FR 609

Minutes for September 6, 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 WM

Gov. Robertson R

Gov. Shepardson

Gov. Mitchell

Gov. Daane

Gov. Maisel

Gov. Brimmer

Minutes of the Board of Governors of the Federal Reserve System on Tuesday, September 6, 1966. The Board met in the Board Room at 10:00 a.m.

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

Mr. Sherman, Secretary
Mr. Kenyon, Assistant Secretary
Mr. Bakke, Assistant Secretary
Mr. Young, Senior Adviser to the Board and Director, Division of International Finance
Mr. Holland, Adviser to the Board
Mr. Solomon, Adviser to the Board
Mr. Molony, Assistant to the Board
Mr. Cardon, Legislative Counsel
Mr. Fauver, Assistant to the Board
Mr. Brill, Director, Division of Research and Statistics
Mr. Hexter, Associate General Counsel
Mr. Shay, Assistant General Counsel
Mr. Leavitt, Assistant Director, Division of Examinations

Governor Robertson reported to the Board his participation in discussions being held by Treasury and other Administration officials relating to the development of a package of proposals for actions in the fiscal area that were being considered for incorporation in a Presidential message to the Congress as part of the program for restraining inflationary pressures. In this connection, it was understood that there would be distributed to the Board copies of a memorandum from Miss Stockwell of the Division of Research and Statistics assessing the

1/ Withdrew from meeting at point indicated in minutes.

likely effects of a suspension of the investment tax credit and accelerated depreciation.

Mr. Hooff, Assistant General Counsel, and Miss Wolcott, Technical Assistant, Office of the Secretary, entered the meeting at this point.

Application for continuation of deposit insurance (Item No. 1). Unanimous approval was given to a letter to the Federal Deposit Insurance Corporation (copy attached as Item No. 1) concerning the application of The Union Bank, Loogootee, Indiana, for continuation of deposit insurance after withdrawal from membership in the Federal Reserve System.

Gold loan (Item No. 2). There had been distributed a memorandum from Mr. Young dated September 2, 1966, relating to a proposed gold collateral loan to Bank of the Republic, the central bank of Colombia. (Aspects of this loan request had been discussed at the Board meeting on September 2, 1966.)

Bank of the Republic had requested a loan or loans against gold collateral of up to $13 million for 180 days. As authorized by the Board of Directors of the New York Reserve Bank, subject to approval by the Board of Governors, such loan or loans: (1) would be made up to 98 per cent of the value of gold bars to be set aside in the vaults of the New York Bank under pledge to it; (2) would mature in 90 days with option to repay at any time before maturity, advances and repayments to be made in multiples of $1 million; (3) would bear interest at the discount rate of the New York Bank in effect on the date on which such loan or loans were made; and (4) could be requested and made at any time after receipt of Bank of the Republic's acceptance of the New York Bank's terms and conditions, but not later than September 30. The usual participation would be offered to the other Reserve Banks.

During discussion it was noted that, although Bank of the Republic had requested the loan for a period of 180 days, for reasons stated in the distributed material approval was being recommended on a 90-day basis only. Question was raised whether a request for renewal might be expected at the end of the 90-day period. It was pointed out that the wire from the New York Bank stated that the Reserve Bank proposed to advise Bank of the Republic that no request for renewal of the loan beyond the 90-day expiration date would be considered "unless facts and figures are presented indicating that a situation exists warranting such consideration."

In response to this question, it was noted that the Board's reply wire to the New York Bank would request the Bank to advise Bank of the Republic that no renewal at the expiration of the 90-day term would be considered. Staff indicated that the Board's position, as stated in the wire, would be made clear to the New York Bank.

Unanimous approval was then given to the telegram to the Federal Reserve Bank of New York, a copy of which is attached as Item No. 2.

