AN ANALYSIS OF CURRENT WRITTEN LOAN POLICIES FOR SECURED LOANS AT SAN FERNANDO VALLEY BANKS

A thesis submitted in partial satisfaction of the requirements for the degree of Master of Science in Business Administration

by

Albert Leslie Van Maele

June, 1968
The thesis of Albert Leslie Van Maele is approved:

Committee Chairman

San Fernando Valley State College

June, 1968
ACKNOWLEDGMENT

Sincere gratitude is hereby expressed to Professor Max Lupul and other staff members of the School of Business Administration and Economics at San Fernando Valley State College for their very valuable assistance and patience in the preparation of this work. Thanks are also due to those banking executives who gave so freely of their time to aid in the gathering of data.
# TABLE OF CONTENTS

<table>
<thead>
<tr>
<th>Section</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>ACKNOWLEDGEMENTS</td>
<td>iii</td>
</tr>
<tr>
<td>LIST OF TABLES</td>
<td>v</td>
</tr>
<tr>
<td>LIST OF ILLUSTRATIONS</td>
<td>vi</td>
</tr>
<tr>
<td>ABSTRACT</td>
<td>vii</td>
</tr>
<tr>
<td>Chapter</td>
<td></td>
</tr>
<tr>
<td>I. INTRODUCTION</td>
<td>1</td>
</tr>
<tr>
<td>II. THE STRUCTURE OF COMMERCIAL BANKING IN CALIFORNIA</td>
<td>8</td>
</tr>
<tr>
<td>III. OPINIONS OF LEADING BANKING EXECUTIVES ON POLICIES</td>
<td>22</td>
</tr>
<tr>
<td>IV. DATA ANALYSIS</td>
<td>31</td>
</tr>
<tr>
<td>V. SUMMARY AND CONCLUSION</td>
<td>54</td>
</tr>
<tr>
<td>APPENDIX A</td>
<td>58</td>
</tr>
<tr>
<td>APPENDIX B</td>
<td>61</td>
</tr>
<tr>
<td>BIBLIOGRAPHY</td>
<td>66</td>
</tr>
</tbody>
</table>
# LIST OF TABLES

<table>
<thead>
<tr>
<th>Table</th>
<th>Description</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Numbers and Types of U. S. Banks</td>
<td>9</td>
</tr>
<tr>
<td>2</td>
<td>U. S. Bank Deposits</td>
<td>10</td>
</tr>
<tr>
<td>3</td>
<td>Purpose and Principal Collateral of Bank Loans</td>
<td>20</td>
</tr>
<tr>
<td></td>
<td>Secured by Stocks and Bonds</td>
<td></td>
</tr>
<tr>
<td>4</td>
<td>Banks from which Data was Gathered</td>
<td>33</td>
</tr>
<tr>
<td>5</td>
<td>Banks Visited for Personal Interviews</td>
<td>34</td>
</tr>
<tr>
<td>6</td>
<td>Policies Discussed During Personal Interviews</td>
<td>36</td>
</tr>
<tr>
<td>7</td>
<td>Typical Interest Rate Table for Loan Using</td>
<td>43</td>
</tr>
<tr>
<td></td>
<td>Listed Securities as Collateral</td>
<td></td>
</tr>
</tbody>
</table>

...
# LIST OF ILLUSTRATIONS

<table>
<thead>
<tr>
<th>Figure</th>
<th>Description</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Numbers of U. S. Branch and Bank Offices</td>
<td>14</td>
</tr>
<tr>
<td>2</td>
<td>Single Payment Personal Loans</td>
<td>19</td>
</tr>
<tr>
<td>3</td>
<td>Rating of Policies in Order of Decreasing Importance</td>
<td>25</td>
</tr>
<tr>
<td>4</td>
<td>Documentation of Policies (Chief Executives)</td>
<td>27</td>
</tr>
<tr>
<td>5</td>
<td>Flexibility and Rigidity of Policies</td>
<td>29</td>
</tr>
<tr>
<td>6</td>
<td>Documentation of Policies (Loan Officers-Personal Interviews)</td>
<td>37</td>
</tr>
<tr>
<td>7</td>
<td>Maximum Margin Extended on Loan (Loan Officers-Personal Interviews)</td>
<td>41</td>
</tr>
<tr>
<td>8</td>
<td>Assets of Bank vs. Maximum Interest Rate on Loans</td>
<td>45</td>
</tr>
<tr>
<td>9</td>
<td>Rating of Policies in Order of Decreasing Importance (Loan Officers-Personal Interviews)</td>
<td>52</td>
</tr>
</tbody>
</table>
ABSTRACT

AN ANALYSIS OF CURRENT WRITTEN LOAN POLICIES FOR SECURED LOANS AT SAN FERNANDO VALLEY BANKS

by

Albert Leslie Van Maele

Master of Science in Business Administration

June, 1968

As of September 26, 1962 a survey conducted by the Federal Reserve System showed that there was a total of nearly 11 billion dollars, represented by 750,000 loans, which were made to borrowers other than brokers, dealers, or bankers and which were collateralized either wholly or partly by securities. This represents just under one-tenth of all loans which were outstanding at the member banks as of the survey date.

This study seeks to determine how well documented are the policies used to determine whether to grant or reject a loan of this type and to what degree these policies limit the amount of decision making to be exercised by the loan officer handling the loan.
Eight criteria were selected for study. These criteria were (1) loan territory, (2) margin requirement, (3) interest rate, (4) length of loan, (5) ratio of amount of loan to annual income, (6) purpose of loan, (7) compensating balances, (8) amount of loan.

The study consisted of two basic parts. The first part of the study consisted of personal interviews with bank lending officers in the San Fernando Valley, Los Angeles County, to determine how the above criteria were stated in their bank. The second part of the study consisted of a survey of the opinions of leading banking executives throughout the country on the same criteria.

An analysis of both parts of the study indicated that the criteria are for the most part well documented and flexible in nature allowing a relatively high degree of decision making on the part of the loan officer.
CHAPTER I
INTRODUCTION

Regulations and laws of various types have been placed upon the banking function of making loans. These regulations and laws are a general overall set of legal constraints. They are not sufficiently detailed to enable a bank to establish a loan policy of any detail for its particular type of operation. It is therefore necessary for a bank to establish a loan policy, preferably written, which satisfies both the applicable regulations and laws as well as the specific needs of the bank in question.

The study was limited to those banks located in the geographical area known as the San Fernando Valley. This area corresponds to that contained in the Northwestern directory for the Los Angeles City area as published by the Pacific Telephone Company.

The survey questions were intended to cover only loans which were made to private individuals for purposes other than buying or carrying securities. This was done since those loans made for the purpose of buying or carrying securities, to either an individual or a brokerage firm, are closely regulated and
therefore would probably hold few secrets as to how well the applicable policies are documented.

It is not the purpose of this study to develop a standardized system for documentation of loan policies in the area under investigation. The study is concerned with the present nature of this system as seen through the eyes of those people most closely connected with the loans: the loan officers at the branch banks in question.

STATEMENT OF THE PROBLEM:

All banks have a lending policy, written or unwritten, rigid or flexible, even though it may not be clearly recognized by all of the lending officers, and even though some who may admit the policy exists may be uncertain of its content. Small banks, instead of developing definite loan policies of their own, probably copy the policies of larger banks. A definite loan policy takes on greater significance in large banks and those which have many branches, or where there are several loan departments and lending officers.

The problems to be analyzed are the following: Do experts in the field of bank management feel that it is extremely important that a banking system have well established and written loan policies.
To what extent banks (individual and branch) operating in the San Fernando Valley have established a written policy covering loans secured by listed securities and at what level within the management structure of the bank this policy is formulated. A loan which uses listed securities as collateral has been chosen since this is the most common type of collateral used for a secured loan.

The reason for undertaking this study is to determine whether or not the banks operating in the San Fernando Valley follow the published consensus of the experts in the field of bank management on the advisability of having written loan policies and at what level within the management structure of the bank these policies are formulated.

HYPOTHESIS:

"The policies used by banks in the San Fernando Valley to determine whether to grant or reject a loan using listed securities as collateral are largely unwritten, are extremely broad in their limitations, and allow a high degree of decision making to be exercised by the loan officer reviewing the loan regarding the terms of such loans."

The type of loan under consideration, those secured by listed securities, represent just under one-tenth of all loans
outstanding at Federal Reserve System banks. It may therefore be considered of some importance that this area of operation be handled efficiently.

One way to promote this efficiency of operation is by having well formed, well stated, and well known policies covering the criteria used to make decisions regarding this type of loan. If the research shows that this situation does not exist, then it may be that this area of operation is lacking in efficiency.

No data were uncovered indicating an interest by others in the problem under discussion here. This is not to say that they do not exist. To be sure the management of banks and their characteristics have been analyzed in many different ways, but no studies dealing with this particular area were located.

