

Name and title	Division	Basic annual salary From	To
	International Finance		
Gordon B. Grimwood, Assistant to the Director		$19,415	$20,005
	Personnel Administration		
Patricia E. Gardosik, Secretary		5,181	5,352
	Administrative Services		
Viola E. Hamilton, Charwoman		3,983	4,102
Esmond C. Langley, Head Messenger		5,733	5,889
John H. McDonald, Guard		4,429	4,569
Blanche E. Peacock, Charwoman		4,459	4,578
Hubert G. Weems, Guard		4,569	4,709

Acceptance of resignation

Edward J. Finck, Purchasing Assistant, Division of Administrative Services, effective the close of business August 31, 1966.

Permission to engage in outside activity

Donna A. Jameson, Clerk-Typist, Division of Personnel Administration, to work for a local department store on a part-time basis.

Secretary

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

Item No. 1
6/23/66

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

June 23, 1966

Board of Directors,
Puritan Bank and Trust Company,
Meriden, Connecticut.

Gentlemen:

The Board of Governors of the Federal Reserve System approves the establishment by Puritan Bank and Trust Company, Meriden, Connecticut, of a branch on property adjacent to 27 East Main Street, Meriden, Connecticut, 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
6/23/66

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

June 23, 1966

Board of Directors,
Hempstead Bank,
Hempstead, New York.

Gentlemen:

The Board of Governors of the Federal Reserve System offers no objection to Hempstead Bank, Hempstead, New York, continuing to provide access to its safe deposit boxes at 3240-42 Hempstead Turnpike, Levittown, New York, while conducting branch operations from new temporary quarters at 3278 Hempstead Turnpike, Levittown, until such time as renovation of the permanent quarters are completed and all operations are resumed at that site.

Very truly yours,

(Signed) Karl E. Bakke

Karl E. Bakke,
Assistant Secretary.

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

Item No. 3
6/23/66

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

June 23, 1966.

Bankers International Corporation,
16 Wall Street,
New York, New York. 10015

Gentlemen:

As requested in your letter of May 17, 1966, the Board of Governors grants consent for your Corporation to acquire 2,631,900 shares of Petroquimica del Atlantico, S.A., Barranquilla, Colombia ("Petroquimica"), at a cost of approximately US$1,462,170, provided such shares are acquired within one year from the date of this letter.

It is understood that the acquisition of approximately 471,900 of the above-mentioned shares will be concurrent with the sale by your Corporation to Petroquimica of 30,035 shares of Antex Oil and Gas Co., Inc., in the approximate amount of US$262,170.

The Board also approves the purchase of shares of Petroquimica within the terms of the above consent in excess of 10 per cent of your Corporation's capital and surplus.

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

Very truly yours,

(Signed) Karl E. Bakke

Karl E. Bakke,
Assistant Secretary.

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

Item No. 4
6/23/66

OFFICE OF THE CHAIRMAN

June 23, 1966

Mr. Wilfred H. Rommel,
Assistant Director for Legislative
Reference,
Bureau of the Budget,
Washington, D. C. 20503

Dear Mr. Rommel:

This is in response to your communication of June 22, 1966, requesting the views of the Board on the enrolled bill H. R. 7371, "To amend the Bank Holding Company Act of 1956."

The Board recommends that the enrolled bill be approved by the President.

Sincerely yours,

(Signed) Wm. McC. Martin, Jr.

Wm. McC. Martin, Jr.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

Item No. 5
6/23/66

OFFICE OF THE CHAIRMAN

June 23, 1966

The Honorable Henry H. Fowler,
Secretary of the Treasury,
Washington, D. C. 20220

Dear Joe:

On April 21, 1966, we responded to your letter of February 28, 1966, requesting our views on the alternative proposals of abandoning the $2 denomination note or the issuance of a $2 Federal Reserve note. The letter stated that the Reserve Banks and the Board would not favor the printing of a $2 Federal Reserve note at this time and that if the $2 bill is discontinued, the Reserve Banks and the Treasury should stop paying out the notes at the same time and the existing stocks should be destroyed.

