FEDERAL RESERVE BANK
OF DALLAS

Dallas, Texas, September 13, 1951

To All Financing Institutions in the
Eleventh Federal Reserve District:

The text of the revision of Bulletin No. 4 of the national Voluntary Credit Restraint Committee, which follows, is being forwarded to you and all other financing institutions in this district at its request.

Yours very truly,

R. R. GILBERT
President

BULLETIN NUMBER 4 (REVISED) OF THE NATIONAL VOLUNTARY CREDIT RESTRAINT COMMITTEE
LOANS ON REAL ESTATE

September 13, 1951

The Voluntary Credit Restraint Committee at its meeting on September 5, 1951, evaluated the experience to date with Bulletin No. 4 covering loans on real estate, and adopted the following statement:

The permanent financing of most new construction will continue to be governed by Regulation X as revised on September 1, 1951, to conform with the provisions of the recently enacted Defense Housing and Community Facilities and Services Act of 1951.

Section 1 of Bulletin No. 4 is revised to recommend, in the case of loans on residential properties of 1- to 4-family units, that loans on existing properties should not exceed the limitations imposed by Regulation X or 66⅔ per cent of the fair value of the property, whichever is greater. This means that on properties the fair value of which is $16,700 or less, the recommended limitations are those imposed by Regulation X (all of which are above 66⅔ per cent); on properties the fair value of which is greater than $16,700, the limitation on borrowing is 66⅔ per cent. In all other respects Bulletin No. 4 remains unchanged.

Experience indicates that two points in Bulletin No. 4 are deserving of special emphasis. First, in determining whether proposed financing conforms to the bulletin, all mortgage indebtedness to be outstanding on the property, including secondary financing, should be taken into account. Second, loans on residential property of more than 4 units and loans on commercial property should be screened as to purpose and loans should not be made unless they are in harmony with the principles of the program. A sale with credit involved not exceeding that recommended in this bulletin is sufficient evidence of proper purpose.

Mortgage lenders, who do not have a regional committee from which to obtain opinions in doubtful cases, may refer questions to the Regional Insurance Voluntary Credit Restraint Committee serving their area.

For the guidance of financing institutions in granting real estate credit encompassed by the voluntary program, Bulletin No. 4, as amended is reprinted on the reverse side.

(Over)

LOANS ON REAL ESTATE

Real estate credit transactions governed by Regulation X, which covers the permanent financing of most new construction and major additions or improvements to existing structures, are not within the area of influence of this voluntary program. Neither does the program apply to FHA or VA loans or to other loans guaranteed or insured or authorized as to purpose by an agency of the United States Government. The program does apply, however, to all other real estate credit transactions. Financing institutions extending such credit are urged to observe the principles and the spirit of the program.

1. **Loans on residential property (1- to 4-family units).** The Committee has been informed that most financing institutions are following conservative lending policies on existing residential properties (1- to 4-family units). The Committee urges all financing institutions to follow such policies and in no case to make a loan on existing property in an amount which would cause the total amount of credit outstanding (primary and all other credit combined) with respect to the property or with respect to the transaction to exceed the limit which Regulation X imposes as to new construction or a limit of 66⅔ per cent of the fair value[1] of the property, whichever of such limits is the greater.[2]

2. **Loans on agricultural property.** While the Committee recognizes that in some instances a loan on agricultural property may be in effect a loan on residential property, the Committee feels that normally such a loan falls in the category of a loan on commercial property (see Section 3 below), and the lender should be guided by the recommendations of that section as to over-all credit limits and purposes.

3. **Loans on residential property (more than 4-family units) and on commercial property.** Loans on residential property (more than 4-family units) and loans on commercial property, such as office buildings, stores, hotels, motels, motor courts, restaurants, etc., should be screened as to purpose and the loan should not be made unless it is in harmony with the principles of the program. If the loan is to be made in connection with a sale of commercial or residential property a determination by the financing institution that the sale and the sale price are bona fide may constitute a sufficient screening of the loan. The Committee conceives that it is not the function of the voluntary credit restraint program to make the transfer of real estate impossible or impracticable, but rather to reduce inflationary pressures by limiting the amount of additional credit created in the process of real estate transfer.

Financing institutions are urged to limit a loan, on any type of property described in this section, whether or not a sale is involved, to an amount which would not cause the total amount of credit outstanding with respect to the property or with respect to the transaction[3] to exceed 66⅔ per cent of the fair value of the property. Also, the Committee urges that financing institutions require an appropriate and substantial amortization of principal.

The Committee recognizes that hardship cases may arise where a 66⅔ per cent loan limitation would not be sound or equitable. Such cases would include a loan to finance the sale of property to close an estate or to pay estate taxes, the refinancing of a maturing mortgage, or the sale of property of a bankrupt company. The Committee makes no recommendation in such cases.

4. **Loans on industrial property.** Loans on industrial property should be screened as to purpose whether or not the loan is to be made in connection with a sale of real property. In this instance, however, there appears to be no need for a percentage limitation on the amount of the loan, since in the industrial field mortgage security usually is merely one of the factors considered by the lender in determining whether to make the loan and often bears comparatively little relation to the amount of the loan.

5. **Sale-lease back arrangements.** The Committee also urges financing institutions to recognize that in most instances a "sale-lease back" arrangement, whereby real property is purchased by a financing institution and leased to the vendor or his nominee, is a substitute for a form of financing and therefore comes within the program and should be screened as to purpose.

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[1] Wherever used in this bulletin, "fair value" means:

1. If the loan is to be made to finance the purchase of real property: The bona fide sale price, or the appraised value of the property securing the loan, whichever is lower;
2. In all other cases: The appraised value of the property securing the loan.

The appraised value should be determined in accordance with sound and established practice in the community. A good definition of "bona fide sale price" is given in Section 2(j) of Regulation X.

[2] As a working rule, the above statement may be interpreted as meaning that where the fair value of the property is $16,700 or less the limits of Regulation X would apply and where such fair value is more than $16,700 the limits of 66⅔ per cent would apply.

[3] If the facts are not already known, the financing institution presumably will want to request the borrower to furnish information as to any other indebtedness or credit existing or contemplated in connection with the transaction.