

MINUTES OF MEETING
of the
FEDERAL ADVISORY COUNCIL
October 7-8, 1937

MINUTES OF MEETING OF THE FEDERAL ADVISORY COUNCIL

October 7, 1937.

The third statutory meeting of the Federal Advisory Council for 1937 was convened in Room 936 of the Mayflower Hotel, Washington, D. C., on Thursday, October 7, 1937, at 10:15 A. M., the President, Mr. Smith, in the Chair.

Present:

Mr. Thomas M. Steele	District No. 1
Mr. Howard A. Loeb	District No. 3
Mr. Charles E. Rieman (alternate for Mr. Charles M. Gohen)	District No. 5
Mr. Edward Ball	District No. 6
Mr. Walter S. McLucas (alternate for Mr. Edward E. Brown)	District No. 7
Mr. Walter W. Smith	District No. 8
Mr. John Crosby	District No. 9
Mr. W. T. Kemper	District No. 10
Mr. R. Ellison Harding	District No. 11
Mr. Paul S. Dick	District No. 12
Mr. Walter Lichtenstein	Secretary

Absent:

Mr. W. W. Aldrich	District No. 2
Mr. Lewis B. Williams	District No. 4

The minutes of the meeting of May 17 to 18, 1937, and subsequent correspondence with accompanying documents relating to S.2344 (Corporate Trusteeships), were read in full by the Secretary and, there being no corrections, the minutes were approved.

Mr. Loeb gave an oral report of the meeting of the committee of the Federal Advisory Council specially appointed to consider S.2344 and the hearings before the subcommittee of the Senate Committee on Banking and Currency. Mr. Loeb stated that the presumption is that the whole matter will again be brought up before the next session of Congress. He pointed out that the bill in its final form was a great improvement upon the original draft of the bill.

It was decided to discuss the proposed amendment to Regulation F, dealing with Common Trust Funds.

At 11:10 A. M. Dr. Goldenweiser, Director, Division of Research and Statistics of the Board of Governors of the Federal Reserve System, appeared before the Council and discussed the general financial and business situation. Dr. Goldenweiser left at 12:50 P. M.

The meeting adjourned for luncheon at 1:00 P. M., at which Vice Chairman Ronald Ransom of the Board of Governors of the Federal Reserve System was present.

The meeting reconvened in Room 936 at 3:15 P. M.

It was voted that Mr. Steele and the Secretary of the Council be appointed a committee to draft a memorandum on the proposed amendment to Regulation F to be presented to the Board of Governors of the Federal Reserve System.

After discussion about the various provisions in the proposed amendment to Regulation F, the meeting adjourned at 4:25 P. M.

WALTER LICHTENSTEIN,
Secretary.

MINUTES OF MEETING OF THE FEDERAL ADVISORY COUNCIL

October 8, 1937.

At 10:20 A. M. the Federal Advisory Council convened in the Board Room of the Federal Reserve Building, the President, Mr. Smith, in the Chair.

Present: Mr. Walter W. Smith, President; Mr. Howard A. Loeb, Vice President; Messrs. T. M. Steele, W. W. Aldrich, C. E. Rieman, Edward Ball, Walter S. McLucas, John Crosby, W. T. Kemper, R. E. Harding, P. S. Dick, and Walter Lichtenstein, Secretary.

The memorandum on the proposed amendment of Regulation F prepared by Messrs. Steele and Lichtenstein (attached to and made a part of these minutes) was read. It was unanimously voted to adopt this memorandum as representing the views of the Council and to be submitted to the Board of Governors of the Federal Reserve System.

The meeting adjourned at 10:50 A. M.

WALTER LICHTENSTEIN,
Secretary.

MINUTES OF JOINT CONFERENCE OF THE FEDERAL ADVISORY COUNCIL
AND THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

October 8, 1937.

At 11:00 A. M. a joint conference of the Federal Advisory Council and the Board of Governors of the Federal Reserve System was held in the Board Room of the Federal Reserve Building, Washington, D. C.

Present: Members of the Board of Governors of the Federal Reserve System:

Vice Chairman Ronald Ransom; Governors Chester C. Davis, John McKee and M. S. Szymczak; also Messrs. Lawrence Clayton, Assistant to the Chairman of the Board of Governors of the Federal Reserve System; Walter Wyatt, General Counsel for the Board of Governors; Chester Morrill, Secretary of the Board of Governors; L. P. Bethea, Assistant Secretary of the Board of Governors; Dr. E. A. Goldenweiser, Director, Division of Research and Statistics of the Board of Governors; Carl E. Parry, Chief of the Division of Security Loans of the Board of Governors; E. L. Smead, Chief of the Division of Bank Operations of the Board of Governors; Elliott Thurston, Special Assistant to the Chairman of the Board of Governors; J. P. Dreibelbis, Assistant General Counsel of the Board of Governors; and George B. Vest, Assistant General Counsel of the Board of Governors.

