

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

April 25, 1947.

The Honorable Charles W. Tobey,
Chairman, Committee on Banking
and Currency,
United States Senate,
Washington, D. C.

My dear Mr. Chairman:

During recent hearings before your Committee on the bill S. 408, relating to guarantees of business loans by the Federal Reserve Banks, there was read into the record a letter addressed to you by Mr. William C. Foster, Acting Secretary of Commerce, dated March 25, 1947, with respect to the merits of that bill.

The Board is pleased to note that Mr. Foster believes that this bill provides a sound basis for the expansion of much needed small business credit facilities and that he endorses the approach to the problem represented by the bill. The letter suggests that the Committee may wish to consider the desirability of including in the bill certain directives, with respect to which the Board would like to express its views.

Regarding the suggestion that consideration be given to the inclusion in the bill of specific lending standards, it is contemplated that limitations relating to interest rates, maturity, and other similar matters would be covered by regulations prescribed by the Board of Governors. The Board believes that the incorporation of specific or rigid requirements in the law itself would tend to impede the flexible administration of the bill. Experience has indicated that it is almost impossible to anticipate the detailed limitations which may be desirable in the future; and if the law should specifically prescribe lending requirements and standards it would doubtless be necessary at a later date to change or clarify them by amendments to the statute. In fact, it might be desirable in times of severe economic depression to have quite different conditions and limitations surrounding the guaranteeing of loans from those appropriate for times like the present.

The Commerce Department's letter expresses the view that special attention should be given to the fixing of a reasonable maximum

interest rate and indicates that 4 per cent would not be considered an unreasonable maximum. The Board feels that flexibility is desirable and that maximum interest rates should be left to be prescribed by regulations from time to time in the light of changing credit conditions and business needs. There may be instances in which a 4 per cent rate of interest would not adequately compensate a lending bank for the supervision and servicing required in connection with a small loan; and the fixing of such a maximum rate might tend to make banks reluctant to extend credit in such cases and might consequently have the effect of defeating the objectives of the bill.

With respect to the suggestion that the bill S. 408 might include an express statement of small business or anti-monopoly objectives, the Board feels that there would be no necessity for including this expressly in the light of the explicit purposes of the bill. Anti-monopoly objectives have been stated in other statutes enacted by Congress; and the Federal Reserve Banks and the Board of Governors, of course, would administer the bill in conformity with those objectives.

The letter also suggests that consideration might be given to an amendment which would permit direct loans under exceptional circumstances, but expresses doubt as to the necessity or desirability for such a provision. On principle, the Board feels strongly that private banks should originate and make loans to business enterprises and that legislation should not now provide for direct loans by the Federal Reserve Banks or by any other governmental agency. Under the bill, the Reserve Banks would not be placed in competition with the private banking system. They would be authorized to make only partial guarantees of loans and then only upon the request of a local bank. Credit judgment and responsibility would and should remain primarily with the lending banks which are fully acquainted with the character, capability, and capacity of their customers.

The Board is glad to have the Commerce Department's support for this bill. We have considered carefully the suggested amendments, and have concluded that the bill does not require additional safeguards and would be more workable and practical without further amendments.

Sincerely yours,

(Signed) Ernest G. Draper

Ernest G. Draper,
Chairman Pro Tem.