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Minutes for September 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 Friday, September 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. Daane
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. Fauver, Assistant to the Board
Mr. Solomon, Director, Division of Examinations
Mr. Leavitt, Assistant Director, Division of Examinations
Mr. Furth, Consultant
Mr. Morgan, Staff Assistant, Board Members' Offices

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

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

Money market review. Mr. Kelty commented on money market developments, Mr. Axilrod reviewed bank credit projections, and Mr. Ruckdeschel summarized developments in foreign exchange markets. Copies of distributed tables bearing on some of the matters discussed have been placed in the Board's files.

Members of the research divisions except Messrs. Brill, Partee, Sammons, Eckert, Ettin, and Keir then withdrew from the meeting and the following entered the room:

Mr. Cardon, Legislative Counsel
Mr. Hexter, Associate General Counsel
Mr. Hooff, Assistant General Counsel
Mr. Veenstra, Chief, Financial Statistics Section, Division of Data Processing
Mr. Forrestal, Senior Attorney, Legal Division
Mr. Egertson, Supervisory Review Examiner, Division of Examinations

Discount rates. The establishment without change by the Federal Reserve Bank of Boston on September 12, 1966, and by the Federal Reserve Banks of New York, Philadelphia, and San Francisco on September 15, 1966, of the rates on discounts and advances in their existing schedules was approved unanimously, with the understanding that appropriate advice would be sent to those Banks.

Approved letters. The following letters, copies of which are attached to these minutes under the respective item numbers indicated, were approved unanimously after consideration of background material that had been made available to the members of the Board:

	Item No.
Letter to Citizens Bank of Ada, Ada, Oklahoma, granting an extension of time to accomplish membership in the Federal Reserve System.	1
Letter to the Federal Reserve Bank of New York granting approval for the Bank to act as fiscal agent with respect to a proposed bond issue by the International Bank for Reconstruction and Development.	2

Item No.

Letter to the Chairman of the Legal and Monetary Affairs Subcommittee of the House Committee on Government Operations regarding bank credit cards. 3

Amendment to Regulation H (Item No. 4). Pursuant to section 9, paragraph 17, of the Federal Reserve Act, member State banks are required to file reports of affiliates, in connection with their call reports, except where the affiliate is itself a member bank or is an organization with respect to which the reporting requirement has been waived by the Board under authority of section 21, paragraph 9, of the Federal Reserve Act.

On the reverse side of the report form appears a section headed "Waiver of Requirement for Reports of Affiliates," which states that the requirement for such reports will be waived except where specified relationships exist. The text of this section was amended by Board action on August 30, 1966, to reflect changes necessitated by those provisions of Public Law 89-385 amending section 2(b) and repealing section 2(c) of the Banking Act of 1933.

There had now been circulated a memorandum from the Legal Division dated September 7, 1966, calling attention to the fact that when the Board's Regulation H (Membership of State Banking Institutions in the Federal Reserve System) was codified in 1938, reference therein to the circumstances under which the Board would waive reports of affiliates (pursuant to section 21 of the Federal Reserve Act) was

inadvertently omitted. Attached to the September 7 memorandum was a draft of amendment to section 208.9 of Regulation H, in form suitable for publication in the Federal Register, to incorporate therein the rules, as amended by the Board's August 30 action, regarding such waiver of reports.

The amendment was approved unanimously, effective August 31, 1966, and transmittal thereof to the Federal Register for publication was authorized. A copy of the amendment in the form submitted to the Federal Register is attached as Item No. 4.

Report on competitive factors. There had been distributed a draft of report to the Federal Deposit Insurance Corporation on the competitive factors involved in the proposed merger of Hawaiian Trust Company, Ltd., Honolulu, Hawaii, with Bank of Hawaii, also of Honolulu.

Following adoption of an editorial change suggested by Governor Robertson, the report was approved unanimously for transmittal to the Corporation in a form in which the conclusion read as follows:

> There is no significant competition existing between Hawaiian Trust Company, Ltd., and Bank of Hawaii. The proposed merger would eliminate potential for competition between these two institutions in the event Bank of Hawaii were to establish a trust department, pursuant to Act 273 of the Sessions Laws of Hawaii.