METHOD AND SCOPE:

An analysis was made to determine if the banks in question have written loan policies covering the type of loan under consideration and to what extent these policies are distributed to the loan officers at all branches. This analysis also attempt to determine the management level at which these policies are formulated as

---

well as the degree to which they limit the activities of loan officers. This analysis took the form of a questionnaire and personal interviews with loan officers at the subject banks.

A second questionnaire was sent to the top executive officers of the largest (50) banks in the country to determine what the consensus of opinion is on the advisability of written loan policies for the type of loan being considered.

The scope (extent) of the analysis was confined to the practices of only those banks in the San Fernando Valley and only to loans made to private individuals using listed securities as collateral. The results obtained here would probably be valid for any similarly structured economic area in this country.

DEFINITIONS OF TERMS:

1) POLICIES: Criteria used to determine whether to grant or reject an application for a loan using listed securities as collateral. These policies will be the following.

LOAN TERRITORY: The geographical area in which the bank (branch) operates.

MARGIN REQUIREMENT: The percent of the market value of securities which may be advanced for this type of loan.

INTEREST RATE: The ANNUAL SIMPLE interest rate applying to this type of loan.
LENGTH OF LOAN: Time for which loan may be outstanding (covers various repayment plans).

RATIO OF AMOUNT OF LOAN TO ANNUAL INCOME: Ratio of the amount of the loan to the annual income of the individual requesting the loan.

PURPOSE OF LOAN: The use to which the borrowed funds will be put.

COMPENSATING BALANCES: The amount of funds which the bank requires the borrower to have on deposit with the bank.

AMOUNT OF LOAN: The total amount which is advanced to a person on a single loan of this type.

2) BANKS IN THE SAN FERNANDO VALLEY: All branches of banks and all individual, independent banks operating in the San Fernando Valley, Los Angeles County, California.

3) LISTED SECURITIES: Any security bought and sold on one or more of the stock exchanges registered with the Securities and Exchanges Commission under the terms and conditions provided in Section G of the Securities Exchange Act of 1934.

4) LOAN OFFICER: Anyone within a banking system who has the authority to grant or reject an application for a loan of the type under consideration.
OUTLINE OF FOLLOWING CHAPTERS:

II. THE STRUCTURE OF COMMERCIAL BANKING IN CALIFORNIA
   A) Multiple Office Banking
   B) Collateral Loans

III. OPINIONS OF LEADING BANKING EXECUTIVES ON POLICIES

IV. DATA ANALYSIS

V. SUMMARY AND CONCLUSION
CHAPTER II

THE STRUCTURE OF COMMERCIAL BANKING IN CALIFORNIA

Our present commercial banking system consists of over 14,000 banks which operate (as of January 1966) over 30,000 separate locations or offices (See Table 1). The total number of banks in this country is large when compared with other nations. There are small banks as well as large ones. Table 2 gives an indication of the way in which the total amount of deposits held in our banking system are distributed.\(^2\)

The system under consideration here in California is one of branch banking as compared with unit banking which is predominant in most other parts of the country. The pros and cons of branch versus unit banking will be discussed in detail later. It might be noted that the banking system of Great Britain is one of branches since the "Big Five" (Barclays, Lloyds, Midland, National Provincial, and Westminster) hold approximately 75 per

---

<table>
<thead>
<tr>
<th></th>
<th>1965</th>
<th>1960</th>
<th>1955</th>
<th>1950</th>
<th>1945</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>NUMBER AND TYPES OF U.S. BANKS</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>NATIONAL BANKS</strong></td>
<td>4,801</td>
<td>4,528</td>
<td>4,697</td>
<td>4,962</td>
<td>5,024</td>
</tr>
<tr>
<td><strong>NATIONAL BANK BRANCHES</strong></td>
<td>8,499</td>
<td>5,236</td>
<td>3,821</td>
<td>2,189</td>
<td>1,669</td>
</tr>
<tr>
<td><strong>STATE BANK &amp; TRUST COMPANIES</strong></td>
<td>8,800</td>
<td>8,772</td>
<td>9,477</td>
<td>9,576</td>
<td>9,402</td>
</tr>
<tr>
<td><strong>STATE BANK BRANCHES</strong></td>
<td>6,676</td>
<td>5,005</td>
<td>3,946</td>
<td>2,811</td>
<td>2,254</td>
</tr>
<tr>
<td><strong>MUTUAL SAVINGS BANKS</strong></td>
<td>506</td>
<td>515</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
</tr>
<tr>
<td><strong>MUTUAL SAVINGS BANK BRANCHES</strong></td>
<td>707</td>
<td>480</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
</tr>
<tr>
<td><strong>PRIVATE BANKS</strong></td>
<td>72</td>
<td>79</td>
<td>91</td>
<td>116</td>
<td>135</td>
</tr>
<tr>
<td><strong>OTHER BANKING INSTITUTIONS</strong></td>
<td>94</td>
<td>108</td>
<td>55</td>
<td>45</td>
<td>93</td>
</tr>
<tr>
<td><strong>OTHER BANKING INSTITUTIONS BRANCHES</strong></td>
<td>104</td>
<td>75</td>
<td>31</td>
<td>20</td>
<td>14</td>
</tr>
<tr>
<td><strong>FACILITIES</strong></td>
<td>415</td>
<td>279</td>
<td>181</td>
<td>N.A.</td>
<td>N.A.</td>
</tr>
<tr>
<td><strong>TOTAL BANKS</strong></td>
<td>14,273</td>
<td>14,002</td>
<td>14,320</td>
<td>14,699</td>
<td>14,744</td>
</tr>
<tr>
<td><strong>TOTAL BRANCHES</strong></td>
<td>15,986</td>
<td>10,796</td>
<td>7,258</td>
<td>5,020</td>
<td>3,937</td>
</tr>
<tr>
<td><strong>DEPOSITS (BILLIONS)</strong></td>
<td>393.8</td>
<td>270.3</td>
<td>223.5</td>
<td>178.0</td>
<td>167.3</td>
</tr>
<tr>
<td>**TOTAL ASSETS (BILLION)</td>
<td>446.0</td>
<td>303.0</td>
<td>245.9</td>
<td>194.3</td>
<td>179.1</td>
</tr>
</tbody>
</table>

*(SOURCE: POLK'S BANK DIRECTORY, 1966, p. VIII)*
<table>
<thead>
<tr>
<th>U.S. BANK DEPOSITS</th>
<th>AS OF MARCH 29, 1967</th>
<th>(MILLIONS $)</th>
</tr>
</thead>
<tbody>
<tr>
<td>ALL BANKS</td>
<td>398,410</td>
<td></td>
</tr>
<tr>
<td>COMMERCIAL BANKS</td>
<td>341,960</td>
<td></td>
</tr>
<tr>
<td>MEMBER BANKS</td>
<td>281,903</td>
<td></td>
</tr>
<tr>
<td>MUTUAL SAVINGS BANKS</td>
<td>56,450</td>
<td></td>
</tr>
<tr>
<td>RESERVE CITY MEMBER BANKS:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>NEW YORK</td>
<td>48,061</td>
<td></td>
</tr>
<tr>
<td>CHICAGO</td>
<td>12,223</td>
<td></td>
</tr>
<tr>
<td>OTHER</td>
<td>105,418</td>
<td></td>
</tr>
<tr>
<td>COUNTRY MEMBER BANKS</td>
<td>116,201</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>AS OF JUNE 30, 1966</th>
<th>(MILLIONS $)</th>
</tr>
</thead>
<tbody>
<tr>
<td>INSURED COMMERCIAL</td>
<td>337,146</td>
</tr>
<tr>
<td>NATIONAL MEMBER</td>
<td>197,792</td>
</tr>
<tr>
<td>STATE MEMBER</td>
<td>83,417</td>
</tr>
<tr>
<td>INSURED NON-MEMBER COMMERCIAL</td>
<td>55,937</td>
</tr>
<tr>
<td>NON-INSURED NON-MEMBER COMMERCIAL</td>
<td>2,009</td>
</tr>
<tr>
<td>NON-MEMBER COMMERCIAL</td>
<td>57,946</td>
</tr>
<tr>
<td>INSURED MUTUAL SAVINGS</td>
<td>46,681</td>
</tr>
<tr>
<td>NON-INSURED MUTUAL SAVINGS</td>
<td>7,046</td>
</tr>
</tbody>
</table>

cent of the total banking system's resources and the same percentage of the total banking offices.

Canada has much the same type of system as Great Britain in that there are only nine chartered banks, five of which operate branches throughout the country.  

MULTIPLE OFFICE BANKING

There are three basic types of multiple office banking systems in use today. They are group, chain and branch.

Group banking consists of two or more banks which are under the control of a holding company which may or may not be a banking institution. The banks may be controlled directly through stock ownership, which is the most common method, or they may be indirectly controlled by means of an association or business trust. Today, approximately nine per cent of all commercial banks in the United States are registered under the Bank Holding Company Act of 1956.  

