

FEDERAL RESERVE BANK  
OF NEW YORK

[ Circular No. 7042 ]  
[ November 22, 1972 ]

EXTENSIONS OF CREDIT BY FEDERAL RESERVE BANKS  
Proposed Revision of Regulation A

To All Member Banks in the  
Second Federal Reserve District:

The Board of Governors of the Federal Reserve System is inviting public comment on a proposal to revise its Regulation A governing the extension of credit by Federal Reserve Banks. This is the regulation under which credit is made available to member banks.

The regulation would be revised to permit banks with significant seasonal needs and without reasonably reliable access to certain other sources of funds because of size or special circumstances, to have access to Federal Reserve credit on a longer term basis and with greater assurance than heretofore. There would be no other substantial change from the present rules for borrowing at the discount window. The provision for a virtually automatic basic borrowing privilege for each bank — widely discussed following publication of a Federal Reserve study in July 1968 — is receiving further study.

The proposed regulation would base the calculation of a bank's seasonal need for funds on patterns of movement in deposits and loans. The seasonal decline in a bank's available funds (deposits minus loans) would have to persist for at least 8 weeks and recur each year at about the same time. The amount and timing of the credit would be arranged in advance by each applying bank with the Reserve Bank's lending officer, and would ordinarily be limited to the amount by which the seasonal need exceeds 5 per cent of the member bank's average deposits in the preceding year.

The proposed regulation would also liberalize in certain respects the requirements for eligibility of paper that can be accepted by the Federal Reserve Banks as collateral for advances at the basic discount rate.

Printed on the following pages are (a) the text of a statement issued today by the Board of Governors of the Federal Reserve System regarding the proposed revision of Regulation A, and (b) the text of the proposed revision. Comments on the proposal should be submitted by February 28, 1973, and may be sent to our Credit and Discount Department.

In the Head Office territory, questions with respect to the proposal may be directed to Herbert H. Ruess, Manager, Credit and Discount Department (Telephone No. 212-732-5700, Extension 8091); in the Buffalo Branch territory, please call Ronald B. Gray, Assistant Vice President and Cashier (Telephone No. 716-853-1700, Extension 204).

Additional copies of this circular will be furnished upon request.

ALFRED HAYES,  
*President.*

## Statement of the Board of Governors of the Federal Reserve System

The Board of Governors of the Federal Reserve System today proposed revision of its rules for lending to member banks designed, primarily, to assist smaller banks in meeting the seasonal borrowing needs of their communities.

The proposal is a further step in a program by the Board to implement recommendations for revision of the Board's Regulation A, governing lending by Federal Reserve Banks. The recommendations were made by a System task force following a three-year study of Federal Reserve lending practices and policies. Certain recommendations resulting from the study have previously been adopted as part of the System's procedures. As suggested by the study, the changes now proposed would modernize and simplify the Regulation. The proposed changes were published for comment through February 28.

In connection with the proposed revision of Regulation A, the Board said:

The rules for Federal Reserve lending apply to all banks that are members of the Federal Reserve System. Member banks hold nearly 80 per cent of all commercial bank deposits.

In proposing revision of Regulation A, however, the Board is particularly interested in encouraging increased use of the resources of member banks serving communities with seasonal needs for funds, such as communities affected by trades or industries with pronounced seasonal operating patterns, and agricultural and resort areas.

Close to half of all member banks — more than 2,400 of the System's approximately 5,700 commercial banks — are estimated, on the basis of historical lending and deposit patterns, to have substantial seasonal calls for credit in their communities. Of these, over 2,000, or more than 90 per cent of the seasonally impacted banks, are banks with no more than \$50 million total deposits.

The seasonal borrowing privilege now proposed is meant to enhance the ability of member banks to serve the credit needs of their communities and areas.

No change in the stance of monetary policy, in either the short or the long run, is intended or expected to result from the proposed revision of Regulation A.

The proposed revision is an outgrowth of recommendations made in a System report entitled "Reappraisal of the Federal Reserve Discount Mechanism" and published in July of 1968 by a System task force headed by Federal Reserve Board Governor George W. Mitchell. In the intervening time, the Federal Reserve has incorporated into its procedures the substance of the recommendations of the task force relating to emergency credit to member and nonmember deposit type institutions. The proposal announced today would establish a new seasonal borrowing privilege in line with task force recommendations. The major remaining recommendation, for a short-term "basic" borrowing privilege, is receiving further study.