Revision of report on commercial and industrial loans by industry. There had been distributed a memorandum from the Division of Research and Statistics dated September 13, 1966, proposing a revision of the report on commercial and industrial loans by industry

(Form FR 416a) for use commencing the first Wednesday in January 1967, subject to approval of the revised form by the Bureau of the Budget.

The memorandum noted that the report in question was solicited from a selected group of banks participating in the Board's weekly reporting member bank series to supplement the basic data in that series with detailed information concerning industrial and commercial loans. The proposed revisions, as specified in the memorandum, were in the areas of coverage, content, and maturity. The proposals had received unanimous endorsement from the Reserve Banks, except that a minority of Banks opposed the request for maturity breakdowns on grounds of reporting burden, respondent relationships, and doubt as to the value of obtaining the statistics. The Division of Research and Statistics felt that the reporting burden would not be too great and that the analytical benefits of the data would be quite substantial.

Following explanation of the background and nature of the proposed changes by Mr. Ettin, whose comments were based essentially on the Division's memorandum, the proposed revision of the report was approved unanimously, with the understanding that the staff would obtain clearance from the Bureau of the Budget.

H.R. 14026. There had been distributed, on a limited basis, a memorandum from Mr. Partee dated September 15, 1966, summarizing a discussion held on September 14 between Governor Robertson, Chairman Randall (Federal Deposit Insurance Corporation), and Chairman Horne

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(Federal Home Loan Bank Board) concerning H.R. 14026. This bill would, among other things, provide for more flexible regulation of maximum rates of interest or dividends payable by banks and mutual thrift institutions on deposits or share accounts.

The memorandum recited three alternative courses of regulatory action that might be taken following enactment of the legislation:

1. Roll back interest rate ceilings to a maximum of 5 per cent for commercial banks and mutual savings banks, and to 5-1/4 per cent for savings and loan associations. Passbook rates for the banks would be retained at 4 per cent, but there would be no similar limitation on the specialized institutions (within the 5 per cent and 5-1/4 per cent ceilings) to establish any particular passbook rate differential.

2. Establish a maturity structure of permissible rates within an over-all ceiling of 5 per cent for the banks and 5-1/4 per cent for the S & L's. On passbook accounts, the ceiling would be 4 per cent for commercial banks and 4-1/2 per cent for S & L's (a specific passbook ceiling for the mutuals was not discussed). For consumer-type bank CD's, the ceilings would be 4 per cent on 90 days and under, 4-1/2 per cent on 91-180 days, and 5 per cent for 6 months or more. Savings and loans could have ceilings 1/4 per cent higher in each of these maturity classes, but for practical purposes they probably would use only the 6-month 5-1/4 per cent option for their existing investment certificate instruments. (Mr. Horne said that 3-year bonus accounts would be abolished under this proposal.)

3. Combine a roll-back in the top posted rates with a temporary freeze on rates lower than the new ceiling currently being offered. The roll-back ceilings would be the same as those specified under option 1--5 per cent for the banks and 5-1/4 per cent for the savings and loans. The freeze on existing rates below those levels would apply to payments on balances through the first quarter of 1967. A procedure for permitting special increases in hardship cases--where an institution had been caught below the prevailing rate levels in its market area--would be contemplated for each of the three types of institutions.

In addition, the following observations were made:

> Regardless of the option chosen--whether one of these three or another--a general question yet to be decided is whether the West Coast savings and loans should be permitted an extra margin in recognition of their historically higher rate levels and in order to attract and hold funds from the East. Mr. Horne maintains that such a premium is needed, and recommends that associations in California, Nevada, Alaska, and perhaps Hawaii be permitted to pay a top rate of 5-1/2 per cent rather than 5-1/4 per cent. The question is whether this should be agreed to, and how it would affect the West Coast banks if they are limited to the national ceiling of 5 per cent.
>
> The views of the group seemed strongly directed to defining consumer-type time deposits as all time deposits of less than $100,000. Mr. Randall suggested that perhaps the figure should be higher--$250,000 or $500,000--and Mr. Horne said that he had been thinking in terms of $100,000 but would have no objection to a higher figure. It was agreed that the $100,000 figure had special meaning, however, since it had been widely used in Congress and by Administration spokesmen.

