

The meeting of the Federal Open Market Committee was recon-  
vened in the offices of the Board of Governors of the Federal Reserve  
System in Washington on November 30, 1937, at 10:40 a.m.

PRESENT: Mr. Eccles, Chairman  
Mr. Harrison, Vice Chairman  
Mr. Szymczak  
Mr. McKee  
Mr. Ransom  
Mr. Davis  
Mr. Sinclair  
Mr. McKinney  
Mr. Martin  
Mr. Day

Mr. Morrill, Secretary  
Mr. Wyatt, General Counsel  
Mr. Dreibelbis, Assistant General Counsel  
Mr. Burgess, Manager of the System Open  
Market Account  
Mr. Carpenter, Assistant Secretary of the  
Board of Governors of the Federal Re-  
serve System

ALSO PRESENT: Mr. Young, President of the Federal Reserve  
Bank of Boston  
Mr. Smead, Chief of the Division of Bank  
Operations of the Board of Governors of  
the Federal Reserve System

Reference was made to the request of the Presidents' Confer-  
ence at its meeting on June 7, 1937, that Messrs. Smead and Burgess  
continue their studies to determine whether a more satisfactory  
formula for the adjustment of participations of Federal reserve banks  
in the System open market account could be devised, and to the under-  
standing reached at the meeting of the executive committee of the  
Federal Open Market Committee on July 6 that President Young of the  
Federal Reserve Bank of Boston would be invited to meet with the

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Federal Open Market Committee for the purpose of outlining his views with respect to the formula used for the reallocation of participations in the System account.

Mr. Burgess read a report which had been prepared by him and Mr. Smead for consideration by the Committee and which recommended the continuation of the present formula (based on the principle that the security holdings should be divided among the Federal reserve banks in relation to their need for earnings to meet expenses, regular charge-offs, prior service contributions, and dividends) with one minor change which would provide that profits and losses on transactions in the System account would be allocated among the reserve banks on the basis of their average holdings in the account since July 1, 1936, rather than on the basis of average holdings in the twelve months preceding any transaction. The report stated that consideration had been given to a proposal for distributing securities, after needs for expenses and dividends had been met, in such manner as to gradually bring about and then maintain a uniform relationship of surplus and reserves for contingencies to paid-in capital at the reserve banks; that, since earnings of the Federal reserve banks may be substantially in excess of expense and dividend requirements, a distribution of securities in such manner as to bring about substantial relative equality among the Federal reserve banks in their ability to absorb extraordinary losses without impairment of capital is, of course, desirable; but that such a formula had not yet been perfected.

The proposed accounting system for handling transactions in accordance with the suggested formula was as follows:

"1. As securities are purchased or sold the New York bank will charge or credit the cost of proceeds of all purchases or sales to accounts carried on its books as follows:

- 'A' System Open Market Account (par value only)
- 'B' Premium on Securities
- 'C' Discount on Securities
- 'D' Interest Accrued

"2. The (a) par amount, (b) premium, (c) discount, and (d) interest accrued on all securities purchased or sold will be prorated by the New York bank to each reserve bank on percentages based on the formula given in paragraph 10 below; and settlement therefor will be made with each reserve bank through the inter-district settlement fund.

"3. Each Reserve bank will carry on its books the following accounts:

- 'A' Participation in System Open Market Account (par value only)
- 'B' Premium on Securities
- 'C' Discount on Securities
- 'D' Interest Accrued

and on its balance sheet form 34, the par value of its participation will be carried under caption 'Participation in System Open Market Account,' the premium and interest accrued under caption 'Miscellaneous Assets,' and the discount under caption 'Miscellaneous Liabilities.'

"4. Adjustments in participation will be made at book values, settlement being made with the New York bank through the inter-district settlement fund in the same manner as for purchases and sales.

"5. The New York bank will maintain memorandum bookkeeping records showing (1) the amount of premium, discount, and interest accrued daily on each issue of securities held in the Account, (2) for the entire account the total amount of premium, discount, and interest accrued (separately), and each reserve bank's pro rata share of the total of each of these three items. (Premium is amortized to earliest callable date and discount to maturity.)

"6. The New York bank will figure the accruals of earnings each day on the entire amount of holdings in the System Open Market Account and each reserve bank's pro rata share, and will advise each bank by telegram the amounts of (1) Premium Amortization, (2) Discount Accrual, (3) Interest Accrued, and (4) Interest Earned on U. S. Government Direct Obligations, on its

"participation. Each reserve bank will accrue earnings on its books daily on this basis. (In order to facilitate handling the System Account, this information will be furnished one day late, except on the last day of the month when two days' earnings will be accrued.) Upon the collection of coupons on interest payment dates, the New York bank will credit each bank through the inter-district settlement fund with its pro rata share of such payments, and each bank will credit this amount in its Accrued Interest Account.