Your letter of February 28 said that the Bureau of the Budget had eliminated from the 1967 budget the Treasury's normal request for funds for printing United States notes and that you could, with our help and some lowering of the standard of fitness, meet the demand for $2 currency in fiscal year 1967 without buying any $2 United States notes. We understand that funds for printing $2 United States notes have been included in the Treasury's proposed budget for fiscal year 1968.

It appears now that it will be impracticable to continue to supply the demand for $2 bills much longer without new supplies. For several weeks, the stock of new $2 bills in Washington has been exhausted, and so far we have requested the Office of the Treasurer of the United States to authorize 24 shipments between one Federal Reserve office and another in order to meet the demand. Our estimates indicate that it will become impracticable to continue to meet the growing demand by such interoffice shipments much beyond June.

Accordingly, we propose to instruct the Federal Reserve Banks to discontinue paying out $2 notes when the total supply at the Reserve Banks becomes so small that it is impracticable to

continue the current procedure of interoffice shipments. The Banks could place the notes in custody for the Treasurer of the United States and hold them until such time as the Treasury can supply additional quantities of $2 United States notes.

I trust you will have no objection to the program outlined in this letter.

Sincerely yours,

(Signed) Bill

Wm. McC. Martin, Jr.

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

Item No. 6
6/23/66

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

June 23, 1966

Mr. Lloyd J. Derrickson,
Associate General Counsel,
National Association of Securities Dealers,
888 17th Street, N. W.,
Washington, D. C.

Dear Mr. Derrickson:

This refers to your letter of April 21, 1966, enclosing a copy of the record in a matter pending before the Board of Governors of the National Association of Securities Dealers, Inc. The matter involves a question whether Regulation T, "Credit by Brokers, Dealers, and Members of National Securities Exchanges", promulgated by the Board of Governors of the Federal Reserve System ("the Board") pursuant to section 7 of the Securities Exchange Act of 1934 ("the Act") has been violated. You have asked for the Board's opinion.

The matter is on appeal from a decision of the District Business Conduct Committee of District No. 11 in regard to Complaint No. P-282, of Dr. Manassi Antonis, against Fahnestock & Co. ("Fahnestock") and Frank Bahr (a registered representative employed by Fahnestock). So far as material to the question before the Board, the facts found by the District Committee are as follows.

Dr. Antonis and his mother had several joint margin accounts with Fahnestock, in which were held positions in certain securities, all registered on a national securities exchange. In October, 1963, Dr. Antonis decided to close the accounts. Since he wished to do this without liquidating any collateral, he paid Fahnestock the total amount of the debit balances in cash. This cash was credited to the accounts on November 1. The debit balances were then cleared, and Fahnestock began to effect the transfer of the securities to the joint names of Dr. Antonis and his mother. The total market value of the securities appears to have been approximately $12,500.

On November 6, 1963, the Supplement to Regulation T was amended, decreasing the maximum loan value of securities registered on a national securities exchange from 50 to 30 per cent, with the effect of raising the margin requirement from 50 to 70 per cent. The retention requirement imposed by section 220.8(c) of the Supplement was increased at the same time to 70 per cent.

On November 8, Dr. Antonis asked Mr. Bahr about the possibility of purchasing shares of Magnafax Co., a stock which is not registered on a national securities exchange. Mr. Bahr explained that these shares would have to be purchased for cash, and told Dr. Antonis that sufficient credit could be made available against the registered securities he owned (which Fahnestock still had in its possession) to finance the purchase of the desired number of shares of Magnafax, with a market value of about $6,200. Dr. Antonis instructed Mr. Bahr to make the purchase.

In a rising market, however, the shares cost some $300 more than the credit Mr. Bahr had indicated was available. Dr. Antonis was then told that section 220.3(c)(1) of Regulation T required that he make an additional deposit of $300 in his margin account. The deposit could be made in cash or he could liquidate some of the registered securities held in the account. He chose liquidation. Under the increased retention requirement, over $1,100 worth of registered securities had to be liquidated in order to release the amount needed for deposit into the margin account.