Governor Robertson observed that the proposals in the memorandum were in the process of being evaluated by the Division of Research and Statistics and that they were being presented to the Board at this time not for a decision on which would be most acceptable, but rather as a point of reference for developing any additional suggestions that might appear to merit consideration in further discussions between representatives of the agencies next week.

Governor Daane commented, with respect to the discretionary authority the Board would have under the legislation to set maximum rates of interest based on size of deposit, that a North Carolina banker who was a member of a banker group that visited the Board

yesterday indicated that imposition of a 5 per cent ceiling on certificates of deposit under $100,000 would cause a substantial run-off of funds as outstanding certificates matured, and that his bank alone might lose $20 million of such deposits.

Governor Brimmer agreed that a statement to such effect had been made, with further indication--although the comments were not entirely clear--that a roll-back of the maximum rate on such instruments to 5 per cent would cause an attrition estimated at approximately 10 per cent. He added that such a rate of attrition would appear roughly comparable to that experienced by large money center banks under the present 5-1/2 per cent Regulation Q ceiling.

Governor Daane then suggested that alternative actions might be explored, such as a cutoff at $50,000 or preferably $25,000, instead of $100,000.

Governor Mitchell offered a proposal that, since the Congressional motivation underlying the pending legislation was to halt the "rate war" between depositary-type financial institutions, it would seem logical to apply a 5 per cent ceiling on certificates under $100,000 to new customers only, allowing banks the option of utilizing the present 5-1/2 per cent time deposit ceiling to encourage existing customers to leave their funds on deposit. Such an approach would have the virtue of permitting banks to forestall a run-off of existing passbook savings accounts occasioned by more attractive rates available elsewhere and should diminish the flows of funds about which the Congress was concerned.

In response to a question whether it was contemplated that the proposal would embrace funds represented by additions to existing accounts, or only deposits on hand as of the effective date of the new regulatory provisions, Governor Mitchell commented that he had no strong feeling in that regard. His concern was that medium-size banks have access to a defense against inroads on their deposits through the ability to pay 5-1/2 per cent on time accounts, if necessary, to retain existing customer relationships.

Governor Maisel concurred in the principle underlying Governor Mitchell's suggestion. However, he would prefer to see that principle implemented by permitting the present 5-1/2 per cent ceiling rate to be extended only to funds on deposit with a bank as of the date of the new regulations, rather than to base availability of that rate upon whether a customer relationship existed on such date. He also felt that a freezing of existing rates on time deposits, regardless of level, would be undesirable, since some of those rates were unrealistically low in light of developing competitive pressures.

Governor Mitchell indicated that he would be willing to accept Governor Maisel's modification of his suggestion.

There followed a brief colloquy concerning the Congressional intent underlying the proposed legislation, in the course of which Mr. Cardon expressed the opinion that, while the general objective was to bring about a reduction of interest rates, in the Board's area of

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responsibility a 5 per cent ceiling on consumer-type time deposits would be regarded as appropriate, with a $100,000 limitation to distinguish consumer-type certificates from money market instruments.

Governor Daane commented that there was no evidence that $100,000 was the actual line of demarcation between consumer-type CD's and those that were essentially money market instruments. He again suggested that consideration be given to a 5 per cent, $25,000 formula.

Governor Robertson noted that the Senate Committee report had stressed the distribution of funds between banks and savings and loan associations. Under the existing rate patterns, savings and loan share accounts had suffered much more in the past six months than bank time and savings deposits, and the Congress was trying to even this out.

Governor Robertson also noted that although the $25,000 cutoff mentioned by Governor Daane might be more reasonable than a $100,000 cutoff, any figure that was picked would necessarily be arbitrary. However, the $100,000 figure would have some backing in the sense that it had been so prominent in the legislative discussions, and apparently it would be acceptable to the savings and loans.

Governor Mitchell agreed that the Board should fasten on the $100,000 figure that had been so prominent in all of the discussions.

