

Office Correspondence

FEDERAL RESERVE
BOARDDate May 14, 1935To Governor EcclesSubject: FHA legislative questionsFrom J. M. Daiger

16-852

*Letter
M.D.*

In view of your chance meeting with Mr. McDonald Saturday, I think it would be well for you to know the suggestions that I have made with regard to four legislative proposals involved in the general changes under discussion at the Federal Housing Administration. I made these suggestions last Tuesday at a conference with McDonald, Catharine, Ferguson, and Riefler. The subjects involved are as follows:

1. Authorizing the Federal Housing Administrator to include, in the face amount of a debenture issued against a foreclosed mortgage, interest up to three per cent from the date on which foreclosure proceedings were instituted by the mortgagee, rather than from the date of conveying title to the Federal Housing Administrator, as now provided in the Housing Act.

I suggested that this be taken up immediately with Senator Bulkley, chairman of the Senate Subcommittee in charge of HOLC and FHA amendments, with a view to having it included in the conference report now pending. I pointed out that this would be somewhat irregular, but that in the absence of any objection among the conferees it might nevertheless be done. I pointed out also that this amendment appropriately belonged in the pending HOLC-FHA bill rather than in the banking bill, though I expressed the view that it might later be put forward by Senator Bulkley as an amendment to the banking bill if he should find that, owing to parliamentary rules, it could not be added to the HOLC-FHA bill in conference.

2. Classifying bonds issued against FHA insured mortgages on low-cost-housing projects as investment securities within the terms of Section 5136 of the Revised Statutes, rather than as real estate loans within the terms of Section 24 of the Federal Reserve Act.

I suggested that this be taken up immediately with Mr. Awalt, with a view to having it put forward as an amendment to Title III of the banking

bill. The Comptroller of the Currency has ruled that, under the existing law, bonds issued against FHA insured mortgages on low-cost-housing projects are real estate loans. Hence banks could participate in this kind of financing only by acquiring an entire issue. Furthermore, the bank would be unable to dispose of any part of the issue to its customers.

3. Exempting bonds issued against FHA insured mortgages on low-cost-housing projects from the provisions of Section 77 B of the Bankruptcy Act.

I suggested that there might be a good deal of difficulty about obtaining Administrative consent to reopen the Bankruptcy Act to amendment at this session of Congress, but that the matter might nevertheless be discussed informally with Tom Corcoran or some others familiar with either the Securities Act or the Bankruptcy Act. The point involved is a serious one where the issuing of bonds on low-cost-housing projects is concerned. A prospectus describing such an issue would have to state that the Government guarantee might in practical effect become inoperative in the event of a receivership, since the essence of a corporate reorganization under Section 77 B is the elimination, for most purposes, of the requirement of foreclosure and judicial sale. The Housing Act, on the other hand, makes the mortgagee's right to recover from the FHA dependent on foreclosure. Moreover, the sale of the bonds in the first instance would be made feasible in the main by the reliance of investors on the possibility of ultimate recovery, in an emergency, from the FHA.

4. Authorizing national banks to purchase the stock of national mortgage associations in the same manner in which they are authorized to purchase the stock of the Federal reserve banks, the National Agricultural Credit Corporations, Edge Corporations, etc.

I suggested that consideration of this proposed amendment be deferred until after the Senate and

House conferees reported on the HOLC-FHA amendments now pending. One of these amendments, as you know, provides for increasing the ratio of mortgage association debentures to capital from 10 - 1 to 15 - 1. The House Committee reported this amendment favorably; the Senate Committee rejected it. Senator Bulkley has proposed a compromise of 12 - 1, but what the conference committee will report is still uncertain. Since it appears that the mortgage associations will require a 15 - 1 ratio in order to operate at a profit, it is doubtful that any effort will be made to organize any associations if the pending amendment fails. For this reason I took the position that there would be no point to considering an amendment authorizing national banks to purchase the stock of mortgage associations until it was known whether an effort to organize them would actually be made.