Subsequent to the liquidation just described, Dr. Antonis made a protest to Fahnestock based on the fact that after November 6, 1963, the current Supplement to the regulation forbade a creditor to lend more than 30 per cent of the current market value of registered securities held as collateral in a margin account. Dr. Antonis contended that Fahnestock had violated the regulation in lending more than approximately $3,750, the maximum permitted under the amended Supplement against the registered securities which Fahnestock had held for him, thereby inducing him to buy more securities than he would have had the proper margin requirement been applied.

It seems clear that a creditor would violate the regulation if in fact he extended credit after November 6, 1963, in excess of 30 per cent of the market value of registered securities held in a margin account, where the purpose of the loan was to purchase securities. As a defense to the charge, however, Fahnestock asserted, and the District Committee apparently assumed, that the credit in question had been extended before November 6. To explain this assertion, Fahnestock stated that on or immediately after clearing the debit balance in the prior margin accounts, a bookkeeping entry was made "withdrawing" 50 per cent of the current market value of the registered shares held in those

accounts, the shares still being, as stated above, in the firm's possession for the purpose of transferring them into the names of Dr. Antonis and his mother. An exhibit in the record indicates that such a withdrawal may have been made on November 4. The amount withdrawn was credited, Fahnestock states, to a memorandum "special miscellaneous account" ("s.m.a.") in Dr. Antonis' name. This credit, according to Fahnestock, was in the amount of $6,200, and was available to Antonis in his "new" margin account.

Section 220.4(f)(6) permits a creditor to " . . . receive from or for any customer, and pay out or deliver to or for any customer, any money . . ." in a special miscellaneous account. Among its other functions, this section affords a benefit to customers who would otherwise have overmargined accounts, protecting a customer's excess purchasing power against changes in margin requirements by permitting the broker to withdraw excess funds out of a general account and hold them as a credit balance in a s.m.a.

An increase in margin requirements reflects the Board's judgment that excessive credit is flowing into the securities markets. The increase is designed not only to reduce the inflow of additional credit into old and new accounts, but through the restrictions on withdrawals to improve the margin status of undermargined accounts. While the use of the s.m.a. to effect withdrawals from overmargined accounts tend to preserve some flexibility for investors, it must be recognized that such procedures detract from the effectiveness of margin requirements, and consequently they should be used only in strict conformity with the contractual arrangement between the creditor and the customer.

The creditor's authority to effect withdrawals from overmargined accounts for deposit in the s.m.a. arises from his contract with the customer, subject to applicable regulations of the Board, the Securities and Exchange Commission, the NASD, and the stock exchanges, as well as local law. Applying the principle that the permission granted by section 220.4(f)(6) is to be strictly construed, it follows that such withdrawals should not be effected unless clearly authorized by the creditor's contract with the customer. In many cases involving a continuing account, this practice may be authorized by the agreement under which the account was opened. In such cases, it can be assumed that the customer has knowingly given his consent to the making of withdrawals where permitted under applicable regulations, without being consulted on each occasion. The burden of proof would be upon the creditor to show that a particular withdrawal was so authorized.

On the other hand, facts such as those found in the present case, where there was an instruction to close an account coupled with payment in full of the debit balance and directions to transfer the securities which had been held in the account out of street name and into the individual names of the customers do not seem compatible with any such continuing authorization. If anything, the facts tend to indicate that no authorization to make withdrawals into an s.m.a. existed.

In such a case, the Board considers that the principle that the regulation should be strictly construed requires, in order to overcome the inference that the credit to the s.m.a. was not made in compliance with section 220.4(f)(6), that the creditor establish that the customer specifically authorized the withdrawal. On the basis of the record submitted to the Board, it does not appear that such an authorization was given, and that as a result, the withdrawal was apparently effected in violation of Regulation T. The Board's conclusion, of course, is limited to the facts before it.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.