Absorption of exchange charges. There had been distributed copies of a communication dated August 23, 1966, from the Comptroller of the Currency to national banks wherein it was stated that a national bank had the right, if not the duty, to absorb exchange charges for its customers in the same manner and in the same amount as its nonmember bank competition. This position was in conflict with the long-standing position of the Board that absorption of exchange charges constituted an indirect payment of interest on demand deposits, a practice prohibited to member banks by virtue of section 19 of the Federal Reserve Act and the Board's Regulation Q (Payment of Interest on Deposits).

Governor Robertson recalled that the question of absorption of exchange charges had been a subject of controversy for many years, with the Federal Deposit Insurance Corporation adhering to a view different from that of the Board. Thus, unlike member banks of the Federal Reserve System, nonmember insured banks were, by virtue of the Corporation's position on this matter, free to absorb exchange charges in connection with the collection for depositors of checks drawn on a nonpar bank. Discussions had been held commencing in 1942 between the Board, the Federal Deposit Insurance Corporation, and the Comptroller in an effort to develop a uniform position among the three Federal bank supervisory agencies, but to no avail, one recent effort at reconciliation, in 1962, having been unsuccessful, partly because of the position taken by the Comptroller at that time.

Governor Robertson noted that the Comptroller's August 23 letter now brought the issue into sharp focus and that it seemed imperative to act promptly to obviate a situation that would result in further inequity of the competitive positions of various classes of banks. As one alternative, the Board could take this opportunity to adopt the position of the Federal Deposit Insurance Corporation and hold that absorption of exchange charges does not represent an indirect payment of interest on demand deposits. As another possibility, the Board could write a letter to the Comptroller, and release it to the press, pointing out that section 19 of the Federal Reserve Act vests in the Board the authority to determine what shall be deemed payment of interest on deposits by member banks and to prescribe rules and regulations to effectuate the purposes of the statute and prevent evasions. As a third possibility, the Board could write a letter to the Secretary of the Treasury calling attention to the non-observance of the so-called "Dillon" procedure by the Comptroller and raising the question of the further usefulness of the procedure in such circumstances.

Governor Robertson then referred to advice he had received by telephone from President Galusha of the Minneapolis Reserve Bank to the effect that the Minnesota State legislature might pass a bill that would prohibit banks in that State from charging exchange. President Galusha had expressed the hope that the Board would adhere to its long-held position in order to avoid jeopardizing this legislation. Governor Robertson expressed the opinion that in view of the situation in the Ninth District the Board should proceed with caution.

Governor Mitchell commented that he had just read a doctoral dissertation, "The Theory and Practice of Nonpar Banking," by Paul F. Jessup, which had caused him to reappraise the merits of the Board's position on absorption of exchange. In his opinion the Board might be perpetuating a situation that was advantageous for a relatively small number of larger nonmember banks who could attract profitable correspondent balances by agreeing to clear checks drawn on nonpar banks and absorb the exchange charges. The present situation tended to insulate the nonpar banks from member bank competition; the requirement that member banks pay checks at par placed them at a distinct economic disadvantage.

Governor Mitchell was of the view that the Board should study whether, all things considered, it might not be the best course to make a change in the Board position to correspond with that of the Federal Deposit Insurance Corporation. He suggested that the Board meet with Chairman Randall and Director Sherrill for the purpose of discussing the problem.

Mr. Hexter then commented on telephone conversations with an officer of a national bank in Atlanta indicating that certain leading national banks in that area, despite the Comptroller's letter, were deferring absorption of exchange charges in the hope that the System would take a strong stand on the matter. The inference was that such a stand would have a restraining effect on other national banks in the

Sixth District. Mr. Fauver added that President Patterson of the Atlanta Reserve Bank also had called on the matter.

On the basis of the foregoing discussion, Governor Robertson suggested that the Board consider (1) sending a letter to Secretary Fowler relating to the Comptroller's disregard of the "Dillon" procedure, and (2) arranging a meeting with the Federal Deposit Insurance Corporation for the purpose of having a complete discussion of the absorption of exchange question.