"7. Profits or losses on sales of securities will be distributed among the reserve banks as they occur on the basis of daily average holdings in the Account since July 1, 1936. (The amount of profit or loss on a sale is determined by the difference between the book value and the sale price at the time of sale.)

"8. When purchases and sales are made in other districts, cash settlement in full will be made with the New York bank and the operation will be carried through in the same manner as though it had been made in New York in the first instance.

"9. Securities purchased for the Account, or vault receipts in case the securities are held by other Federal reserve banks, will be retained at the New York bank. The securities will be lodged in a vault compartment apart from all other securities of the bank, except that on proper authority amounts will be held in joint custody of the Federal Reserve Bank and the Federal Reserve Agent as security for note issues.

"10. Adjustments in participations of the several Federal Reserve banks in the System Open Market Account will be made quarterly as of January 1, April 1, July 1, and October 1 of each year in accordance with the following formula:

- A. Expenses
  1. Estimated current expenses during year
  2. Prior service contribution
  3. Total
- B. Earnings
  1. Current earnings to date of allocation
  2. Estimated for remainder of year (exclusive of earnings on Govts.)
  3. Net profit on Govts. sold to date
  4. Total
- C. Excess of A-3 over B-4
- D. Allocation required (on basis of current annual rate of earnings on Govts.) to furnish earnings equal to 'C'

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- "E. Estimated Dividend requirements (a)
- F. Allocation of remainder of System Account in proportion to 'E'
- G. Total allocation (D + F)
- (a) Accrued dividends to date plus 6 percent per annum on current paid-in capital for remainder of year."

The report suggested that the plan be sent to the Federal reserve banks for their comments and suggestions and that when these have been received and met as fully as possible, so that a large majority of the reserve banks shall have approved the plan, the plan be put into effect by the Federal Open Market Committee requesting the banks to make the necessary adjustments as of January 1, 1938, and quarterly thereafter, subject to the understanding that each reserve bank would be free at any time to ask for a reconsideration of the plan.

Chairman Eccles then invited Mr. Young to express his views. Mr. Young stated that in his opinion Section 12A of the Federal Reserve Act, as amended by the Banking Act of 1935, provides that authority over open market operations by the Federal reserve banks rests exclusively with the Federal Open Market Committee, but that he felt certain that the Committee would not take any action under that authority that was inequitable or unreasonable. He said that the Federal Reserve Bank of Boston had accepted the law and the regulations of the Federal Open Market Committee on that basis and the directors of the bank had been advised that the responsibility for purchases and sales of securities and shifts of securities in the System account was with the Federal Open Market Committee and that, therefore, the Federal Reserve Bank of Boston need not approve or disapprove such transactions. He added that he had not declined to participate in any

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open market transactions engaged in by the Federal reserve banks but he had protested against the use of a formula for the allocation of securities which would require his bank to take securities at a higher price than they could be purchased for in the open market, that originally he had asked authority from the board of directors of the bank to put through transactions when directed to do so by the Federal Open Market Committee, and that when the question arose whether the action of the Committee with respect to reallocation of securities in the account was in the nature of a direction or a request to his bank he felt that the matter should be definitely determined before further reallocations were effected. He also said that if the Federal Reserve Bank of Boston were directed to accept a larger participation in the System open market account at appreciably higher prices than the securities could be purchased for in the open market his bank would probably accept the participation but only under vigorous protest.

Reference was made during the ensuing discussion to the questions which had been raised as to the authority of the Federal Open Market Committee to make allocations and reallocations of securities in the System open market account and to require the Federal reserve banks to execute such allocations and reallocations. In this connection there was presented a memorandum prepared by Mr. Wyatt under date of November 26, 1937, in which it was stated that the Federal Open Market Committee had the legal power to continue to allocate the System open market account among all Federal reserve banks, to require each Federal reserve

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bank to accept its pro rata participation, and from time to time to reallocate such account and require some federal reserve banks to relinquish part of their participations and others to accept increased participations, all in substantial accordance with the practices which had been in effect since 1929, whereby such allocations and reallocations are based on the current needs of each Federal reserve bank for earnings and whereby transfers of participations are made on the basis of the book value of the securities in the account instead of the current market price.

Mr. Harrison suggested that, in the light of Counsel's opinion, Messrs. Smead and Burgess consider the desirability of amending their report to provide that, after the comments and suggestions of the Federal reserve banks had been received, the formula recommended in the report be put into effect by the Federal Open Market Committee directing, instead of requesting, that the Federal reserve banks make the necessary adjustments as of January 1, 1938, and quarterly thereafter, it being understood that each Federal reserve bank would be free at any time to ask for a reconsideration of the present plan or to make suggestions or criticisms of any later plan which might be proposed. Messrs. Smead and Burgess stated that they would be willing to amend their report as suggested.

Thereupon Messrs. Young and Smead withdrew from the meeting.