Governor Brimmer said that was why he had suggested that the Board's action be kept as simple as possible by establishing a ceiling

of 5 per cent on CD's under $100,000. The Board might with benefit consider the Maisel proposal whereby accounts on the books at present rates could be rolled over, but the 5 per cent, $100,000 formula would hopefully achieve agreement on the part of the other agencies so as to permit an announcement before September 28.

Governor Maisel commented that the Home Loan Bank Board should not be asked to roll back savings and loan rates. The Board of Governors should not, in consultations, support any attempt to achieve a roll-back in that area. Governor Mitchell expressed agreement, and Governor Robertson pointed out that under the statute each agency must make its own decision after consulting with the other agencies.

Governor Daane then said that if action was called for, he would favor a simple action involving a 5 per cent ceiling, with his preference for the cutoff still being $25,000. Mr. Brill noted that if the $100,000 figure was not right, an action by the Board establishing a cutoff at that level would tend to legitimatize it, and Governor Daane repeated his observation that it did not distinguish money market instruments from consumer investments.

Governor Mitchell agreed that the impact of whatever might be done was uncertain. At the same time, action was expected by the Congress. Under all the circumstances, he felt that the psychological acceptance of $100,000 as the dividing line was so firmly entrenched that adherence to that figure would probably have the least unsettling effect. He would accept it despite some personal qualms.

Discussion then turned to the matter of the amount of lead time desirable between announcement of the regulatory action, when taken, and its effective date.

Governor Brimmer felt, in retrospect, that more time should have been allowed for banks to adjust to the Board's announcement on July 15, 1966, of a reduced maximum rate of interest on multiple maturity time deposits, and he believed a greater lead time would be desirable in this instance.

Governor Mitchell noted that if the new regulations were to contain a "grandfather clause" it would be necessary to provide for an immediate effective date in order to avoid a rush of advertising and promotional activity on the part of banks. If no "grandfather clause" was included, it would seem desirable to provide a reasonable adjustment period.

Other expressions were along somewhat the same lines, and comments were made that prompt announcements by the regulatory agencies would be desirable. Governor Robertson indicated that he intended to meet again with Messrs. Randall and Horne early next week, and he expressed the hope that action could be taken soon thereafter.

Cease and desist bill. Mr. Cardon reported on a telephone call he had received yesterday from a member of Congressman Ashley's staff who inquired as to the Board's position with respect to a proposal by the United States Savings and Loan League for an amendment to S. 3158

(the so-called "cease and desist" bill) providing for an increase in Federal deposit and share account insurance from $10,000 to $20,000. Indications were that Mr. Ashley was thinking of proposing an increase to $15,000.

By way of background, Mr. Cardon noted that in 1963 the Administration, with Board concurrence, proposed an increase in deposit insurance to $15,000, in a bill also containing provisions designed to improve savings and loan liquidity and to deter conflicts of interest at both banks and savings and loan associations.

In discussion of this question a consensus developed that Congressman Ashley should be advised that while the Board would have no strong objection to an increase in Federal deposit and share account insurance to $15,000, the Board would hope no such provision would be added to S. 3158. That bill had already passed the Senate, and to introduce an extraneous issue at this point might diminish the chances for its passage.

It was understood that Mr. Cardon would communicate the foregoing views to Congressman Ashley's office.

All staff members except Messrs. Sherman, Kenyon, and Fauver then withdrew from the meeting.

Director appointment. Chairman Bemis of the Federal Reserve Bank of Minneapolis having indicated that he would not be available for reappointment as a Class C director, it was agreed unanimously to appoint

Joyce A. Swan, Executive Vice President and Publisher of the Minneapolis Star and Tribune, Minneapolis, Minnesota, who was currently serving as a Class B director, as a Class C director for the three-year term beginning January 1, 1967, and to designate Mr. Swan as Chairman and Federal Reserve Agent of the Bank for the year 1967, with compensation in an amount equal to the fees payable to any other director of the Minneapolis Bank for equivalent time and attendance to official business. It was understood that Mr. Swan's appointment as Class C director and designation as Chairman and Federal Reserve Agent would not be announced publicly by the Board until the end of this year, but that the Reserve Bank would be free to proceed with arrangements for the election of a successor to Mr. Swan as a Class B director.

