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National Advisory Council
Document No. 261
October 22, 1946

MEMORANDUM To: National Advisory Council

From: Secretary of the Council

Subject: Flotation of Securities of the International Bank

The attached report from Mr. Collado, dealing with some problems facing the International Bank in the issuing of its securities, is transmitted for the information of Council members in connection with the discussions to be held at the joint meeting with the Aldrich Committee on October 28, 1946.

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MEMORANDUM To: National Advisory Council

From: Mr. E. G. Collado, U. S. Executive Director,
International Bank

Subject: Report No. 21 on Activities of the International
Bank

There is attached a survey, prepared by Mr. Corbett, of the staff of the International Bank, of problems facing the International Bank in the issuing of its securities.

Attachment.

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SURVEY OF PROBLEMS FACING THE INTERNATIONAL
BANK IN THE ISSUE OF ITS SECURITIES

I.

Before the International Bank can safely make appreciable loan commitments, it must be able to market its obligations in member countries capable of exporting capital. The principal country is the United States, and in this country significant legal and regulatory barriers exist which render the obligations of the Bank ineligible for purchase by the principal fiduciary investors. These obstructions take several forms, the most noteworthy of which are failure of the Bank's obligations to qualify as "legal investments" under State laws governing insurance companies, mutual savings banks, and building and loan associations; absence of regulatory rulings on the part of national banking authorities (the Comptroller of the Currency, the F.D.I.C.): registration under the Securities Acts of 1933 and 1934; statutory limitations on the amount of funds that may be invested by national and State banks; and, finally, State "blue sky" laws.

Mr. E. G. Collado, U. S. Executive Director, has recently undertaken, for the National Advisory Council, the task of obtaining eligibility for the Bank's obligations for purchase by the various State and national financial institutions. He may count upon the assistance of the Council, U. S. Government agencies, and the staff of the Bank.

The complexity of the problem cannot be underestimated. The variety in State laws is great; the number of associations, groups, and authorities involved (and which must be reached) are many; the time element is important, because all but four of the State legislatures meet in January and, then, are only in session for relatively short periods. Thus, the whole attack on the problem must be on a broad front. Failure of the Bank's obligations to be made "eligible" in certain states for purchase by certain investors would materially limit the potential market for the Bank's obligations.

II.

Numerous steps have been taken and the ultimate and satisfactory solution of the problem has been brought much nearer. Much remains to be done and definite plans must be laid if substantial success is to be obtained.

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The National Advisory Council authorized a small working party to study the problem of eligibility of the Bank's obligations and to bring the matter to the attention of banking and insurance authorities in the states as well as the principal banking and insurance interests. Work was done in New York, Massachusetts, and New Jersey, and considerable interest was stimulated. In New York, the Savings Bank Association was most active and succeeded in securing the passage of enabling legislation in the 1946 session. In all other states, and on insurance in New York, no action was taken. The lateness of the approach relative to the sessions of the legislatures and the general lack of information on the Bank and its obligations were primarily responsible for the lack of success, although this preliminary step cannot be underestimated.

This subcommittee of the National Advisory Council also instituted a survey of State bank laws to determine the eligibility of the Bank's securities in the various states. This survey was conducted by the National Association of Supervisors of State Banks. The survey was only recently completed and the results will be discussed in detail later in this report.

The Life Insurance Association of America volunteered its services in making a survey of laws governing investments by insurance companies in various states, with particular reference to the eligibility of the Bank's securities. This group completed a preliminary study, the results of which were received by Mr. Collado in July. Attempts have been made to obtain the final and detailed report of the Association. Thus far, this report has not been forthcoming.

Mr. Collado was invited to speak at the convention of the National Association of Insurance Commissioners in June but found it impossible to attend the session, and, in his stead, Mr. Burke Knapp of the Federal Reserve Board appeared. Since that time, further efforts have been made to establish closer working relationship with the Association.

During the summer, very little work was done on this general problem, although sporadic contact was maintained with interested groups, banks, insurance companies and individuals. Plans were also laid for presentation of a uniform statute to the Council of State Governments. This statute, if adopted by any State, would permit all types of investors in such State to purchase International Bank obligations. In October, Mr. Elting Arnold of the Treasury and Mr. Corbett of the Bank appeared at the Council of State Governments meeting in Chicago at which the proposed uniform statute was presented. The Council adopted the statute for presentation at regional meetings, but appended a paragraph to the effect that the statute indicated the scope of the problem but did not appear completely suitable as a means of amending State investment laws. It should be pointed out that the Council does not necessarily endorse the substance of the statute but does indicate that it is a suitable matter to be considered by State Governments.