Upon motion duly made and seconded, it was voted unanimously that, in view of the opinion

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of Counsel referred to above, the report submitted by Messrs. Smead and Burgess be adopted and that the Committee direct that, after the report and Mr. Wyatt's opinion had been submitted to the Federal reserve banks and the comments and suggestions with respect to the proposed formula had been received and met as fully as possible, so that a large majority of the reserve banks shall have approved the plan, the Federal reserve banks, upon receipt of advice from the Secretary of the Federal Open Market Committee, make adjustments in their participations as provided in the formula as of January 1, 1938, and quarterly thereafter.

Upon motion duly made and seconded, and by unanimous vote, the minutes of the meeting of the Federal Open Market Committee on September 11-12, 1937, were approved.

Upon motion duly made and seconded, and by unanimous vote, the actions of the executive committee as set forth in the minutes of the meetings of the executive committee on September 11-12 and November 9, 1937, were approved, ratified and confirmed.

Prior to this meeting Mr. Burgess had sent to each member of the Federal Open Market Committee a report prepared by the Federal Reserve Bank of New York as of November 24, 1937, covering the open market operations conducted by the bank for the System open market account since the meeting of the Federal Open Market Committee on September 11-12, 1937. At this meeting Mr. Burgess reviewed the transactions in the account since November 24, 1937, up to and including November 29, and stated that the report prepared by the New York bank should be changed to show that, as the result of an agreement over the telephone by members of the executive committee since the meeting of the Committee on November 9, purchases totaling only \$37,825,000 were made under the direction given at that meeting.

Upon motion duly made and seconded, and by unanimous vote, the transactions in the System open market account since the previous meeting of the Federal Open Market Committee and up to and including November 29, 1937, were approved, ratified and confirmed.

Reference was made to the fact that the Federal Reserve Banks of Boston and Richmond were holding in "Miscellaneous Assets Acquired in Settlement of Claims Account Closed Banks" \$6,325 and \$52,800, respectively, of bonds of the Home Owners Loan Corporation and the Federal Farm Mortgage Corporation and that it would be necessary for the Committee to decide as to the action to be taken by it in connection with the retention or disposition of the securities by the banks in question.

Upon motion duly made and seconded, and by unanimous vote, it was decided that, in view of the fact that securities acquired by the Federal reserve banks in settlement of claims against closed banks will be in such small amounts as to be unimportant from the standpoint of credit control, the Committee, until otherwise directed by it, would interpose no objection to a Federal reserve bank holding any such securities acquired by the bank, or to the sale of such securities whenever such sale is deemed to be advisable by the holding bank. The Secretary was requested to advise the banks accordingly.

Mr. Ransom recommended that, in view of the changed situation since the appointment of the special committee (Messrs. Ransom, Davis and Sinclair) for the purpose of considering the forms of resolutions adopted by the Federal Open Market Committee, the special committee be discharged until such time as the Federal Open Market Committee might wish to take the matter up again.

Upon motion duly made and seconded, Mr. Ransom's recommendation was approved by unanimous vote.

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Reference was made to discussions at previous meetings of the question as to the desirability of granting authority to the members of the Committee to disclose to alternate members of the Committee and to other Presidents and to directors of their own Federal reserve banks information with respect to the actions taken by the Federal Open Market Committee. Attention was also called to the suggestion made to Mr. Szymczak recently by President Fleming of the Federal Reserve Bank of Cleveland, that the Committee advise the Presidents by telegram of actions taken with respect to which announcements are made to the press. In this connection the representative members of the Committee expressed the feeling that it would be distinctly helpful if they could discuss such matters with their respective alternates and that such a procedure was desirable particularly in order that each alternate might be familiar with the problems of the Committee in the event he was called upon to serve in the absence of a regular member. Mr. Harrison said that he believed the directors as well as the Presidents of all Federal reserve banks should be kept advised of the actions of the Committee.

Upon motion by Mr. Harrison which was duly seconded, it was voted unanimously to request the Chairman to appoint a special committee to consider and submit a recommendation to the full Committee as to the position to be taken with respect to the extent, if any, to which the Presidents and boards of directors of the Federal reserve banks should be advised of discussions and actions of the Federal Open Market Committee.

In accordance with this action, the Chairman appointed Messrs. Szymczak, McKee and Sinclair as members of the special committee.

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At 1:20 p.m. the meeting recessed and reconvened at 2:45 p.m. with the same attendance as at the conclusion of the morning session except that Messrs. Goldenweiser, Williams and Thurston were also in attendance.

There were submitted copies of a draft of statement which had been prepared by Messrs. Goldenweiser, Williams and Thurston in accordance with the understanding at the meeting of the Committee yesterday afternoon and the statement was discussed.

At the conclusion of the discussion the meeting recessed with the understanding that, as the executive committee of the Federal Open Market Committee was to meet with the Secretary of the Treasury Wednesday morning, December 1, 1937, for the purpose of discussing December 15 Treasury financing, the Federal Open Market Committee would reconvene at 2:30 p.m. Wednesday afternoon.

Orestes Morrie  
Secretary.

Approved:

W. S. ...  
Chairman.