> Secretary's Note: It having been ascertained that Mr. Swan would accept the appointment as Class C director and designation as Chairman and Federal Reserve Agent for 1967, a wire of appointment and designation was sent to him on September 19, 1966.

Mr. Fauver then withdrew from the meeting.

Retention of Mr. Chase on consultant basis. The Board approved an arrangement whereby G. Howland Chase, retired Assistant General Counsel, would be retained on a consultant basis for a temporary period, possibly in the area of three months, to assist in certain activities currently in process in the Legal Division, with the terms of compensation to be subject to approval by Governor Shepardson.

> Secretary's Note: Governor Shepardson subsequently approved compensation at the rate of $65 for each day worked.

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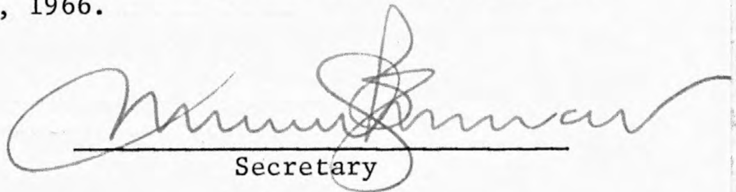
Request for leave of absence without pay. Mr. Brill was called back into the meeting and outlined the circumstances involved in a request by a member of the Board's staff for an extended leave of absence without pay in order that he might accept a post outside the United States. Various possible alternatives were considered, and it was understood that Mr. Brill would discuss the matter further with the staff member concerned on the basis of the views expressed, which among other things touched upon the problem of carrying on the functions for which the staff member was currently responsible.

The meeting then adjourned.

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

Memorandum from Mr. Holland, Adviser to the Board, dated September 9, 1966, recommending that arrangements be made with the Federal Reserve Bank of Chicago for William Hocter to spend some time, partly in Washington, from early October through the end of 1966 in connection with the current study of the discount mechanism, it being understood that the Chicago Bank would assume all expenses incident to the assignment.

Memorandum from the Legal Division recommending acceptance of the resignation of Jane T. Fletcher, Stenographer in that Division, effective the close of business September 16, 1966.



Secretary

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

Item No. 1
9/16/66

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

September 16, 1966

Board of Directors,
Citizens Bank of Ada,
Ada, Oklahoma.

Gentlemen:

The Board of Governors of the Federal Reserve System extends to April 13, 1967, the time within which admission to membership in the Federal Reserve System may be accomplished by Citizens Bank of Ada, Ada, Oklahoma.

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. 2
9/16/66

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

September 19, 1966

Mr. H. A. Bilby, Vice President,
Federal Reserve Bank of New York,
New York, New York. 10045

Dear Mr. Bilby:

This refers to your letter of September 9, 1966, and enclosures, concerning the proposed issue by the International Bank for Reconstruction and Development of its Two-Year Bonds of 1966, due October 1, 1968, in an aggregate principal amount to be determined by designated officers of the International Bank but not to exceed $100 million. The International Bank has informed you of its intention to appoint your Bank as its fiscal agent in connection with this bond issue, and in this regard you state that it is proposed to amend Schedule A of the Fiscal Agency Agreement, dated as of February 6, 1950, between the International Bank and your Bank to include the bonds in question.

The Board of Governors approves of your Bank acting as fiscal agent with respect to the proposed bond issue, and approves the execution and delivery by your Bank of an agreement with the International Bank substantially in the form of the draft of Supplement No. 29 to the Fiscal Agency Agreement enclosed with your letter.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

Item No. 3
9/16/66

OFFICE OF THE CHAIRMAN

September 20, 1966

The Honorable Dante B. Fascell, Chairman,
Legal and Monetary Affairs Subcommittee
of the Committee on Government Operations,
United States House of Representatives,
Washington, D. C. 20515

Dear Mr. Fascell:

This refers to your letter of July 20, 1966, in which you requested our comments on the danger of losses in the misuse of bank credit cards and on the growth and implications of these new credit devices. As indicated in the acknowledgment of receipt of your inquiry, we forwarded a copy of your letter to each of the System's 12 Reserve Banks and requested information or comments which might be helpful to your Subcommittee. The views of the Reserve Banks are incorporated in the following comments.