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Mr. Corbett, on the same trip, also made visits to Madison, Wisconsin; St. Louis, Missouri; and Cincinnati, Ohio. In Wisconsin, where the Bank's securities are not eligible, except in token amounts, for investments by State commercial banks, savings banks, and insurance companies, he held discussions with the Commissioners of Banking and Insurance. The officials are reluctant to take any steps which would qualify the Bank's securities for investment purposes, and careful consideration will have to be given to the type of approach, if any, to be made in Wisconsin. In St. Louis, discussion with a representative group indicated that the legislature will take the necessary steps to declare the Bank's securities eligible investments for insurance companies and other investors, when this matter is presented to it.

In Cincinnati, similar discussions were held, and it may also be concluded that favorable action in Ohio will eventually be obtained. It should be pointed out that the Bank's securities are not eligible investments for any type of institutional investor in Ohio, with the possible exception of mutual building and loan associations.

In September, Mr. Collado and Mr. Corbett made a two-day trip to New York, where discussions were held with various insurance companies and banks. The net result of these discussions was to confirm the impression that New York insurance companies would not take the lead in introducing legislation in New York to qualify the Bank's securities for insurance company investment, but would lend their support in the passage of such legislation once introduced. It appears that no great problem will be encountered in New Jersey, and a pledge of full support was received from the Prudential Insurance Company. A number of discussions were held with commercial bankers regarding distribution of the Bank's securities and the general role to be played by commercial banks in the financing of the International Bank. A brief discussion was held with Mr. Eugene R. Black, Vice President of the Chase National Bank, concerning the possible aid which might be rendered by the "Aldrich Committee."

The Aldrich Committee, in its meeting in Washington on September 26, devoted considerable time to discussion of the eligibility of the Bank's securities in the States, and also to the effect of present limitations upon national and member banks regarding dealing and investment in the International Bank's securities. Another meeting on this problem will be held in Washington October 22. Following this meeting, Mr. Collado held extensive discussions with Mr. Tom K. Smith, President, Boatmen's National Bank, and Mr. L. M. Giannini, President of the Bank of America. After a lapse of several months, contact has been reestablished with the Comptroller of the Currency regarding a pre-issue ruling on eligibility of the Bank's securities for purchase by national banks. This matter will be discussed in greater detail in the appended memorandum.

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Meetings have also been resumed with the Securities and Exchange Commission, on the subject of registration of the Bank's securities. Very close contact has been maintained with the SEC at all times in an informal manner by Mr. Collado. Recently, it has appeared advisable to advance discussions on the type of registration required for the issuing of securities by the Bank. A preliminary meeting has been held by representatives of the Securities and Exchange Commission and Mr. McLain, General Counsel of the Bank. It might be noted at this point, an SEC study indicates that registration of the Bank's securities will be of considerable assistance in meeting statutory requirements of State "blue sky" laws.

A fairly detailed review of the current position of the Bank's securities in the various states was given to Dr. Randolph Burgess, prior to his attendance at the Chicago convention of the American Bankers Association. During the course of his speech at the convention, he had occasion to bring this problem of eligibility of the Bank's securities to the attention of the convention as a whole, and called upon the Association and the individual bankers to render their support.

The American Bar Association has formed a subcommittee on Bretton Woods institutions, and this group, under the chairmanship of Mr. Charles Taft of Cincinnati, has repeatedly offered its assistance to the Bank. During Mr. Corbett's trip to St. Louis and Cincinnati, Mr. Taft and another member of his committee arranged very useful meetings. It is believed that committee members in other states will be able to render the same type of assistance.

Mr. Collado has talked with Mr. Vogeliuss of Moody's Rating Service regarding the rating of International Bank securities. This talk was purely exploratory, but it bears on the eligibility of the Bank's securities in a number of states where a satisfactory rating by these bond services is one of the statutory requirements for an investment security.

Finally, the NAC is planning to establish a small working committee to investigate and correlate the activities of the principal Federal agencies having to do with the Bank's securities. This committee will investigate the desirability of a pre-issue ruling by the Comptroller, as well as the advisability of amending national laws to permit distribution by commercial banks.

III.

It is necessary at this point to devote some attention to a plan of operations designed to qualify the Bank's securities as eligible investments for principal investors in the most important states. While the ultimate objective is to obtain legislation in all the states for all types of

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investors, it must be recognized that only a relatively small number of states are of financial importance. It must also be recognized that success in obtaining favorable legislation in any state depends a great deal upon personal approaches to the various interested groups and authorities. Therefore, considering the limited personnel available to approach the various states, it will be necessary to exercise some economies in the use of personnel. In other words, efforts must be directed to those areas where the potential return is greatest.