Present: Members of the Federal Advisory Council:

Mr. Walter W. Smith, President; Mr. Howard A. Loeb, Vice President; Messrs. T. M. Steele, W. W. Aldrich, C. E. Rieman, Edward Ball, Walter S. McLucas, John Crosby, W. T. Kemper, R. E. Harding, P. S. Dick, and Walter Lichtenstein, Secretary.

The Secretary of the Council read the memorandum adopted by the Council relating to the proposed amendment to Regulation F. The memorandum was read section by section and discussed in detail by members of the Council and members of the Board of Governors of the Federal Reserve System.

Vice Chairman Ransom pointed out that the proposed amendment had been purposely made rigid with the idea of arousing discussion and comments. He stated that the Board was in no wise committed to the amendment in its present form.

The President of the Council informed the Board that the Council had voted to have its next meeting on December 6 and 7, but after some discussion it was agreed by the Council and concurred in by the Board that the next meeting of the Council should take place on December 13 and 14.

The members of the Council reported on business conditions in their respective districts.

The meeting adjourned at 1:30 P. M.

WALTER LICHTENSTEIN,
Secretary.

October 8, 1937.

MEMORANDUM OF FEDERAL ADVISORY COUNCIL ON
PROPOSED AMENDMENTS TO REGULATION F RELATING
TO ADMINISTRATION OF COMMON TRUST FUNDS AND OTHER MATTERS

In response to the letter from Mr. L. P. Bethea, Assistant Secretary of the Board of Governors of the Federal Reserve System, to Mr. Walter Lichtenstein, Secretary of the Federal Advisory Council, dated September 18, 1937, the Council submits to the Board herewith its comments upon the proposed amendments to Regulation F referred to in Mr. Bethea's letter. The Council is in agreement that the common trust fund offers a method by which the man of small means may get the benefit of trust service not now available to him because of the expense involved. It believes that it is highly desirable that machinery be set up under which common trust funds may be established by trust institutions and recognizes that regulations bringing about this result are necessary and must be in conformity with the general provisions of the Federal Reserve Act and with the statutes of the several States in which the member banks operate. The members of the Council regret, however, that it has been thought necessary to suggest regulations so rigid and so involved. It is the unanimous feeling of the members that the present rigidity is likely, with a large number of banks, completely to defeat their intended purpose.

The members of the Council endeavor in the following memorandum to point out what seem to them the most important points of criticism, but feel that specific suggestions are of far less importance than their general criticism that the proposed regulations should be greatly simplified.

One more general observation should be made. The members of the Council have assumed that Regulation F and the proposed amendments are not intended to affect agency accounts for which the trust institutions have no fiduciary responsibility other than that of custodianship and the general obligation to follow such instructions as are specifically given by those who have established the agency.

The specific points to be touched upon ~~will~~ be treated by reference to page and paragraph in the tentative draft of amendment sent with Mr. Bethea's letter and identified by the serial number L-501.

Page 2, line 2, Section 10(c)(2). The Council suggests that the words "sole trustee" should be "a trustee". As drawn, the amendment eliminates co-trusteeships even though the instrument creating the trust, such as a will, could not be changed under any circumstances. It also raises some question as to whether or not the spirit of the regulation would be violated if common trust fund investments otherwise proper were made in those cases where the trustee is required to consult with a third party prior to investing or reinvesting. The Council can see no reason why a bank which acts as sole trustee should be permitted to invest in participations in a common trust fund but should be debarred from such investment if a testator or a living trustor has seen fit to name a co-trustee.

Page 2, line 8, Section 10(c)(2). The Council suggests that the word "and" should be "or". It is unlikely that the laws of any State specifically forbid such investments in a voluntary trust and, on the

other hand, it may be some time before any large number of States specifically authorize such investments in either testamentary or voluntary trusts. When the statutes are silent on the subject a testator or a living trustor ought to be allowed to authorize such investments. It should be considered whether it is not sufficient that such funds are not prohibited by State law, as is provided in connection with the section dealing with collective investment of small cash balances.

Page 3, line 5, Section 11(b). The Council suggests three million dollars as a proper minimum of trust assets which must be held by trust institutions desiring to undertake the management of a common trust fund.

Page 3, line 8, Section 11(b). The Council suggests one million dollars as the minimum aggregate capital and surplus which a fiduciary institution must hold to entitle it to undertake the management of a common fund.