Bank credit card plans are by no means a recent innovation in the field of consumer credit, but only recently has their usage become widespread. In the late 1940's a few banks experimented with charge account plans using scrip rather than a credit card. Scrip, however, had many disadvantages and was gradually replaced by the credit card system.

The introduction of credit cards encouraged more banks to investigate the profit potential of such service and in the early 1950's several banks established local charge account plans. However, because of the rather substantial cost required to establish and operate such plans, many of these banks, both large and small, discontinued the service. The investment in processing equipment was far more than many anticipated and the need for specialized personnel had often been overlooked. The initial advertising and promotional expense required to establish the plan in the community and build volume to a profitable level was too costly for others. Moreover, in their efforts to gain community acceptance, some banks lowered their customary credit standards and indiscriminately mailed credit cards without making proper credit investigation. Large volumes of poor quality loans developed in some banks, resulting in substantial losses. Although fully cognizant of their losses, both from operations and bad loans, many continued the service until they could withdraw with a minimum loss of prestige in the community. Even today some continue to operate uneconomical plans but, because of their contacts with a greater number of customers, they regard their plans as a normal part of their business development and customer relations programs.

It was not until about 1958 that major banks, including the largest in the United States entered the credit card field. Several of these banks have been able to expand their card systems substantially which today are on a profitable basis. Size alone, however, has not meant success. One of the nation's largest banks could not sustain the needed growth of its plan and after several years of unprofitable operations sold its credit card plan to a nonbanking organization. On the other hand, several small banks have been enjoying highly profitable operations since the early 1950's.

Notwithstanding the sometimes conflicting reports on the profitability of bank credit card plans, several banks are evidencing more and more interest in entering this field of customer service. Some have purchased existing nationwide plans in recent months while others are currently establishing their own such plans or joining national syndicates. The latter pooling arrangement is particularly attractive to many smaller banks since the initial promotional expenses are spread among the participating institutions.

A variation of the credit card plan, a check credit device, is also becoming more popular because it is considered by some to have advantages over the credit card plan. Under this device a customer obtains a revolving line of credit, similar to that granted under the card plan, and is issued a book of checks to use for any purchase anywhere.

The experience of System examiners with bank credit card and check credit plans has been somewhat limited. Of the some 1,371 State member banks which they examine only a few are operating some form of credit card plan. However, the consensus is that there is every indication that this form of credit will probably expand in the near future.

Bank credit card and check credit plans are essentially another form of retail instalment credit. The plans can be an important adjunct to a bank's consumer instalment operations and can be of substantial assistance in developing customer relationships. As long as the bank observes the generally accepted credit standards which are applied to other forms of instalment credit, there appears to be little danger of substantial loss from the misuse of credit cards. It is possible, of course, that regardless of how well a plan is operated, a cardholder could lose or have his card stolen. As reported by System examiners, and attested to by several State member banks which operate plans, relatively simple precautions such as requiring merchants to obtain the bank's approval for credit beyond a specified amount tend to limit losses arising from such misuse of credit cards. Losses of this type are reported by these banks to have been readily absorbed out of income from their plans.

As indicated earlier, it is possible that bank credit cards could be misused in those instances where a bank, in an effort to develop an adequate volume of business, lowers its customary credit standards and indiscriminately distributes cards. However, as banks have gained experience in the handling of credit card plans, they have become aware of the importance of maintaining their usual credit standards in issuing credit cards and have become more selective with their cardholders. Misusage because of indiscriminate distribution of credit cards does not now appear to be a problem. The few plans that are in operation in State member banks appear to be properly managed and our examiners have found little reason to criticize them; such criticism, if any, has not been related to the misuse of credit cards. Of course many of the largest banks which operate credit card plans are nationally chartered and thus primarily supervised by the Comptroller of the Currency.

We have not had under review any of the various new systems being introduced which extend credit card plans beyond local or regional areas by a bank or group of banks. We have, however, attempted to remain generally familiar with the nature of these plans, and we continue to observe developments in this area.