Some states are recognized leaders in matters of investment laws governing fiduciary investors. Among these are Massachusetts, New York, New Jersey, Connecticut, and Pennsylvania. These are likewise states which offer the greatest potential market for the Bank's securities -- at least in the immediate future. Many states follow the actions of these states in matters of legislation on securities, and it is believed that if substantial success is obtained in these states other areas not so familiar with the International Bank will be more inclined to adopt favorable legislation.

Present plans are for Mr. Collado to visit each of these states. In New York, Mr. Robert Dineen, Superintendent of Insurance, and Mr. Shelby Davis, his Deputy, have both been seen. They will be visited again in the coming months. The hope is that the enabling legislation on insurance companies will be included in the Governor's program in New York, which would facilitate its passage. Conversations have been held with Mr. George L. Harrison of New York Life and Mr. Lewis W. Douglas of Mutual Life of New York. A meeting is also planned with the legislative committee of the Life Insurance Association, to determine just what role it will play. This committee is headed by Mr. Charles G. Taylor, Executive Vice President of Metropolitan Life Insurance Company. The importance of obtaining the necessary legislation in New York State cannot be overemphasized. In New Jersey, a meeting has been held with Mr. Donald Cruse of the Prudential Insurance Company. Mr. Cruse volunteered the cooperation of the Prudential, which will, no doubt, prove most useful. Mr. Collado and Mr. Corbett will see the Commissioner of Insurance and Banking in Trenton on October 23, 1946. There is no reason to believe there will be any appreciable difficulty in having appropriate legislation on insurance companies and savings banks introduced and approved in New Jersey. In Pennsylvania, a member of the American Bar Association Committee on the Bretton Woods Agreements, Mr. Robert Dockert of Philadelphia, will be consulted on the principal people and institutions, other than the State authorities, to be seen in that state. Inasmuch as the NAC subcommittee has already established relations with the Commissioners of Banking and Insurance in Massachusetts, these will be further developed. Meetings also were held with Massachusetts insurance company executives and these preliminary conversations will be renewed and extended. The New York insurance companies should be able to make valuable suggestions as to companies and persons to be seen in Massachusetts.

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A list of insurance companies and savings banks to be visited in Connecticut will be developed and these, as well as the Commissioners of Banking and Insurance, will be seen in November.

State banking and insurance commissioners are, in general, extremely sensitive to the views of the principal banks and insurance companies, as well as to the views of the associations of which these institutions are members. As a practical matter, it might be said that no legislation introduced in any State legislature would have a significant change of success unless supported by these institutions and associations. Therefore, considerable attention will be devoted to enlisting the active aid and support of the banking and insurance associations. Fairly detailed plans will have to be worked out as to the form this assistance will take. In general, it is hoped that the banking and insurance groups can be prevailed upon to take the lead in preparing, endorsing, and supporting the necessary legislation, as was done by the Mutual Savings Bank Association in New York. When such initiative is not forthcoming, every effort will be made to secure the support of these groups after the matter has been placed in the hands of the State authorities.

Plans will also have to be made to make the greatest possible use of such groups as the American Bar Association and the Aldrich Committee. It is not always easy to fit these less specialized but interested groups into the general scheme, but there is adequate reason to believe that they can be of use and, by all means, should be cultivated.

It will be necessary in some states to rely primarily upon the principal financial institutions, such as the Northwestern Mutual Life Insurance Company in Wisconsin and the Bank of America in California. If such institutions will take an active role, it is felt that the results will be, in many cases, greater than those deriving from a direct government approach.

As for the remainder of the states to which personal visits cannot be made, reliance will be placed upon the statute submitted to the Council of State Governments. There is reason to doubt the total success of this method, but it is possible that with the aid of state banking associations and other such groups, some favorable action may be obtained. In any event, it is doubtful if these states will want to keep International Bank obligations ineligible for investment purposes after the principal states have acted. It is entirely probable that the states which do not act in 1947 will take the necessary action in 1948, after the Bank's bonds have been purchased by large and respected financial institutions in the principal states.

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The matter of obtaining enabling legislation in the states would be facilitated by a more widespread knowledge of the Bank and its obligations. This lack of awareness is not as great a handicap at the present as it will be during the period when the bonds are being marketed. Every opportunity should be seized to obtain favorable publicity for the Bank, and in this task the U. S. Government and the International Bank can both do useful work. Particular attention should be devoted to those publications which have special appeal to investors. The information disseminated should be current, as well as historical.