Page 3, lines 13 and 14, Section 11(c). The Council considers that the language of this paragraph is not entirely clear. It has assumed, however, that the correct interpretation is that the word "Funds" in line 13 is intended to read "Fund". On this assumption, the Council suggests five hundred thousand dollars as an appropriate limitation on the size of a single common trust. If the Council is mistaken in its assumption and it is intended to impose a limit upon the aggregate value of assets in all of the several common funds which may be administered by any trust institution, the Council feels that no limitation whatever should properly be imposed as the propriety

of such limitation must in any case depend upon the size of the institution and the total amount of trust funds held by it.

Page 5, paragraph beginning with line 4, Section 11(f). The Council is not clear as to the meaning of the first four lines of this paragraph, and for that reason is not prepared to comment upon its effect. It suggests that the meaning be elucidated.

Pages 5 and 6, and page 9, Section 11(h) and (m). These two subsections provide for frequent audits, which the Council recognizes as perfectly proper, and call for the furnishing of copies to persons having an interest, which is also unexceptionable. They provide, however, that the cost of the audit and the cost of furnishing the copies shall be at the expense of the bank and these rules are made so strict that the bank cannot in any way be reimbursed. It seems to the Council that these provisions are unfair and unreasonable. The underlying purpose of the common trust fund is not the convenience or pleasure of the bank but the welfare and the positive benefit of the several cestui que trusts. There seems no apparent reason why the bank should bear the cost of the advantage to the beneficiary. It is the belief of the Council that all such out-of-pocket expenses in connection with the administration of a common trust fund should be charged against the fund as an operating expense.

The Council also calls attention to an ambiguity as to compensation to the managing bank. The Council assumes that it is not intended to prohibit compensation from the several participating trusts but

only to prohibit possible double compensation. The Council suggests that this point should be clarified.

Page 6, line 3, Section 11(h). The Council suggests that the words "purchases or sales" should read "purchases and sales".

Page 6, last line, et seq., Section 11(i). At the bottom of page 6 it is provided that no participation shall be admitted to the common fund or terminated except on the basis of a valuation, and in determining such valuation allowance should be made for income accrued on the assets of the common fund to the date of such termination. This presents some accounting difficulties. The funds to be invested are principal funds. If accrued income enters into the calculation, as it should, just as in a bond purchase, the income accrued should not affect the principal investment but should call for an advance from the income fund of the participating trust.

Page 8, lines 9 to 11, Section 11(j). These three lines provide that participations in a common fund shall not be assignable or transferable except to the common fund for the purpose of termination of such participation. The Council believes that so strict a rule is undesirable and unnecessary. It can see no reasonable objection to the assignment of a participation from one trust to another if made at the time of the regular periodic valuation of the assets and provided that the participation is a proper one for the substituted trust to take.

Page 8, lines 6 and 7, Section 11(k). In the sixth and seventh lines of this subsection the word "marketable" is used. As the word

"marketable" is subject to many constructions, it ought to be defined in the regulations or else definitely left to the judgment of the trust investment committee. It is the opinion of the Council that, owing to the difficulties of definition, this should be left to the judgment of the trust investment committee.

Page 8, Section 11(k). The Council is unable to understand the meaning of the last sentence of this subparagraph.

There are two paragraphs of Mr. Bethea's letter of September 18 addressed to the Presidents of all Federal Reserve banks which seem to the Council to require further consideration. These paragraphs relate to the provisions of subsections (b) and (c) of Section 6 of Regulation F. It is explicitly stated in this letter that the provisions of subsection (c) relating to a trust investment committee contemplate that there shall be only one such committee for each bank.

The members of the Council feel that if this is a true interpretation of the present regulations they are entirely too restrictive and should be amended. The attention of the Council was specifically called to one large institution with more than fifty million dollars of trust funds which has found it expedient to appoint three trust investment committees, upon each of which the same three executive officers serve together with two different directors. The bank in question feels that by the adoption of this method the trusts which are allotted to each of these several committees secure not only the desirable continuity of management but also secure a much greater degree of knowledge and interest on the part of the director members than would be possible if

the same directors were required to supervise all trust assets.

It is suggested that subsection (b) of Regulation F be amended so as to allow the committee approving the acceptance of trust accounts to be composed of either officers or directors or both. It is difficult as a matter of practical operation to have a committee consisting solely of directors for this purpose, and furthermore it is believed that experienced officers are better able to pass upon the desirability of proffered trusts than are the directors.

It is also suggested that the provisions of subsection (c) of Section 6 of Regulation F, relating to the trust investment committee, be amended to provide for alternates who may serve in place of the regular members of the committee when the regular members are unable to serve on account of illness, absence from the bank, or other duties. It may be that the informal rulings which have taken place are regarded by the Board as sufficient to effect this purpose.