Some details of the proposed new Federal Reserve lending rules follow:

### *The Seasonal Borrowing Privilege*

This new lending arrangement would be available to member banks that lack reasonably reliable access to national money markets. It is intended to assist them in meeting seasonal needs for funds arising from a recurring pattern of anticipated movements in deposits and loans that persists for at least eight weeks. An eligible bank would be required under this arrangement to provide part of its own seasonal needs — up to 5 per cent of its average total deposits in the preceding calendar year. It could obtain its additional seasonal needs by borrowing from the Federal Reserve. The bank would be required to arrange in advance with its Reserve Bank for seasonal borrowing. Credit under this arrangement would be extended to member banks for periods of up to 90 days at a time. Under ordinary circumstances, a Federal Reserve Bank will be prepared to grant renewals extending the borrowing for the duration of the demonstrated seasonal need.

### *Eligibility requirements*

As part of the proposed revision of Regulation A, a number of technical and clarifying changes would be made in provisions regarding the eligibility of paper that can be accepted by the Federal Reserve Banks as collateral for advances at the discount rate. For example, the new rules would eliminate the present prohibition against lending on paper drawn for the purchase of permanent or fixed investments. Consequently, the note of a home mortgage lender would be eligible as a basis for a Federal Reserve loan to a member bank if that note has a maturity of not more than 90 days. In addition, the revised Regulation would make it clear that a note given for the purchase of services is drawn for a commercial purpose, thus making such a note eligible as collateral for Federal Reserve credit to member banks and permitting increased assistance to consumer lenders.

### *Adjustment credit*

Under the revised regulation, a Reserve Bank would continue, as at present, to extend credit to a member bank to assist in adjusting to temporary requirements for funds, or to cushion more persistent outflows, pending an orderly adjustment of the member bank's assets and liabilities. Examples are where individual banks must meet unexpected loan demands, or adjust to a drain of deposits, or other circumstances that temporarily outstrip a bank's internal resources. There is no change in the principle that the Federal Reserve lending to member banks is not a substitute for capital.

## Emergency lending

The revised rules would reaffirm the System's readiness to extend credit available in emergency situations to other financial institutions, corporations, partnerships, and individuals on the security of Government obligations.

Separately from Regulation A, in exceptional circumstances, the Federal Reserve Act makes possible emergency lending to others than member banks, on the basis of any paper eligible for discount at a Federal Reserve Bank.

### FEDERAL RESERVE SYSTEM

[12 CFR Part 201]

[Reg. A]

### ADVANCES AND DISCOUNTS BY FEDERAL RESERVE BANKS

#### Proposed Revision of Regulation A

The Board of Governors proposes to amend Part 201 by changing the heading to read "Extensions of Credit by Federal Reserve Banks"; deleting § 201.0; amending §§ 201.1, 201.2, 201.3, 201.4, 201.5, and 201.6; and by adding §§ 201.7 and 201.8 as set forth below.

The principal purposes of the proposed revision of the Board's Regulation A are (1) to make specific provision for extensions of seasonal credit; (2) to eliminate certain restrictions with respect to the eligibility of paper as collateral for Federal Reserve credit; and (3) to condense and simplify technical provisions of the Regulation. Short-term Federal Reserve credit would continue to be provided in accordance with present rules. No change in the posture of monetary policy in the short or long run would result from the adoption of the proposals.

The major impact of the new rules would be to improve the ability of banks to meet strong seasonal credit needs of their communities. Such seasonal credit would be provided to banks to accommodate intermediate-term recurring needs for funds over and above a threshold amount, for such amounts and duration as the applying member bank is able to demonstrate a need.

The new rules would include certain changes as to the eligibility of paper for discount or as security for Federal Reserve advances. The present Regulation makes ineligible any paper the proceeds of which are used for "permanent or fixed investments of any kind, such as land, buildings or machinery, or for any other fixed capital purpose." This provision, which is not statutory, would be omitted, so that paper given for such purposes would be eligible for discount or as collateral for advances if it meets the 90-day maturity requirement of the law and if the funds are not used *merely* for investment purposes. The revision would also make it clear that paper given for the purchase of services, as well as tangible goods, would be eligible for discount and as collateral for advances.

Finally, the revision would condense, simplify, or clarify a number of technical provisions of the Regulation. For example, detailed limitations and conditions with respect to the discounting of bankers' acceptances would be replaced by a general para-

phrasing of statutory requirements regarding the types of bankers' acceptances eligible for discount; it would be made clear that the limitation on the amount of paper of one borrower that may be discounted applies in the same manner to both national and State member banks and to Reserve Bank advances at the discount rate as well as to discounts; detailed provisions regarding financial statements and other information would be eliminated; and there would be included a new section regarding the circumstances under which advances would be made to individuals, partnerships, and corporations other than member banks.