---


4Frazer and Yohe, op. cit., p. 344.
Chain banking is extremely difficult to define and to recognize. It was defined for a time as a situation where "the same individual or group of individuals controls two or more banks." It has recently been broadened to include "any community of interests or links among banks arising directly or indirectly from stock ownership." The control of banks by stock ownership was brought to light from special studies which showed, for example, that one Chicago bank held in excess of 50 per cent of the stock of 27 banks as collateral for loans. The study also showed that this type of banking is more prevalent in those states where branch banking and holding companies are restricted.

Branch banking is a form of multiple office banking where a bank acting as a single legal entity operates more than one banking office. Here in California this type of banking system has reached its greatest heights through the Bank of America National Trust & Savings Association, which is not only the largest bank in the world in terms of assets ($19 billion plus as of 1966), but also operates more branches than any other bank, with more than 800 in California.

---

5 Ibid., p. 246.
6 Ibid., p. 247.
As of March, 1966 the total number of branch banks in the United States exceeded the total number of banks by 15,987 to 14,273 (See Table 1). It is estimated that by the year 1975 the banking system will have 10,000 banks and 25,000 branches (See Figure 1).

As of 1963 the nationwide branch banking picture was as follows: Eight states prohibited branch banking entirely, eight permitted branches but usually only on a local level, ten permitted state-wide branch banking with no location limitations, and twenty-four permitted various degrees of local and/or state-wide branch banking. 8

One of the oldest controversies in the banking field is that of the proponents of unit versus branch banking. Those favoring unit banking do so since they feel that this type of system is essential to maintain competition and to preserve the small banks. On the other hand, those proposing a branch system do so since they feel that this is the best way to maintain stability and efficiency in banking. There are no statistical data available which point to the superiority of one system over the other. 9 For this reason the


FIGURE 1
NUMBER OF U.S. BRANCH AND BANK OFFICES

(Source: Banking, November, 1966, p. 41).
American Bankers Association holds the view that:

decisions as to types of banking organization within the states, including branching, should be reserved for the states. We believe that the enactment of Federal branching statutes which override state laws would undermine and ultimately destroy our dual system of banking.\(^{10}\)

**COLLATERAL LOANS**

As of June 30, 1966 the total of all loans at commercial banks was $211.98 billion. Of this, $178.25 billion was located at banks which were members of the Federal Reserve System. These loans are classified by the Federal Reserve System as Commercial and Industrial, Agricultural, For Purchasing or Carrying Securities, Financial Institutions, Real Estate, Individuals, and Others. As of this same date, there was $258.6 billion outstanding in total loans at all banks. Not all commercial banks are members of the Federal Reserve System. The $33.73 billion represents the 15.9% of all commercial bank loans held by non-member commercial banks.\(^{11}\)

These non-member banks are small and many in number. Table 1 indicates the relative numbers of the various types of

---


banking facilities. From Table 1 it can be seen that although over 50% of all banks in the U.S. are not members of the Federal Reserve System, they hold only 29.2% of all bank deposits.\textsuperscript{12}

Many bank loans are made without the need for the borrower to provide collateral. There are three main reasons why a banker may require collateral from a borrower. First, the borrower's ability to repay the loan may be uncertain. Secondly, the amount of the loan may be such that collateral is needed (large loans). Thirdly, economic conditions may exist which leave the future in doubt.\textsuperscript{13}

There are five principal forms of collateral used for secured loans. They are: (1) Stock and bond collateral; (2) Mortgages; (3) Bills of lading; (4) Warehouse receipts; and (5) Life Insurance.\textsuperscript{14} We shall be concerned with only the first of these in this study.

There are basically four ways of using stocks and bonds for collateral. They are: (1) loans which are to be used for the

\begin{itemize}
\item \textsuperscript{12}Ibid.
\item \textsuperscript{13}Anderson et al., \textit{op. cit.}, p. 146.
\item \textsuperscript{14}Ibid.
\end{itemize}
purpose of investment or speculation in securities; (2) loans to finance securities brokers and dealers; (3) loans to businessmen who wish to use the proceeds for working capital; and (4) loans to a private individual who intends to use the funds for personal consumption. 15

The first two of the above are in the class of "purpose" loans in as much as they are specifically for the purpose of purchasing or carrying securities. The second two above are in the class of loans known as "non-purpose" because the funds resulting from the loan are to be used for purposes other than purchasing or carrying securities.

Loans which are to be used for the purpose of purchasing or carrying securities are made for four reasons: (1) finance the underwriting of new issues; (2) finance dealer inventories; (3) finance stock exchange member accounts; (4) finance individual security purchases. 16

This study is concerned with a very special type of stock-secured loan. It is concerned with those loans made to individuals


other than dealers or brokers that are non-purpose in nature. Information on the volume of this type of loan is not regularly published as is the volume of loans which are made to dealers and brokers for purpose loans. The only source of information on the volume of such loans has been the surveys made by the Federal Reserve System. The last of these was conducted as of September 26, 1962. This survey indicated that out of a total of nearly $11 billion in loans, collateralized by stocks and bonds, made to people other than dealers and stock brokers, $4.6 billion was in the form of single payment loans to individuals for household and other personal purposes. This $4.6 billion represented almost 60% of all single payment personal loans reported by Federal Reserve System member banks and involved nearly 500,000 individual borrowers. The remaining $6.4 billion was held by about 250,000 borrowers. 17

The distribution of these loans is shown in Figure 2 and Table 3.

If it is assumed that at the present time the same ratio of single payment personal loans (made to people other than dealers and brokers) to total loans at Federal Reserve System member banks exists as did at the time of the survey, the current volume of stock and bond secured single payment personal loans to individuals

FIGURE 2
SINGLE-PAYMENT PERSONAL LOANS

Size of Collateral Loan in thousands of dollars

1000 and over
25-100
5-25
Less than 5

Per cent of Total Amount

Personal
Business
Security

Purpose Category of Loan
### Table 3

**Purpose and Principal Collateral of Bank Loans Secured by Stocks and Bonds**

<table>
<thead>
<tr>
<th>Purpose</th>
<th>Secured by stocks</th>
<th>Secured by bonds</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Mutual funds</td>
<td>Actively traded</td>
</tr>
<tr>
<td></td>
<td>Listed shares</td>
<td>Not actively traded</td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>Convertible</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Govt.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Other (^1)</td>
</tr>
<tr>
<td>All col-lateral loans</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Single-payment personal</td>
<td>4,613</td>
<td>591</td>
</tr>
<tr>
<td></td>
<td>3,040</td>
<td>699</td>
</tr>
<tr>
<td>Business</td>
<td>1,046</td>
<td>789</td>
</tr>
<tr>
<td></td>
<td>366</td>
<td>501</td>
</tr>
<tr>
<td>Security</td>
<td>1,949</td>
<td>230</td>
</tr>
<tr>
<td></td>
<td>695</td>
<td>141</td>
</tr>
<tr>
<td>Other</td>
<td>1,046</td>
<td>87</td>
</tr>
<tr>
<td></td>
<td>695</td>
<td>141</td>
</tr>
<tr>
<td>All purposes</td>
<td>10,936</td>
<td>1,924</td>
</tr>
</tbody>
</table>

### Amount outstanding (millions of dollars)

<table>
<thead>
<tr>
<th>Purpose</th>
<th>All purposes</th>
<th>Secured by stocks</th>
<th>Secured by bonds</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>10,936</td>
<td>6,187</td>
<td>243</td>
</tr>
<tr>
<td></td>
<td>3,120</td>
<td>1,196</td>
<td></td>
</tr>
<tr>
<td></td>
<td>1,924</td>
<td>286</td>
<td></td>
</tr>
<tr>
<td></td>
<td>309</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>792</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Number (thousands)

<table>
<thead>
<tr>
<th>Purpose</th>
<th>All purposes</th>
<th>Secured by stocks</th>
<th>Secured by bonds</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>754</td>
<td>488</td>
<td>44</td>
</tr>
<tr>
<td></td>
<td>163</td>
<td>57</td>
<td></td>
</tr>
<tr>
<td></td>
<td>106</td>
<td>10</td>
<td></td>
</tr>
<tr>
<td></td>
<td>20</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>29</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

\(^1\)Includes some loans secured principally by collateral other than stocks or bonds.

for household and other personal purposes would be $7.6 billion. There is no way of determining the total number of loans involved for this new total, but if the average size of the loan is the same as in 1962, there would now be approximately 825,000 individual borrowers having this type of loan.

The policies used in determining whether or not to grant a loan using listed securities as collateral at San Fernando Valley banks will now be examined.
CHAPTER III

OPINIONS OF LEADING BANKING EXECUTIVES ON POLICIES

This work is concerned with two main questions. The first of these is to what degree loan policies covering non-purpose (proceeds not to be used for the purpose of buying or carrying securities) loans secured by listed securities are documented by the bank making the loan (written or unwritten). The second question is to what degree loan officers using these policies are allowed to make decisions within the limits of the policies (flexible or rigid). The first step was to determine how the leaders in the field of banking feel on the two questions above. In order to do this, a questionnaire was prepared (See Appendix A) and sent to the chief executive officers of the 50 largest banks in the country.

