A meeting of the Board of Governors of the Federal Reserve System was held in Washington on Thursday, November 14, 1935, at 11:30 a.m.

PRESENT: Mr. Thomas, Vice Chairman
Mr. Hamlin
Mr. Miller
Mr. James
Mr. Szymczak

Mr. Morrill, Secretary
Mr. Bethea, Assistant Secretary
Mr. Carpenter, Assistant Secretary

The Board acted upon the following matters:

Letter to Mr. Case, Federal Reserve Agent at the Federal Reserve Bank of New York, reading as follows:

"In connection with its consideration of the application of the 'Clifton Trust Company', Clifton, New Jersey, for a voting permit entitling such bank to vote the stock which it owns or controls of 'The First National Bank of Clifton', Clifton, New Jersey, the Board has determined that such applicant is not engaged, directly or indirectly, as a business in holding the stock of, or managing or controlling, banks, banking associations, savings banks, or trust companies, within the meaning of section 2(c) of the Banking Act of 1933, as amended by section 301 of the Banking Act of 1935, and that, accordingly, the applicant is not a holding company affiliate for any purposes other than those of section 25A of the Federal Reserve Act.

"Inclosed herewith is a letter to the applicant advising it concerning the Board's action in this matter. If, for any reason, you believe that this matter should be reconsidered by the Board, please communicate with the Board at once. Otherwise, you are requested to transmit the inclosed letter to the applicant. A copy of the letter is also inclosed for your files.

"As you will note, the Board expressly reserves the right to make a further determination of this matter at any time on the basis of the then existing facts. In this connection, it is requested that you advise the Board if, at any time, you believe this matter should again be considered by the Board."

Approved unanimously, together with
a letter to the "Clifton Trust Company", Clifton, New Jersey, reading as follows:

"This refers to the application of your company for a voting permit entitling it to vote the stock which it owns or controls of 'The First National Bank of Clifton', Clifton, New Jersey.

The Board understands that your company is engaged in the general banking business and was organized and is operated for that purpose; that your company owns 24.1% of the stock of The First National Bank of Clifton and also owns stock of seven other banks in amounts not exceeding 1% of the outstanding stock in any instance; that only a relatively small portion of your company's assets is invested in bank stock; and that your company was not organized and is not operated for the purpose of managing or controlling banks.

As you perhaps know, section 301 of the Banking Act of 1935 amended section 2(c) of the Banking Act of 1933, defining the term 'holding company affiliate', by adding thereto the following paragraph:

'Notwithstanding the foregoing, the term "holding company affiliate" shall not include (except for the purposes of section 23A of the Federal Reserve Act, as amended) any corporation all of the stock of which is owned by the United States, or any organization which is determined by the Board of Governors of the Federal Reserve System not to be engaged, directly or indirectly, as a business in holding the stock of, or managing or controlling, banks, banking associations, savings banks, or trust companies.'

In view of the above facts, the Board has determined that your company is not engaged, directly or indirectly, as a business in holding the stock of, or managing or controlling, banks, banking associations, savings banks, or trust companies, within the meaning of the above quoted statutory provision, and, therefore, is not a holding company affiliate for any purposes other than those of section 23A of the Federal Reserve Act. Accordingly, it is not necessary for your company to obtain a voting permit in order to vote the stock which it owns or controls of The First National Bank of Clifton and on this basis the Board will give no further consideration to your application for such a permit.

"If, however, your company acquires control over any other bank, or the character of the business of your company, the nature of its assets, or the purpose for which it is operated should at any time differ from the description thereof contained in this letter to an extent which would indicate that it might be engaged as a business in holding the stock of, or managing or controlling, banks, this matter should again be submitted to the Board for its determination. The Board reserves the right to make a further determination of this matter at any time on the basis of the then existing facts."
Letter to Mr. O'Connor, Comptroller of the Currency, reading as follows:

"This refers to Mr. Awalt's letter dated September 27, 1935, with which was inclosed a copy of a proposed draft of regulations governing the purchase of 'investment securities' and further defining the term 'investment securities' as used in Section 5136 of the Revised Statutes, as amended by the Banking Act of 1935. In such letter Mr. Awalt requested the comments of the Board regarding such proposed draft.

"On October 15, 1935, members of the Board's staff conferred with members of your staff regarding the proposed draft of the regulations and at that time submitted detailed written suggestions regarding such draft. On October 25, 1935, a revised draft of the regulations was informally submitted to the Board by your office and the suggestions in this letter are based upon such revised draft. In view of the understanding that only Sections I and II of the revised draft of the regulations are prescribed under the authority of Section 5136 of the Revised Statutes, the suggestions of the Board have been confined to such sections.