The revised rules would reaffirm the System's readiness to supply credit assistance to its member banks in general or isolated emergency situations. In addition, it would recognize that — in its role as lender of last resort — the Federal Reserve should be prepared, under emergency liquidity conditions, to provide certain types of credit assistance to financial institutions other than member banks.

This notice is published pursuant to section 553(b) of Title 5, United States Code, and § 262.2(a) of the Rules of Procedure of the Board of Governors.

To aid in the consideration of this matter by the Board, interested persons are invited to submit relevant data, views, or arguments. Any such material should be submitted in writing to the Secretary, Board of Governors of the Federal Reserve System, Washington, D.C. 20551, to be received not later than February 28, 1973.

Following receipt of these comments, the Board will weigh them in arriving at a final decision regarding the adoption of the proposed amendments.

#### PART 201 — EXTENSIONS OF CREDIT BY FEDERAL RESERVE BANKS

- Sec.
- 201.1 Authority and scope
  - 201.2 General principles
  - 201.3 Policy guidelines
  - 201.4 Advances to member banks
  - 201.5 Discounts for member banks

- 201.6 General requirements
- 201.7 Federal Intermediate Credit banks
- 201.8 Emergency credit for others

Authority: The provisions of this Part 201 issued under 12 U.S.C. 84, 248, 301, 330, 343-347, 347b, 347c, 348, 349, 351, 352, 361, 371, 372, 373, 374.

#### § 201.1 — Authority and scope.

This Part is issued under section 13 and other provisions of the Federal Reserve Act and relates to extensions of credit by Federal Reserve Banks.

#### § 201.2 — General principles.

(a) Extending credit to member banks to accommodate commerce, industry, and agriculture is a principal function of Reserve Banks. While open market operations and changes in member bank reserve requirements are important means of affecting the overall supply of bank reserves, the lending function of the Reserve Banks is an effective method of supplying reserves to meet the particular needs of individual member banks.

(b) The lending functions of the Federal Reserve System are conducted with due regard to the basic objectives of the Employment Act of 1946 and the maintenance of a sound and orderly financial system. These basic objectives are promoted by influencing the overall volume and cost of credit through actions affecting the volume and cost of reserves to member banks. Borrowing by individual member banks, at a rate of interest adjusted from time to time in accordance with general economic and money market conditions, has a direct impact on the reserve position of the borrowing banks and thus on their ability to meet the needs of their customers. However, the effects of such borrowing do not remain localized but have an important bearing on overall monetary and credit conditions.

(c) Federal Reserve credit is available on a short-term basis to assist member banks in meeting temporary requirements for funds and in meeting more persistent outflows pending an orderly adjustment of a member bank's asset and liability structure. Federal Reserve credit is also available for longer periods in order to assist member banks in meeting significant seasonal needs. Federal Reserve credit is available to assist member banks in meeting emergency or unusual situations, such as may result from national, regional, or local difficulties or from exceptional circumstances involving only particular member banks. Emergency credit assistance may also be made available in exigent circumstances to others than member banks under such terms and conditions as may be specified. Federal Reserve credit is not a substitute for capital and ordinarily is not available for extended periods.

(d) Each Reserve Bank is required by law (1) to 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 (2) to give consideration to such information in determining whether to extend credit.

#### § 201.3 — Policy guidelines.

In conformity with the foregoing principles and the requirements and limitations of the Federal Reserve Act and this Part, Reserve Banks will ordinarily extend credit as follows:

(a) *Adjustment credit.* A Reserve Bank may, under such rules as may be prescribed, extend credit to a member bank to such extent as may be appropriate to assist in meeting temporary requirements for funds or to cushion more persistent outflows of funds pending an orderly adjustment of the member bank's assets and liabilities.

(b) *Seasonal borrowing privilege.* (1) Credit will also be extended to a member bank that lacks reasonably reliable access to national money markets to assist in meeting seasonal needs for funds arising from a combination of expected patterns of movement in its deposits and loans. Such seasonal credit will ordinarily be limited to the amount by which the member bank's seasonal needs exceed 5 per cent of its average total deposits in the preceding calendar year. It will be available if (i) the member bank has arranged in advance for such seasonal credit for the full period, as far as possible, for which the credit is expected to be required, and (ii) the Reserve Bank is satisfied that the member bank's qualifying need for funds is seasonal and will persist for at least eight consecutive weeks.

(2) In making such arrangements for seasonal credit, a Reserve Bank may agree to extend such credit for a period of up to 90 days,<sup>1</sup> subject to compliance with applicable requirements of law at the time such credit is extended. However, in the event that a member bank's seasonal needs should persist beyond such period, the Reserve Bank will normally be prepared to entertain a request by the member bank for further credit extensions under the seasonal credit arrangement.