A total of 23 questionnaires were returned, 13 of which were completed. Based upon the response rates to other questionnaires, 15%\(^{18}\) and 33%,\(^{19}\) this response rate of 26% completed and


46% returned could be considered average.

Question 1 was an attempt to determine the relative importance of each of the eight policies under consideration as seen by the chief executive officers of the banks in question (50 largest). They were asked to rate each of the policies using a scale of 1, 2 and 3. A rating of 1 indicated they felt the policy was one of the MOST IMPORTANT policies. A rating of 2 indicated they felt the was one of only AVERAGE IMPORTANCE. A rating of 3 indicated they felt the policy was one of NO IMPORTANCE.

The data indicates that the most important loan policy concerns margin requirement. Ninety per cent of the respondents rated this policy as one of the MOST IMPORTANT, 10% rates it as of AVERAGE IMPORTANCE, and none of the respondents rated it as of NO IMPORTANCE.

Next in order of importance were policies covering interest rates and the length of loan. On both of these policies 60% of the respondents rated these policies as MOST IMPORTANT, 40% rated them as of AVERAGE IMPORTANCE, and none rated them as of NO IMPORTANCE.

The purpose of the loan was seen by 50% of the respondents as one of the MOST IMPORTANT policies and by 50% as one of only
AVERAGE IMPORTANCE. Compensating balances were rated as MOST IMPORTANT by 30% and of AVERAGE IMPORTANCE by 70%.

Only those policies covering loan territory, amount of loan, and ratio of amount of loan to borrower's income were rated as of NO IMPORTANCE by some of the respondents. Loan territory policy must be considered as the least important since it was rated as of NO IMPORTANCE by 40%, of AVERAGE IMPORTANCE by 40%, and as one of the MOST IMPORTANT by only 20% of the respondents. This represents the lowest percentage of MOST IMPORTANT and highest percentage of NO IMPORTANCE ratings among all of the policies. Data for all of the policies may be seen in Figure 3 where all policies are arranged in their order of decreasing importance.

The question of whether or not these policies should be written or unwritten produced the following results. Eighty per cent of the respondents felt that those policies rated as MOST IMPORTANT should be written while only 10% felt they should be unwritten. Fifty per cent felt that even those policies that were rated as of only AVERAGE IMPORTANCE should be written while only 40% felt they should be unwritten. Only for those policies rated as of NO IMPORTANCE did a larger per cent (70%) feel they should be unwritten than felt they should be written (20%).
FIGURE 3
RATING OF POLICIES IN ORDER OF DECREASING IMPORTANCE (RESPONSE FROM CHIEF EXECUTIVES OF 50 LARGEST BANKS)

- Margin Requirement
- Interest Rate
- Length of Loan
- Purpose of Loan
- Amount of Loan
- Compensating Balances
- Ratio of Loan to Borrower's Income
- Loan Territory

Most Important
Average Importance
No Importance

% Respondents
In all cases the relative percentage of how the respondents felt regarding the policies being written or unwritten agreed exactly with what they considered to be the existing conditions (see question 3). All data regarding the policies being written or unwritten are summarized in Figure 4.

From this summary we can say that the majority of the respondents (more than 50%) believe that those policies which they rated as either MOST IMPORTANT or of AVERAGE IMPORTANCE, can best be implemented when they are written, whereas it is felt by the majority of the respondents that policies considered to be of NO IMPORTANCE may be unwritten. From this we can conclude that all of the eight policies under consideration should be written in the opinion of the respondents since none of the policies were considered to be of NO IMPORTANCE by more than 40% of the respondents. 20

Regarding the question of flexibility and rigidity, all of the respondents (100%) agreed that those policies of AVERAGE IMPORTANCE and NO IMPORTANCE are, and indeed should be,  

---

20 The above 40% is not more significant than a simple majority (51%) since a test of the null hypothesis $\mathcal{H}_0 = .40$ must be rejected in favor of the alternate $\mathcal{H}_1 : .40$ since there is a probability of .28 that the value will be between .40 and .51 (40% - 51%).
flexible. Seventy per cent felt that those policies rated as **MOST IMPORTANT** should be flexible and 30% felt they should be rigid.

On this same question only 25% felt the **MOST IMPORTANT** policies **WERE** rigid while 80% felt they were flexible. This is an overwhelming endorsement for flexibility in the establishment of the loan policies under consideration. For a summary of these data see Figure 5.

All of the respondents (100%) indicated that these policies are formulated at the Upper (Main Office) level of management rather than at the Middle, or Lower (Branch Office) level.

Since California has a statewide branch banking system, it was thought to be of some interest to see how the respondents felt regarding this type of system. Ninety per cent preferred the branch system and 10% stated they had no preference. Branch banking was preferred by some bankers who operate in states where the unit banking system is strictly adhered to and branches are not allowed. This question, regarding the type of banking system preferred, produced the most comments. It seems to be the feelings of the executives in question, based on their comments, that branch banking offers the community the following advantages over unit banking systems.
Respondents Opinion As To Situation Which **DOES** Exist

![Graph showing the percentage of respondents' opinions about the existence of different policy ratings.](image)

**FLEXIBILITY AND RIGIDITY OF POLICIES (CHIEF-EXECUTIVES)**

**FIGURE 5**

- Policies Rated "Most Important"
- Policies Rated "Average Importance"
- Policies Rated "No Importance"

% Respondents Opinion As To Situation Which **SHOULD** Exist

![Graph showing the percentage of respondents' opinions about the existence of different policy ratings.](image)
1) Larger banks (branch system) are able to offer a much wider range of financial services to the local community.

2) A branch banking system attracts more capable management ability and therefore serves the local community more efficiently.

3) A branch system, since it is usually more aggressive, stimulates competition among banking institutions in the area, thereby improving service to the area.

Rounding out the questionnaire was an inquiry into the length of time the respondents had been in the banking business. The average time was 27.5 years, the median was 30 years, the shortest time was 15 years, and the longest time was 40 years.

The following conclusions may be drawn from the information contained in the respondents questionnaires.

1) The policies under consideration should be written rather than unwritten.

2) The policies should be flexible rather than rigid.

3) The policies should be formulated at the Upper (Main Office) management level.

4) Branch banking appears to be the choice of the chief executive officers of the nations 50 largest banking institutions.
CHAPTER IV
DATA ANALYSIS

The major portion of this work, as stated in the introduction, is concerned with determining "to what extent banks (individual or branch) operating in the San Fernando Valley have established a written policy covering loans secured by listed securities and at what level within the management structure of the bank this policy is formulated." In order to obtain this information two methods were used: The first of these was a mailed questionnaire and the second was personal interviews at the banks.

AREA CHARACTERISTICS:

The area of interest is that of the San Fernando Valley. This is an area of approximately 220 square miles (40% of the total area of the city of Los Angeles) having a population of 1,294,263 of a total of 2,731,000 Los Angeles City population and a total of 7,032,938 Los Angeles County population. The San Fernando Valley has natural mountain boundaries on the north, south, west, and part of the east side. This area is one which contains a large number of commuters since the area contains approximately 40% of the city's residents yet only 20% of all people employed within
the city are working in the area.

**SAMPLE SIZE:**

At the time the mail questionnaire was sent out, March 5, 1967, there were 114 banking offices in the San Fernando Valley. Table 4 gives a summary of the banks included in the mailing as well as other characteristics of the banks.

Due to the number of banks being relatively small for a mailed questionnaire, a 100% sample was selected for this effort. Since time would not permit a 100% sample for the purpose of personal interviews, a random sample of 14 banks was selected for these interviews. Table 5 shows those banks selected for personal interviews.

**MAIL QUESTIONNAIRE:**

The mail questionnaire (Appendix B) was sent with a cover letter in the form of a four page booklet to each of the banks listed in Table 5. They were sent in a 9-1/2 X 13 manila envelope and each contained a 9 X 5 stamped, self addressed envelope for the return of the completed questionnaire. The mailing was addressed to the "Operations Manager" of each of the banks in question.