APPENDIX ON PRINCIPAL POTENTIAL INVESTORSState Bank and Trust Companies:

The survey of State banks and trust companies indicates that the Bank's securities and its guarantees are not recognized as legal investments in 12 states, the most important of which are Ohio, Wisconsin and Connecticut. Investigations made by a member of the Bank's staff would indicate that chances of enabling legislation being passed in Ohio are good: in Wisconsin, poor. Word has been received by the Federal Reserve Board that the Connecticut State Bankers Association is working on a change in that state's legislation. The remaining 9 states are not important financially and no particular attention is being given them. In very few instances are State laws more restrictive than paragraph 7 of R.S. 5136, with respect to the amount of funds that a bank may invest. Since many State banks are members of the Federal Reserve System, they are governed by national statutes on investments.

National Banks:

The only obstacle to be overcome here in qualifying the Bank's securities for investment is to have the Comptroller of the Currency rule them "investment securities." While it is fairly certain that he will do so, it is also important that a decision be reached as to when this ruling will be forthcoming. It would be contrary to custom for the Comptroller to issue a "pre-sale" ruling, but there are strong reasons recommending such a course. A staff committee of the National Advisory Council is being created to explore this matter. Among the advantages of an early ruling from the Comptroller would be to remove doubt as to the eligibility of the Bank's securities for purchase by national and State member banks and to encourage State authorities to take necessary action to legalize the Bank's securities for investment by State-controlled financial institutions.

Mutual Savings Banks:

There are mutual savings banks in 17 states: in other states, savings deposits are held by State and national banks, which banks are subject to the laws and rulings discussed above. The laws governing the investment of assets by savings banks are similar to those governing insurance company investments. Very little discretion is allowed as to the type of security eligible for purchase by a savings bank. If a security is not listed by name or type, there is usually no general banking authority or "prudent man" section in savings bank laws which would permit purchase. Furthermore, eligibility of a security or a type of security is usually a statutory matter and enabling legislation is required to legalize a security which does not fall into any of the established groups. The securities of the International Bank are faced with this condition. The excellent preparatory work of the NAC sub-committee, and the energetic interest of the New York mutual savings banks,

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resulted in the issued and guaranteed obligations of the International Bank being made legal investments for New York savings banks in the last session of the New York legislation. The assets of the New York mutual savings banks are approximately one-half of all mutual savings bank assets in the country. Maryland and Delaware likewise permit investment in the Bank's obligations by virtue of liberal laws - that is to say, laws which allow banks to exercise the judgment of a "prudent man" in making their investments. It is not anticipated that any great difficulty will be encountered in New Jersey in obtaining an amendment of existing laws. No recent work has been done in Massachusetts, but visits are planned there as well as to Pennsylvania and Connecticut, in the near future. Conversations held in Wisconsin make chances of "legalizing" the Bank's securities appear dim, while the opposite is the case in Ohio. The foregoing are the principal states have mutual savings banks.

Life Insurance Companies:

A preliminary study of State laws governing investments by insurance companies has been received from a committee of the Life Insurance Association. This study has proved to be of little use, beyond confirming the existing impression that life insurance companies can now make, at most, only token purchases of the Bank's securities. As in the case of mutual savings banks, laws governing investment by insurance companies are fairly specific and restrictive, and it will be necessary, usually, to have legislation before the Bank's obligations become eligible. In addition to the work done by the NAC subcommittee last January and February, Mr. E. G. Collado has held discussions with insurance company executives in New York and New Jersey. Visits to Massachusetts, Connecticut, and Pennsylvania are also planned.

Mutual Building and Loan Associations:

Relatively little work has been done on this class of investor. It is not thought that this will constitute a very important class because of the general nature of the activities of such associations. Most of their assets are in the form of loans on real estate, while such idle cash as they have is placed in U. S. Governments. It is also believed that if the Bank's securities become legal investments for mutual savings banks and life insurance companies, it will be a small and simple step to have them legalized for these associations.

Fire and Casualty Insurance Companies:

If anything, the laws governing these groups are more liberal than for life companies, and if a State is willing to broaden its legislation for life companies there is no reason to believe that they will not also take the same step for the fire and casualty companies.

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Trusts:

Reference is had here to trusts administered by banks, trust companies, and individuals. There seems to be little likelihood that important trusts exist which do not allow trustees to exercise judgment sufficiently broad to permit purchase of the Bank's securities. Once again, if States are willing to amend laws on insurance companies and savings banks, there is no reason to believe that trust laws would not be similarly amended. This would cover those trusts where no instrument exists.