(c) *Emergency credit.* A Reserve Bank may also extend credit (1) to any of its member banks in unusual or emergency circumstances, and (2) to individuals, partnerships, and corporations that are not member banks in emergency circumstances in accordance with § 201.8 of this Part if in its judgment credit is not practicably available from other sources and failure to obtain such credit would adversely affect the economy.

<sup>1</sup>As provided in the law and in this Part, the maturity of advances to member banks is limited to 90 days, except as provided in § 201.4(b) of this Part.

§ 201.4 — Advances to member banks.

(a) *Advances on obligations or eligible paper.* Reserve Banks may make advances to member banks for not more than 90 days if secured by obligations or other paper eligible under the Federal Reserve Act for discount or purchase by Reserve Banks.

(b) *Advances on other security.* A Reserve Bank may make advances to a member bank for not more than four months if secured to the satisfaction of the Reserve Bank, whether or not secured in conformity with § 201.4(a), but the rate on such advances shall be at least one-half of one per cent per annum higher than the rate applicable to advances made under § 201.4(a).

§ 201.5 — Discounts for member banks.

If a Reserve Bank should conclude that a member bank would be better accommodated by the discount of paper than by an advance on the security thereof, it may discount for such member bank any paper endorsed by the member bank and meeting the following requirements:

(a) *Commercial or agricultural paper.* A note, draft, or bill of exchange issued or drawn or the proceeds of which have been or are to be used (1) in producing, purchasing, carrying, or marketing goods in the process of production, manufacture, or distribution, (2) for the purchase of services, (3) in meeting current operating expenses of a commercial, agricultural, or industrial business, or (4) for the purpose of carrying or trading in direct obligations of the United States; provided that (i) such paper has a period remaining to maturity of not more than 90 days, except that agricultural paper (including paper of cooperative marketing associations) may have a period remaining to maturity of not more than nine months and (ii) the proceeds of such paper have not been and are not to be used merely for the purpose of investment, speculation, or dealing in stocks, bonds, or other such securities, except direct obligations of the United States.

(b) *Bankers' acceptances.* A banker's acceptance (1) arising out of an importation or exportation or domestic shipment of goods or the storage of readily marketable staples or (2) drawn by a bank in a foreign country or dependency or insular possession of the United States for the purpose of furnishing dollar exchange; provided that such acceptance complies with applicable requirements of section 13 of the Federal Reserve Act.

(c) *Construction paper.* A note representing a loan made to finance construction of a residential or farm building, whether or not secured by a lien upon real estate, which matures not more than nine months from the date the loan was made and has a period remaining to maturity of not more than 90 days, if accompanied by an agreement requiring some person

acceptable to the Reserve Bank to advance the full amount of the loan upon completion of such construction.

§ 201.6 — General requirements.

(a) *Information.* A Reserve Bank shall require such information as it deems necessary to insure that paper tendered as collateral or for discount is acceptable and meets any pertinent eligibility requirements and that the credit granted is used consistently with this Part.

(b) *Amount of collateral.* A Reserve Bank shall require only such amount of collateral as it deems necessary or advisable.

(c) *Indirect credit for nonmember banks.* Except with the permission of the Board of Governors, no member bank shall act as the medium or agent of a nonmember bank (other than a Federal Intermediate Credit bank) in receiving credit from a Reserve Bank and, in the absence of such permission, a member bank applying for credit shall be deemed to represent and guarantee that it is not so acting.

(d) *Limitation as to one obligor.* Except as to credit granted under § 201.4(b), a member bank applying for credit shall be deemed to certify or guarantee that as long as the credit is outstanding no obligor on paper tendered as collateral or for discount will be indebted to it in an amount exceeding the limitations in section 5200 of the Revised Statutes (12 U.S.C. 84), which for this purpose shall be deemed to apply to State member as well as national banks.

§ 201.7 — Federal Intermediate Credit banks.

A Reserve Bank may discount for any Federal Intermediate Credit bank (1) agricultural paper, or (2) notes payable to and bearing the endorsement of such Federal Intermediate Credit bank covering loans or advances made under section 202(a) of Title II of the Federal Farm Loan Act which are secured by paper eligible for discount by Reserve Banks. Any paper so discounted shall not have a period remaining to maturity of more than nine months or bear the endorsement of a nonmember State bank.

§ 201.8 — Emergency credit for others.

In emergency circumstances a Reserve Bank may extend credit for periods of not more than 90 days to individuals, partnerships, and corporations (other than member banks) on the security of direct obligations of the United States or any obligations which are direct obligations of, or fully guaranteed as to principal and interest by, any agency of the United States, at such rate in excess of the rate in effect at the Reserve Bank for advances under § 201.4(a) as its board of directors may establish subject to review and determination of the Board of Governors.