The mail questionnaire response was very poor since only five were returned completed. Due to this poor response, the
TABLE 4
BANKS FROM WHICH DATA WAS GATHERED

<table>
<thead>
<tr>
<th>Number of Branches</th>
<th>National</th>
<th>State</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Calif.</td>
<td>SFV*</td>
</tr>
<tr>
<td>Bank of America</td>
<td>810</td>
<td>43</td>
</tr>
<tr>
<td>Security 1st National</td>
<td>330</td>
<td>27</td>
</tr>
<tr>
<td>Crocker-Citizens</td>
<td>258</td>
<td>12</td>
</tr>
<tr>
<td>United California</td>
<td>189</td>
<td>11</td>
</tr>
<tr>
<td>Union Bank</td>
<td>10</td>
<td>4</td>
</tr>
<tr>
<td>1st Western</td>
<td>58</td>
<td>1</td>
</tr>
<tr>
<td>City National</td>
<td>13</td>
<td>2</td>
</tr>
<tr>
<td>Community Bank</td>
<td>4</td>
<td>1</td>
</tr>
<tr>
<td>Valley National</td>
<td>4</td>
<td>4</td>
</tr>
<tr>
<td>San Fernando Valley</td>
<td>5</td>
<td>3</td>
</tr>
<tr>
<td>Independence Bank</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>Surety National</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>Lincoln Bank</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>Providencia Bank</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>Boulevard Bank</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>National Bank of Commerce</td>
<td>3</td>
<td>1</td>
</tr>
<tr>
<td><strong>TOTAIS</strong></td>
<td>16</td>
<td>1690</td>
</tr>
</tbody>
</table>

*San Fernando Valley  **Federal Reserve System
### TABLE 5
BANKS VISITED FOR PERSONAL INTERVIEWS

<table>
<thead>
<tr>
<th>BANK</th>
<th>NUMBER OF BRANCHES INTERVIEWED</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank of America</td>
<td>3</td>
</tr>
<tr>
<td>United California Bank</td>
<td>2</td>
</tr>
<tr>
<td>Security 1st National Bank</td>
<td>1</td>
</tr>
<tr>
<td>Crocker-Citizens National Bank</td>
<td>2</td>
</tr>
<tr>
<td>City National Bank</td>
<td>1</td>
</tr>
<tr>
<td>Union Bank</td>
<td>1</td>
</tr>
<tr>
<td>Surety National Bank</td>
<td>1</td>
</tr>
<tr>
<td>1st Western Bank</td>
<td>1</td>
</tr>
<tr>
<td>Providencia Bank</td>
<td>1</td>
</tr>
<tr>
<td>Community Bank</td>
<td>1</td>
</tr>
</tbody>
</table>
primary sources of data are the personal interviews conducted with the loan officers at the banks listed in Table 5. The mail questionnaire is analyzed only as a matter of curiosity.

**QUESTION 1**

The respondents were asked which of the policies listed (Table 6) were written and which were unwritten. The results of this question are shown in Figure 6.

Only 4 of the 14 banks interviewed indicated that all the subject policies were unwritten. These banks were notably the smaller ones in terms of assets and numbers of branches. These 4 banks represented only 8 of the total 114 branches in the area and half of these (4 branches) belonged to one bank.

Only 2 of the remaining 10 banks interviewed indicated that any of the policies were unwritten. Both of these banks indicated that "loan territory," "ratio of amount of loan to annual income," and "purpose of loan-use of funds" were unwritten policies. One of the two also listed "amount of loan" as unwritten.

**QUESTION 2**

In this question respondents were asked to indicate only the level at which the subject policies were formulated. Seventy nine per cent of the respondents indicated that all of the policies
<table>
<thead>
<tr>
<th></th>
<th><strong>POLICIES DISCUSSED DURING PERSONAL INTERVIEWS</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td><strong>LOAN TERRITORY</strong> - Geographic area in which the bank operates.</td>
</tr>
<tr>
<td>2.</td>
<td><strong>MARGIN REQUIREMENT</strong> - The percent of market value of a security which may be advanced on the loan.</td>
</tr>
<tr>
<td>3.</td>
<td><strong>INTEREST RATE</strong> - Annual SIMPLE interest rate applied to a loan of the type under consideration.</td>
</tr>
<tr>
<td>4.</td>
<td><strong>LENGTH OF LOAN</strong> - Time for which loan may be outstanding (this covers various repayment plans).</td>
</tr>
<tr>
<td>5.</td>
<td><strong>RATIO OF AMOUNT OF LOAN TO ANNUAL INCOME</strong> - For a person receiving loan.</td>
</tr>
<tr>
<td>6.</td>
<td><strong>PURPOSE OF LOAN</strong> - Use to which borrowed funds will be put.</td>
</tr>
<tr>
<td>7.</td>
<td><strong>COMPENSATING BALANCES</strong> - Degree to which bank requires these of borrower.</td>
</tr>
<tr>
<td>8.</td>
<td><strong>AMOUNT OF LOAN</strong> - Total amount for all loans of this type which may be advanced to one individual at a given time.</td>
</tr>
</tbody>
</table>

**NOTE:** The above policies are those which apply to loans which have as collateral, listed securities. They also apply only to loans advanced to private parties and not to brokers, dealers, or bankers for the purpose of buying or carrying securities.
under consideration were formulated at the Upper Management level. Only 3 banks indicated these policies were formulated at the Lower or Branch level and, as in question 1, these were the smaller banks representing 6 of a total of 114 branches, and as before, 4 of the 6 branches belong to one bank.

QUESTION 5

Regarding the question of how often the subject policies were revised, 100% of all respondents (both personal and mailed response) indicated that all policies are revised on an "as required" basis and in the case of a rapidly changing financial world, such as we have recently experienced, this is at times on a daily basis for such policies as interest rate.

The remainder of the questions were asked in order to obtain more specific information regarding the policies in question to determine their degree of rigidity of flexibility.

LOAN TERRITORY - QUESTIONS 8 thru 11

The "Loan Territory" which we are concerned with has been defined as "The geographical area in which the bank (branch) operates." This area is not limited for the type of loan under consideration by state or federal law. A bank may legally make this type of loan to an individual wherever he may be located. The
banks do, however, suggest that the best interest of the customer will be served if the loan is located at a branch that is located close to the customer. Some banks indicated that a few of these types of loans were outstanding to customers who lived in the area previously and had been considered a "good" customer or in the case of someone who is a permanent resident in the area but has been working out of the area for extended periods of time (up to a number of years). One point was made clear by all banks interviewed and that was that at no time do they actively solicit loan customers outside of the state of California for this type of loan.

For the most part any loan territory that the banks have established for themselves is loosely regarded. Should a customer inquire at a branch they might only suggest that perhaps it would be more convenient for him if the loan were located at a branch closer to his residence or place of employment.

No real conclusions can be drawn from the questions regarding "Loan Territory" as defined, since it appeared to have had a somewhat different meaning in the minds of each of the individuals interviewed. For the record, 5 banks indicated that a "Loan Territory" existed while 9 indicated that it did not.
Margin requirement is defined in this study as "The percent of the market value of the securities which may be advanced for this type of loan." It was pointed out to the loan officers interviewed that this was an attempt to determine how their values for margin requirement might differ from the legal limits which for a listed security is fixed at a maximum of 75% by Section 7 (a) of the Securities and Exchange Act of 1934 as follows.

"......An amount not greater than whichever is the higher of -
(1) 55 per centum of the current market price of the security, or
(2) 100 per centum of the lowest market price of the security during the preceding thirty-six calendar months, but not more than 75 per centum of the current market price."

A summary of the results of this question may be found in Figure 7. From this it appears that the majority of banks (8 out of 14) would like to have a 5% (70% margin) hedge against possible future market declines and in fact this was the comment of several of the respondents.

Before continuing, some observations must be made on the way in which some of the policies to follow are very closely related. All of the loan officers interviewed indicated that it was very difficult to give individual values for the policies covering "interest
FIGURE 7
MAXIMUM MARGIN EXTENDED ON LOAN (LOAN OFFICERS-PERSONAL INTERVIEWS)
rate, "length of loan," "compensating balances," and "amount of loan" since these four in particular were very closely related and will be dependent on the financial position of the borrower to a great degree. As an example, a large loan might carry a smaller interest rate than would a loan for a smaller amount. This is best illustrated by the interest rates shown in Table 7. This rate table is used by one of the larger banks in determining the interest rate to use for a particular loan depending upon the amount of the loan. It can be seen that a range of rates is given in order to allow the loan officer to evaluate other characteristics of the individual loan prior to setting the interest rate. The reason for this difference in rates depends on a number of factors, one of which is the fact that a loan costs the same to administer, assuming all things except the amount are equal, no matter what the amount of the loan. Therefore, since the interest rate must cover the cost of administering the loan, a larger loan may carry a small interest rate. Also, a larger loan usually indicates that the borrower may be in a somewhat more desirable financial position than the borrower of a smaller loan, and therefore the chances of having to liquidate all or part of the collateral, which is an added expense, are much less for the larger loan.
# TABLE 7

**TYPICAL INTEREST RATE TABLE FOR LOAN USING LISTED SECURITIES AS COLLATERAL**

<table>
<thead>
<tr>
<th>AMOUNT OF LOAN</th>
<th>ANNUAL SIMPLE INTEREST RATE</th>
</tr>
</thead>
<tbody>
<tr>
<td>0 - $10,000</td>
<td>7.5 - 8.0%</td>
</tr>
<tr>
<td>10 - $25,000</td>
<td>7.0 - 7.75%</td>
</tr>
<tr>
<td>25 - $50,000</td>
<td>6.75 - 7.75%</td>
</tr>
<tr>
<td>50 - $100,000</td>
<td>6.5 - 7.5%</td>
</tr>
</tbody>
</table>

*(SOURCE: BANK OF AMERICA)*
To further substantiate the belief that loan officers are allowed a degree of freedom in exercising the policies under consideration, it was noted that almost all of the respondents commented that no two loan officers in the same branch would probably handle the same loan request in the same manner regarding the policies under discussion.

