

FOR RELEASE ON DECEMBER 14

STATEMENT BY VICE CHAIRMAN BALDERSTON OF THE
BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
BEFORE THE SUBCOMMITTEE ON SECURITIES OF THE COMMITTEE
ON BANKING AND CURRENCY OF THE SENATE ON MAY 21, 1957

Mr. Chairman and Members of the Committee:

The Board of Governors of the Federal Reserve System appreciates the opportunity to present its views to this Subcommittee. Four of the five bills which we understand that the Subcommittee is considering, S. 594, S. 810, S. 843, and S. 1061, do not directly affect the responsibilities of the Board, and we have no comments to offer with respect to them. Accordingly, we will confine our comments to the remaining bill, S. 1168.

As Chairman Martin stated in testifying before this Subcommittee on a similar bill introduced in the 84th Congress, the Board is in complete agreement with the purposes of S. 1168.

Under the Securities Exchange Act of 1934, corporations whose securities are registered on a national securities exchange are subject to specified requirements covering publication of financial reports and related information, solicitation of proxies, and so-called "insiders' profits" resulting from trading in the company's stock. With certain exceptions, S. 1168 would apply those requirements to corporations with more than \$2,000,000 of assets and 750 stockholders, whether or not their securities are registered on an exchange.

These provisions of S. 1168 would assure for the security holders of such corporations not registered on an exchange, the same information and many of the safeguards that the Securities Exchange Act provides for the holders of securities that are registered on an exchange. As these provisions are administered by the Securities and Exchange Commission, the Commission is better able than the Federal Reserve to express an informed opinion regarding them.

However, section 3 of the bill directly relates to the responsibilities of the Federal Reserve System. Under this section any security covered by the bill, unless excluded by the Board as "not comprehended within its purposes", would be subject to the same margin requirements as the securities that are registered on an exchange.

The bill contains certain exemptions. In addition to bank stocks, the bill would exempt the securities of all corporations that do not have more than \$2 million in assets. It would also exempt any class of equity securities held of record by not more than 750 persons. In addition, it would exempt any debt securities which have not been registered under the Securities Act of 1933, or which are outstanding in a principal amount of not more than \$1 million.

Since securities covered by the bill would be subject to the margin regulations that now apply to securities registered on an exchange, let me outline those rules and how they differ from the rules that apply to unregistered securities.

Under present law, when brokers lend for the purpose of purchasing or carrying securities, they can lend on registered securities the amount specified in the Board's margin regulations--now 30 per cent--but they are forbidden to lend anything at all on unregistered securities. In other words, in a brokerage margin account registered securities have the loan value specified in the Board's regulations and unregistered securities have no loan value whatever. The rules that apply to loans made by banks also distinguish between securities that are registered and those not registered. Loans made by banks to purchase or carry registered securities are subject to the standard margin requirements; loans made by banks to purchase or carry unregistered securities are exempt.

Under S. 1168, securities covered by the bill would be entitled to loan value in brokerage margin accounts just as registered securities are, and loans by banks to purchase or carry securities so covered would be subject to the usual margin requirements.

Stated differently, borrowers upon securities covered by section 3 would be more favored than at present in one respect and less in another. On the one hand, such securities would have loan value in brokerage margin accounts. On the other hand, however, loans by banks to purchase or carry such securities would become subject to the present margin requirements.

Both S. 1168 and the present law regarding margin requirements recognize that there are important differences between the securities of small, closely held companies and larger, more widely-owned ones. The securities of small, closely held companies usually do not enjoy a wide or ready market. They are more likely to be purchased or financed on the basis of personal knowledge of the individual company, its conditions and prospects, and not on the basis of ready marketability. In contrast, the securities of larger, more widely held companies are usually more seasoned, more widely known, more readily marketable, and more likely to be traded on margin.

Section 3 says, in effect, that such securities should be treated for the purposes of the margin requirements in the same way that the law now treats securities that are registered on an exchange. Under the exemptions in the bill, a stock would not be covered unless the issuer of the stock has at least 2 million in assets and there are also more than 750 holders of the stock.

The Board believes section 3 would help to carry out the general purposes of the present law relating to margin requirements and that its enactment would be in the public interest.