Governor Robertson then withdrew from the meeting.

There followed comment on the suggestions made by Governor Robertson, during which Governor Brimmer expressed concern that the Board not act in a manner that would jeopardize the legislation said to be under consideration in Minnesota, and possibly also South Dakota, to abolish the charging of exchange. Also, he felt it important to consider carefully the effect any change in Board position might have on System membership.

Governor Maisel said that he was in favor of meeting with the Federal Deposit Insurance Corporation in an effort to resolve the exchange absorption problem one way or the other, but he suggested that release of any statement be postponed, particularly in view of the reported developments in Minnesota. He would also favor sending a letter to the Secretary of the Treasury calling attention to the Comptroller's August 23 communication, but he would hope that the letter would be confined to a recitation of the facts and a request that some action be taken by the Secretary to guard against recurrence of such situations.

Governor Mitchell felt it would be helpful before the meeting with the Corporation for the other members of the Board to have an opportunity to read the Jessup dissertation and a staff analysis of its salient points.

Following further discussion, it was agreed that a draft of letter to the Secretary of the Treasury would be prepared by the staff along the lines suggested and that arrangements would be made for a meeting with the Federal Deposit Insurance Corporation. It was understood that copies of the Jessup dissertation would be obtained and that the Division of Research and Statistics would prepare a summary of the document for the members of the Board.

Public Bank. Mr. Leavitt informed the Board of the reported status of negotiations pertaining to a possible merger of Public Bank of Detroit, Detroit, Michigan, into Bank of the Commonwealth, also of Detroit.

Meeting on Retirement System. Governor Maisel referred to a contemplated meeting of the Board with an Ad Hoc Committee of Trustees of the Retirement System of the Federal Reserve Banks, presently scheduled for September 14, 1966. He raised the question whether it might be appropriate to postpone the meeting to a date when there was greater certainty that all of the members of the Board could be present, and it was understood that the question of prospective attendance would be explored further by the Secretary.

Secretary's Note: It was subsequently decided, with Governor Maisel's concurrence, that the meeting would be postponed.

The meeting then adjourned.

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

Transfer

Carolyn Marie Nesbit, from the position of Stenographer in the Division of Personnel Administration to the position of Stenographer in the Division of Examinations, with no change in basic annual salary at the rate of $4,269, effective upon assuming her new duties.

Acceptance of resignations

Rudolph Keyes, Summer Trainee, Division of Administrative Services, effective the close of business September 2, 1966.

C. Anthony Mack, Summer Trainee, Division of Administrative Services, effective the close of business September 2, 1966.

Merritt Sherman

Secretary

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

Item No. 1
9/6/66

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

September 6, 1966

Honorable K. A. Randall, Chairman,
Federal Deposit Insurance Corporation,
Washington, D. C. 20429

Dear Mr. Randall:

Reference is made to your letter of August 31, 1966, concerning the application of The Union Bank, Loogootee, Indiana, for continuance of deposit insurance after withdrawal from membership in the Federal Reserve System.

There have been no corrective programs urged upon the bank, or agreed to by it, which have not been fully consummated, and there are no programs that the Board would advise be incorporated as conditions of admitting the bank to membership in the Corporation as a nonmember of the Federal Reserve System.

Very truly yours,

(Signed) Karl E. Bakke

Karl E. Bakke,
Assistant Secretary.

TELEGRAM
LEASED WIRE SERVICE

Item No. 2
9/6/66

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON

September 6, 1966.

Waage - New York

Board approves granting of loan or loans on gold up to a total of $13 million by the Federal Reserve Bank of New York to Banco de la Republica (Colombia) on terms described in your wire of September 1, 1966, and requests that you inform the Bank of the Republic that no renewal thereof at the expiration of the 90 day term will be considered.

(Signed) Merritt Sherman

Sherman