**INTEREST RATE - QUESTIONS 16, 17 and 18**

As stated previously, interest rates are dependent on several other characteristics of an individual loan. For this reason the only value which probably has significance is the maximum interest rate a branch would charge for a loan of this type. The minimum interest rate was indicated by about fifty per cent of the respondents as being that which they currently paid on savings accounts plus 1 - 1.5%. Attention should again be directed to Table 7 as an example of typical interest rates.

The interest rate seemed to be more dependent on the size of the bank in terms of assets than to any other characteristic. The maximum interest rate charged versus the banks assets is shown in Figure 8.
FIGURE 8

ASSETS OF BANK VS. MAXIMUM INTEREST RATE ON LOANS
LENGTH OF LOAN - QUESTIONS 21 and 22

In this question it was hoped to determine the degree to which the length of the loan or the way in which it is repaid affects the interest rate charged. Eight of the 14 respondents (57%) indicated that the interest rate was affected by the type of repayment plan selected. A more important factor in determining the length of the loan or repayment method was that of the financial condition of the borrower and his ability to repay the loan.

The methods of repayment are varied and change to meet the existing financial picture. In times when prime interest rates may be rising and money becomes tight, loans may be written for very short periods of time, such as 30 to 90 days. Almost all such loans are made "callable" at any time by the lender. At the end of the specified period the interest is paid on the loan and the loan is either repaid or renewed for another period of time which again is determined by current financial conditions. In this way the bank is able to limit more easily the amounts outstanding for this type of loan should they so desire and they are able to increase the interest rate on the loan if in the meantime their own prime interest rate has increased. It was noted that "very seldom" are loans which are written for short periods of time set up with any type of interim principal repayment program. Another advantage, although this
was not discussed, might be the fact that a loan which is periodically reviewed, as all of them should be, has a better chance of keeping within the policy framework of the bank as policy changes than do those loans of this type which might be written for longer times and therefore allowed to remain undisturbed for extended periods of time.

In times when the prime interest rates on money are expected to be stable and money for loans is readily available, loans of this type may be written for somewhat longer periods of time with quarterly interest payments made and at that time the note is usually renewed for another 90 days. These loans are commonly made to be repaid in 1 to 2 years with only quarterly interest paid and the principal due at the end of the loan. These loans are also almost always made "callable" at the discretion of the lender.

**RATIO OF AMOUNT OF LOAN TO ANNUAL INCOME - QUESTIONS 23 and 24**

Fifty per cent of the respondents (7 of 14) indicated that they did consider the annual income of a borrower for a loan of this type and 50% indicated they did not. This question again is very dependent on the borrower's ability to repay the loan when it is due. Those that felt the annual income was important indicated they did so because if the man did not have a sufficiently high income, if
this was to be the source of repayment, then he would not be able to repay the loan without the bank having to liquidate some or all of the stock used for collateral. These respondents indicated that the bank did not like to have to liquidate collateral in order to recover the loan when due.

The 50% of the respondents who did not consider the borrower's income as an important factor stated that as far as they were concerned the loan was completely secured by the collateral held and it was up to the borrower to provide a method of repaying the loan. We may probably assume that this meant that even if at the time the loan was made the borrower intended to sell some of the securities if necessary to repay the loan, the loan still would have been made. Unfortunately this exact question as to whether or not a loan would be made if the borrower stated that he intended to sell some of the securities in order to repay the loan was only asked of the last two gentlemen interviewed. One of them said that he would still make the loan (He had said there was no requirement for annual income), the other said that he probably would not make the loan under those conditions (He did consider annual income an important factor).
Sixty four per cent of the respondents (9 of 14) indicated that other than section 7 of the Securities Exchange Act of 1934 they had no restrictions on the use to which the borrowed funds were to be put, other than they be used for a legal purpose.

The conditions which the other 5 respondents stated would prevent them personally from making a loan for this type were many and varied. Some of them are as follows.

1) A down payment on a car or home;

2) Capital for any type of business where alcoholics were involved;

3) Vacations;

4) Betting of any form even where legal;

5) Any type of compensation involving an unwanted pregnancy illegally developed.

A recent survey by the Federal Reserve Board indicated that of the total of $9.6 billion in loans for which securities were used as collateral, $4.6 billion was in the form of a single payment loans to individuals for household or other personal purposes; this represents almost 60% of all single-payment personal loans reported
by member banks on their September 28, 1962 condition reports. 21

COMPENSATING BALANCES - QUESTIONS 27 and 28

Seventy-nine per cent of the respondents (11 of 14) indicated that compensating balances were required. This could mean anything from merely having an account with the bank no matter what the average balance too, in some cases, a requirement (what they would like to see) of as much as 30% of the value of the loan. The respondents also indicated that the amount of compensating balance does have an effect on the interest rate which the loan carries.

AMOUNT OF LOAN - QUESTION 15

The amount of the loan is a rather hard question on which to obtain meaningful data. All of the respondents were unanimous on the following points, however,

1) Section 5200 of the National Banking Act of June 16, 1933 sets the limitation on loan to one person at "10 per centum of the amount of the capital stock of such association actually paid in and unimpaired and 10 per centum of its unimpaired surplus fund."

2) Each loan officer has a limit above which amount he may not make a loan on his own. In turn each branch manager has a loan authorization limit which he may not exceed.

3) The amount that is loaned to an individual, assuming the approval level exists and the 10 per cent rule is observed, depends largely on the nature of the collateral and the financial position of the borrower.

QUESTION 29

This question, as was question 1, was an attempt to determine the relative importance of each of the eight policies under consideration as seen by the respondents, in this case the loan officer being interviewed. As before, the respondents were asked to rate each of the policies using a scale of 1, 2, and 3. A rating of 1 indicated they felt the policy was one of the MOST IMPORTANT policies. A rating of 2 indicated they felt the policy was one of only AVERAGE IMPORTANCE. A rating of 3 indicated they felt the policy was one of NO IMPORTANCE.

The data indicates that the most important loan policy concerns margin requirement. One hundred per cent of the respondents rated this policy as one of the MOST IMPORTANT. A summary of the data for this question may be seen in Figure 9.
Most Important | Average Importance | No Importance

Margin Requirement
Interest Rate
Purpose of Loan
Length of Loan
Compensating Balances
Ratio of Loan to Borrower's Income
Amount of Loan
Loan Territory

% Respondents

Figure 9: Rating of Policies in Order of Decreasing Importance (Loan Officers-Personal Interviews)
As a matter of curiosity one final question was asked of the respondents and that was the number of years they had been in the field of banking. The average time was 21 years, the median was 20 years, the shortest time was 3 years by an assistant manager of one of the smaller banks, and the longest time was 35 years. This compares with an average of 27.5 years, median of 30 years, shortest time of 15 years, and longest time of 40 years for the chief executive officers responding to the questionnaire of Appendix A.
CHAPTER V
SUMMARY AND CONCLUSION

The first part of the hypothesis states that the policies under consideration are "largely unwritten." From the analysis of Chapter III, "Opinions of Leading Banking Executives on Policies," we have shown that "the majority of the respondents (more than 50%) believe that those policies which they rated as MOST IMPORTANT or of AVERAGE IMPORTANCE can best be implemented when they are written, whereas the majority of the respondents felt that policies considered to be of NO IMPORTANCE may be unwritten. From this it can be concluded that all of the eight policies under consideration should be written in the opinion of the respondents since none of them were considered of NO IMPORTANCE by more than 40% of the respondents." In Chapter IV, "Data Analysis," it was observed that 5 of the 8 policies were rated by 68% of the respondents as being written and by only 32% as being unwritten. Three of the eight policies were rated by 58% of the respondents as being written and by 42% as being unwritten. Based on these figures and keeping in mind that those banks rating the policies as unwritten represent only 15% of the total assets represented by the
banks surveyed, the first part of the hypothesis must be rejected and say that the policies under consideration are "largely written."

The second part of the hypothesis states that these policies "are extremely broad in their limitations, and allow a high degree of decision making to be exercised by the loan officer reviewing the loan regarding the terms of such loans." This is equivalent to a rating of "flexible" by the respondents of Chapter III. From Figure 5 it can be seen that the highest percentage of respondents which felt those policies rated as MOST IMPORTANT should be "rigid" was 30%. For those policies of AVERAGE IMPORTANCE and of NO IMPORTANCE, 100% of the respondents felt the policies should be "flexible." Perhaps the best way to examine the response from the loan officers interviewed is to take each policy in turn.