If and when an examination of a State member bank discloses that it has established a credit card plan or entered into such an arrangement with other banks, examiners are to explore carefully the details of the plan, make a careful assessment of the exposure involved, appraise the adequacy of safeguards in effect, and make such suggestions and recommendations as deemed appropriate in the circumstances. As with the introduction of other forms of credit, the examiner would be expected to insist on sound credit policies in the issuance of credit cards, appropriate safeguards and internal controls, and the establishment of ample reserves for losses.

Sincerely yours,

(Signed) Wm. McC. Martin, Jr.

Wm. McC. Martin, Jr.

TITLE 12--BANKS AND BANKING

Item No. 4
9/16/66

CHAPTER II--FEDERAL RESERVE SYSTEM

SUBCHAPTER A--BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

[Reg. H]

PART 208--MEMBERSHIP OF STATE BANKING INSTITUTIONS IN THE FEDERAL RESERVE SYSTEM

Waiver of Reports of Affiliates

1. Effective August 31, 1966, section 208.9 is amended by adding the following subsection:

§ 208.9 Publication of reports of member banks and their affiliates.

* * * * *

(c) Waiver of reports of affiliates. (1) Pursuant to section 21 of the Federal Reserve Act (12 U.S.C. 486), the Board of Governors of the Federal Reserve System waives the requirement for the submission of reports of affiliates of State bank members of the Federal Reserve System, except:

(i) When indebtedness, if any, of the affiliate to the member bank has been carried for more than 6 months in the 12 months preceding the report date as an asset on the bank's books at a value in excess of $5,000 or 1 per cent of the bank's capital and surplus, whichever is the greater, regardless of whether the affiliate is so indebted on the report date: Provided, That any indebtedness of the affiliate to the member bank fully secured by direct obligations of the United States Government or by obligations fully guaranteed by the United States Government may be disregarded in determining whether or not the indebtedness of the affiliate is in excess of the limitations prescribed herein.

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(ii) When, on the report date, the affiliate is indebted to the member bank, or the member bank owns obligations of, or stock or other evidences of ownership in, the affiliate, and the aggregate amount of such indebtedness, obligations, stock, or other evidences of ownership is carried as an asset on the bank's books at a value in excess of $5,000 or 1 per cent of the member bank's capital and surplus, whichever is the greater: Provided, That any indebtedness of the affiliate to the member bank fully secured by direct obligations of the United States Government or by obligations fully guaranteed by the United States Government may be disregarded in determining whether or not the indebtedness of the affiliate is in excess of the limitations prescribed herein.

(2) The Board of Governors of the Federal Reserve System also waives the requirement for the submission of reports of affiliates in all cases (i) where the affiliate relationship is based solely on ownership or control of any voting shares of the affiliate by a member bank as executor, administrator, trustee, receiver, agent, depositary, or in any other fiduciary capacity, except where such shares are held for the benefit of all or a majority of the stockholders of such member bank, and (ii) where the affiliate relationship is based solely on the fact that a majority of the affiliate's directors, trustees, or other persons exercising similar functions are directors of any one member bank, except where they constitute more than one-fourth of the directors of the member bank.

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(3) The above provisions with respect to the waiving of the requirement for submission of reports of affiliates are subject to change whenever deemed advisable by the Board of Governors of the Federal Reserve System in order to require the submission of reports which are necessary to disclose fully relations between member banks and their affiliates and the effect thereof upon the affairs of member banks.

2a. The purpose of this section is to incorporate into this Part the long-standing rules of the Board of Governors with respect to waiving reports of affiliates of State member banks. Such rules were originally established in 1935 shortly after the enactment of the Banking Act of 1935, which authorized the Board of Governors to waive the requirement of the Banking Act of 1933 relating to submission of reports by affiliates of State member banks (12 U.S.C. 334 and 486).

b. The requirements of section 4 of the Administrative Procedure Act with respect to notice, public participation, and deferred effective date were not followed in connection with this amendment. The provisions of this section were inadvertently omitted from the Board's initial codification of its regulations in 1938. Because this action corrects the previous omission and does not constitute a new rule by the Board, the requirements of notice, public participation, and deferred effective date are considered inapplicable.

(12 U.S.C. 248(i) and 486.)

Dated at Washington, D. C., this 31st day of August, 1966.

By order of the Board of Governors.

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.

(SEAL)