MARGIN REQUIREMENT: All respondents were governed by Section 7(A) of the Securities and Exchange Act of 1934 which sets the maximum margin for a non-purpose loan at 75%. Other than this, they may advance any lesser per cent of the market value of the securities depending upon how the financial condition of the borrower appears to the loan officer personally.

CONCLUSION: This policy is "flexible" below the legal maximum set by law.
INTEREST RATE: In general, banks have a basic minimum interest rate and a range of interest rates for various size loans. (see Table 7).

CONCLUSION: For those banks having an interest table, the rate is considered "flexible" and is even more "flexible" for those banks which have no table for the loan officer to refer to since this rate is left to his own personal discretion.

LENGTH OF LOAN: This policy depends upon how the loan officer views the financial position of the borrower and his ability to repay the loan.

CONCLUSION: Policy is one of the most "flexible."

AMOUNT OF THE LOAN: This policy is again dependent upon the financial position of the borrower as seen by the loan officer.

CONCLUSION: Within the lending limitations of the loan officer, this policy is very "flexible."

COMPENSATING BALANCES: As for many of the other policies, this policy depends on the discretion of the loan officer in the way in which he views the financial position of the borrower and the level at which the other policies are set (e.g., interest rate).

CONCLUSION: "Flexible."
PURPOSE OF LOAN: Other than the legal requirement that the loan be for a purpose which is not of an illegal nature, this is up to the discretion of the loan officer.

CONCLUSION: The loan officer is allowed a high degree of "flexibility" in administering this policy.

RATIO OF AMOUNT OF LOAN TO INCOME OF BORROWER: Again this depends on the method of repayment proposed and the financial position of the borrower as seen by the loan officer. This is a policy which is viewed quite differently by each loan officer. Some do not even use it as a criterion.

CONCLUSION: Policy is extremely "flexible."

LOAN TERRITORY: This policy is one which is very hard to define. Loans are not prohibited because of the physical location of the borrower and it is up to the discretion of each loan officer to see that loans are not made which will be prohibitively expensive to administer because of the distance between the loan officer and the borrower.

CONCLUSION: Extremely "flexible."

Therefore, based on the above analysis of each of the policies, the second portion of the hypothesis stating that the policies are "flexible," shall be accepted.
Gentlemen:

The enclosed questionnaire is being sent to you in the hope that you will be willing to provide the necessary information. You have been selected to participate in a project designed to determine how leading executives in the field of banking feel regarding the importance of having written policies covering loans which use as collateral, listed securities. We are also trying to determine to what extent you feel loan officers are allowed to make the required decisions within the policy framework.

This questionnaire is a major fact finding document for a Master's thesis in the School of Business Administration and Economics at San Fernando Valley State College which deals with the question of the documentation and use of loan policies. Your cooperation in completing the enclosed form will be greatly appreciated.

Be assured that this information will be treated as confidential and the only release will be of the final analysis of the responses. There is a coding number located in the upper right hand corner of the questionnaire for purposes of data analysis. If you prefer, you may easily remove this number before returning the form in the enclosed self addressed, stamped, envelope. Your answers will, however, be of additional value if the number is allowed to remain.

Should you not feel that you have the time to participate in this project, although I sincerely hope that this is not the case, we ask that you please return the form in the envelope provided, blank.

We sincerely hope that you will find the time to provide this much needed information. We look forward to hearing from you in the near future. Thank you very much.

Very truly yours,

Albert L. Van Maele
1. Please rate the following policies (1-1) thru (1-8) using a scale of 1 thru 3 as shown below.

1- Indicates you feel the policy is one of the MOST IMPORTANT
2- " " " " " " " of AVERAGE IMPORTANCE
3- " " " " " " " NO IMPORTANCE

1-1 LOAN TERRITORY: Geographical area in which the bank operates
1-2 MARGIN REQUIREMENT: Percent of market value of securities which may be advanced on the loan
1-3 INTEREST RATE: Annual SIMPLE interest rate for this type loan
1-4 LENGTH OF LOAN: Time for which loan may be outstanding (covers various repayment plans)
1-5 RATIO OF AMOUNT OF LOAN TO ANNUAL INCOME: For borrower
1-6 PURPOSE OF LOAN: Use to which borrowed funds will be put
1-7 COMPENSATING BALANCES: Degree to which required of borrower
1-8 AMOUNT OF LOAN: Total amount for all loans of this type which may be advanced to one individual at a given time

2. Please indicate your personal feelings as to whether or not the policies which you rated in question 1. SHOULD BE written or unwritten. (Check one for each of the following)

2-1. MOST IMPORTANT should be __ written, __ unwritten
2-2. AVERAGE IMPORTANCE should be __ written, __ unwritten
2-3. NO IMPORTANCE should be __ written, __ unwritten

3. Please indicate, based upon your experience, whether or not the policies in question 1. ARE written or unwritten.

(check one for each of the following)

3-1. MOST IMPORTANT policies are __ written, __ unwritten
3-2. AVERAGE IMPORTANCE policies are __ written, __ unwritten
3-3. NO IMPORTANCE policies are __ written, __ unwritten
4. Do you feel the policies SHOULD BE flexible (decisions made by loan officers) or rigid (no decision needed by loan officer)? (check one for each of the following)

4-1. MOST IMPORTANT policies should be ___flexible, ___ rigid
4-2. AVERAGE IMPORTANCE policies should be ___flexible, ___ rigid
4-3. NO IMPORTANCE policies should be ___flexible, ___ rigid

5. With reference to question 4., do you feel that the policies ARE flexible or rigid? (Check one for each of the following)

5-1. MOST IMPORTANT policies are ___flexible, ___ rigid
5-2. AVERAGE IMPORTANCE policies are ___flexible, ___ rigid
5-3. NO IMPORTANCE policies are ___flexible, ___ rigid

6. At what management level ARE the policies under discussion formulated? (check one of the following)

___Upper (Main Office) ___Middle ___Lower (Branch Office)

7. Please indicate your preference in banking systems and give a brief explanation of why you feel this way.

___Unit banks ___Branch banks ___Other
Explaination. ___________________________________________

8. Please indicate the number of years you have been in the banking field.

___Years

In the space below make any comments you feel may be of benefit in evaluating your answers to the preceding questions.
APPENDIX B

BANK MAIL QUESTIONNAIRE
Gentleman;

The enclosed questionnaire is being sent to you in the hope that you will be willing to provide the necessary information. Your bank has been selected to participate in a project designed to determine how the policies governing the administration of loans, which have as collateral listed securities, are established and implemented. We are attempting to obtain this information from the people who are most closely connected with these policies, the branch loan officer.

This questionnaire is a major fact finding document for a Master's thesis in the School of Business Administration and Economics at San Fernando Valley State College which deals with the question of the documentation and use of loan policies. Your cooperation in completing the enclosed forms will be of great value and very much appreciated. It is also possible that in some small way the information you provide may eventually aid in social and business improvements in this area.

Be assured that this information will be treated as confidential and the only release will be of the final overall analysis of the survey responses. The only identification is that of a coding number which appears in the upper right hand corner on page 3. This number is for the purpose of data analysis only. If you prefer, you may remove this number before returning the forms in the enclosed, self addressed, stamped envelope, but the answers you give will naturally be of more use if the number is allowed to remain.

Should you not wish to participate in this study, we ask that you please return the form in the envelope provided, blank.

We sincerely hope that you will find the time to provide this much needed information. We look forward to hearing from you in the near future. Thank you very much.

Very truly yours,

Albert L. Van Meele
19517 Satiroy
Reseda, California

INSTRUCTIONS: This survey is divided into two parts. Part I is designed to obtain information regarding the way in which policies are established and implemented. Questions 1-7 in Part I are meant to apply to each of the policies shown in the matrix on page 3. 1-6 can be answered by placing an X in the appropriate matrix position, i.e. in question 1 we would like to know for each of the eight policies, if it is written (1-1), unwritten (1-2), or other (1-3). Question 7 may be answered by placing the correct number (1-5) in the proper matrix position depending upon how you feel regarding the phases of policy formulation shown. The correct number can be obtained from the rating scale shown. In questions 4 & 6, it would be very useful if you would please indicate a definite number of days or weeks. The policies under consideration are as follows.

LOAN TERRITORY: The geographical area in which the bank (branch) operates
MARGIN REQUIREMENT: The percent of the market value of securities which may be advanced in this type of a loan
INTEREST RATE: The ANNUAL SIMPLE interest rate applying to this loan class
LENGTH OF LOAN: Time for which loan may be outstanding (various repayment plans)
RATIO OF AMOUNT OF LOAN TO ANNUAL INCOME: Ratio for person obtaining loan
PURPOSE OF LOAN: The use to which the borrowed funds will be put
COMPENSATING BALANCES: The degree to which these are required of the borrower
AMOUNT OF LOAN: The total amount which is advanced to a person on a single or several separate loans of this type

NOTE: The INSTRUCTIONS for Part II may be found on page 2.
NOTE: Use the matrix on page 3 to indicate the answers to questions 1-7.

1. The policy is (select one for each policy)
   1-1 Written; 1-2 Unwritten; 1-3 Other (please explain briefly on page 4)

2. Indicate the management LEVEL, and LOCATION within your organization at which the policy is formulated. (select one for each policy at LEVEL and LOCATION)
   LEVEL: 2-1 Upper; 2-2 Middle; 2-3 Lower;
   LOCATION: 2-4 Central (Main) office; 2-5 Branch bank

3. How is this policy information made available to branch loan officers?
   3-1 Regular mail; 3-2 Formal meeting; 3-3 Informal contact;
   3-4 Other (please explain briefly on page 4)

4. Indicate the usual time period between formulation of a policy and its distribution to branch loan officers. (days or weeks may used as needed)
   4-1 Days: 4-2 Weeks; (indicate number for each policy)

5. Are these policies revised on a REGULAR or AS REQUIRED basis?
   5-1 Regular; 5-2 As required; (select one for each policy)

6. If policy is revised on a REGULAR basis, indicate time between revisions.
   6-1 Days; 6-2 Weeks; (indicate number for each policy)

7. Indicate using the scale of 1 to 5 shown below, your opinion as to the sufficiency of the phases of policy formulation listed (7-1 thru 7-5).

   RATING SCRAP: 1- Completely Satisfactory
                   2
                   3
                   4
                   5- Completely Unsatisfactory

   7-1 Location of formulation (Main or branch); 7-2 Management level of formulation; 7-3 Completeness of distribution; 7-4 Frequency of revision
   7-5 Speed of distribution

PART II

INSTRUCTIONS: Questions 8-10, are designed to obtain more detailed information regarding some of the characteristics of the eight policies. Each of these questions has its own set of answers. Questions may be answered by placing an X in the proper location after each question.

8. Is there a LOAN TERRITORY established within which your branch operates?
   _____ 8-1 Yes; _____ 8-2 No (If No, go to question 12 next)

9. If LOAN TERRITORY exists, please indicate the following.
   9-1 Approximate size ____________ ; 9-2 By whom selected

10. May a loan officer grant a loan to someone outside of the LOAN TERRITORY?
    _____ 10-1 Yes; _____ 10-2 No (If No, go to question 12 next)
<table>
<thead>
<tr>
<th>QUESTION</th>
<th>ANSWER</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>1-1</td>
</tr>
<tr>
<td></td>
<td>1-2</td>
</tr>
<tr>
<td></td>
<td>1-3</td>
</tr>
<tr>
<td>2</td>
<td>2-1</td>
</tr>
<tr>
<td></td>
<td>2-2</td>
</tr>
<tr>
<td></td>
<td>2-3</td>
</tr>
<tr>
<td></td>
<td>2-4</td>
</tr>
<tr>
<td></td>
<td>2-5</td>
</tr>
<tr>
<td>3</td>
<td>3-1</td>
</tr>
<tr>
<td></td>
<td>3-2</td>
</tr>
<tr>
<td></td>
<td>3-3</td>
</tr>
<tr>
<td></td>
<td>3-4</td>
</tr>
<tr>
<td>4</td>
<td>4-1</td>
</tr>
<tr>
<td></td>
<td>4-2</td>
</tr>
<tr>
<td>5</td>
<td>5-1</td>
</tr>
<tr>
<td></td>
<td>5-2</td>
</tr>
<tr>
<td>6</td>
<td>6-1</td>
</tr>
<tr>
<td></td>
<td>6-2</td>
</tr>
<tr>
<td></td>
<td>7-1</td>
</tr>
<tr>
<td></td>
<td>7-2</td>
</tr>
<tr>
<td></td>
<td>7-3</td>
</tr>
<tr>
<td></td>
<td>7-4</td>
</tr>
<tr>
<td></td>
<td>7-5</td>
</tr>
<tr>
<td>11</td>
<td>If loans are granted outside of LOAN TERRITORY, explain briefly under what conditions this is done.</td>
</tr>
<tr>
<td>12</td>
<td>Which of the following types of limits apply to the percent of the market value which may be loaned on securities?</td>
</tr>
<tr>
<td></td>
<td>12-1 Max. %; 12-2 Min. %; 12-3 Absolute %; 12-4 Other (If 12-4 Other, please explain)</td>
</tr>
<tr>
<td>13</td>
<td>May a loan officer exceed the limitations stated in question 12?</td>
</tr>
<tr>
<td></td>
<td>13-1 Yes; 13-2 No (If No, go to question 15 next)</td>
</tr>
<tr>
<td>14</td>
<td>If answer to 13 was Yes, explain briefly conditions making this possible.</td>
</tr>
<tr>
<td>15</td>
<td>Is there a maximum or minimum amount which may be loaned to an individual using this type of loan? Please indicate amounts.</td>
</tr>
<tr>
<td></td>
<td>15-1 Max. (Amount = ); 15-2 Min. (Amount = )</td>
</tr>
<tr>
<td>16</td>
<td>Which of the following types of limits apply to the ANNUAL SIMPLE interest rate used for this type of loan? Please indicate current rates.</td>
</tr>
<tr>
<td></td>
<td>16-1 Max. (Rate = ); 16-2 Min. (Rate = ); 16-3 Absolute (Rate = ); 16-4 Other (Please explain)</td>
</tr>
<tr>
<td>17</td>
<td>May a loan officer exceed the limitations of question 16?</td>
</tr>
<tr>
<td></td>
<td>17-1 Yes; 17-2 No (If No, go to question 19 next)</td>
</tr>
<tr>
<td>18</td>
<td>If answer to 17 is Yes, please explain briefly.</td>
</tr>
<tr>
<td>19</td>
<td>Does the amount of the loan have an effect on the ANNUAL SIMPLE interest rate?</td>
</tr>
<tr>
<td></td>
<td>19-1 Yes; 19-2 No (If No, go to question 21 next)</td>
</tr>
<tr>
<td>20</td>
<td>If answer to 19 is Yes, explain briefly.</td>
</tr>
</tbody>
</table>
21. Does the repayment plan selected affect the interest rate charged?

   ___ 21-1 Yes; ___ 21-2 No (If No, go to question 23 next)

22. If answer to 21 is Yes, explain briefly.

23. Is there a requirement for the ratio of the amount of the loan to the annual income of the person receiving the loan?

   ___ 23-1 Yes; ___ 23-2 No (If No, go to question 25 next)

24. If answer to 23 is Yes, explain briefly.

25. Are there any restrictions placed upon the purpose for which the borrowed funds may be used other than those of Regulation U of the Board of Governors of the Federal Reserve System (Buying or carrying stock—an individual)?

   ___ 25-1 Yes; ___ 25-2 No (If No, go to question 27 next)

26. If answer to 25 is Yes, explain briefly.

27. Are compensating balances required for this type of loan?

   ___ 27-1 Yes; ___ 27-2 No (If No, go to question 29 next)

28. If answer to 27 is Yes, explain briefly.

29. Please indicate your opinion of the importance of each of the following policies (29-1 thru 29-8), in making a loan of the type under consideration by placing the number corresponding to your opinion, as shown on the rating scale below (1 thru 5), before each policy.

   Rating Scale:
   1- Policy is the most important one
   2- 
   3- 
   4- 
   5- Policy is of no importance

   ___ 29-1 Loan Territory
   ___ 29-2 Margin Requirement
   ___ 29-3 Interest Rate (Annual Simple)
   ___ 29-4 Length of Loan (Repayment)
   ___ 29-5 Ratio of Amount of Loan to Annual Income
   ___ 29-6 Purpose of Loan
   ___ 29-7 Compensating Balances
   ___ 29-8 Amount of Loan

30. Place the following policies in their order of importance (your opinion). A rank of #1 indicates that you feel this is the most important of the eight policies (30-1 thru 30-8). A rank of #8 indicates that you feel this is the least important of the policies. Each number from 1 thru 8 may be used only one time (for only one policy).

   ___ 30-1 Loan Territory
   ___ 30-2 Margin Requirement
   ___ 30-3 Interest Rate (Annual Simple)
   ___ 30-4 Length of Loan (Repayment Program)
   ___ 30-5 Ratio of Amount of Loan to Annual Income
   ___ 30-6 Purpose of Loan
   ___ 30-7 Compensating Balances
   ___ 30-8 Amount of Loan

NOTE: On the enclosed sheet of paper, please make any comments you feel will be of use in analyzing the data. You may also use this paper for any extended explanation for a question (please reference questions by number).

Your assistance in this project is very deeply appreciated. Thank you very much.
BIBLIOGRAPHY

PUBLIC DOCUMENTS


BOOKS


ARTICLES AND PERIODICALS