"Page 3, paragraph immediately preceding Section I. It is suggested that this paragraph be designated Section I and that the present section numbers be changed accordingly, in order to show that such paragraph is a part of the regulations. It is also suggested that the following sentence be added at the end of such paragraph:

'State member banks are not subject to the provisions of Sections III and IV hereof.'

"The paragraph in its present form states that an obligation can be purchased for a member bank's own account only under the provisions of Sections I and II but it does not state that State member banks are not subject to the provisions of Sections III and IV. It is true that the headings of Sections III and IV mention only national banks but this does not clear up the point, since any regulation by the Comptroller under Section 5136 would naturally refer to national banks. In view of the fact that State member banks are subject only to such limitations and conditions as are prescribed by the Comptroller of the Currency under the authority of Section 5136 of the Revised Statutes, it would seem preferable not to publish Sections III and IV, which are not prescribed under the provisions of Section 5136, in the same document with Sections I and II, which are prescribed under the provisions of Section 5136, since it is believed that State member banks might be confused by the fact that all four sections are published together and might think that they were subject to the provisions of Sections III and IV as well as to the provisions of Sections I and II.

"If, however, Sections III and IV are published in the same document with Sections I and II, it is believed to be desirable to add a
"sentence of the type suggested above in order to indicate clearly that State member banks are not subject to the provisions of Sections III and IV of the regulations.

"Page 3, Section I, third paragraph of section. It is suggested that this paragraph be amended to read as follows:

'In order to come within the definition of an "investment security" a security must meet the following minimum requirements:

(a) The issue of which the security is a part must be of a sufficiently large total to make marketability possible;

(b) (1) A sufficiently wide public distribution of such issue must have been provided for or made in a manner to effect, or to create a reasonable probability of effecting, the marketability of the issue, or, in the alternative,

(2) Other existing securities of the issuer must have such a public distribution as to effect, or to create a reasonable probability of effecting, the marketability of the issue under consideration, and such latter issue must be registered under the provisions of the "Securities Act of 1933", as amended, unless such issue is exempt from registration under Section 3 thereof;

(c) Where the security is issued under a trust agreement, the agreement must provide for a trustee independent of the obligor, and such trustee must be a bank or trust company.'

"The above suggestion is made for the purpose of eliminating any confusion as to whether the Comptroller proposes to classify given securities 'in specific cases' as marketable. It is believed that the statement that the Comptroller may 'give consideration to various facts and circumstances' adds nothing to the definition and that the definition would be clearer if it were stated in the form of minimum requirements applicable to all 'investment securities'. The substitution of the words 'to effect, or to create a reasonable probability of effecting,' for the words 'to protect or insure' has been suggested in order to remove any implication that the persons responsible for the flotation of the issue may be expected to protect the market for the security, after it has been floated, through purchases in the market.

"On page 4, Section I, fifth line from bottom of last paragraph of section. It is suggested that the word 'investment' be stricken out so that the exception clause will read 'Exception - Bonds or notes in the form of "securities" * * * '.

"Page 5, Section II. It is suggested that a new subsection numbered (1) be inserted before the present subsection (1) and that the present numbers be changed accordingly, such new subsection to read as follows:
"(1) Although the bank is permitted to purchase "investment securities" for its own account for purposes of invest-
ment under the provisions of R. S. 5136 and this regu-
lation, the bank is not permitted to participate as a
principal in the purchase or sale of securities in con-
nection with the marketing or distribution thereof.'

"The addition of this new subsection is suggested in order to
make it clear that the authority to purchase 'investment securities'
for a bank's own account does not include the authority to purchase
and sell securities as a principal in connection with the marketing
or distribution thereof. The specific prohibition of the statute
against underwriting seems to indicate an intention that the pur-
chases permitted were to be for investment and not for distribution
but, since purchases for a bank's own account for purposes of distri-
bution would not come within the technical meaning of 'underwriting',
it is believed that it should be made clear in the regulation that
purchases for such purposes are not permitted.

"Page 5, Section II(2). It is suggested that this subsection
would be clearer if worded as follows:

'(2) The purchase of "investment securities" which are distinctly
or predominantly speculative, or "investment securities"
of a lower designated standard than those which are dis-
tinctly or predominantly speculative, is prohibited.* The
purchase of securities which are in default either as to
principal or interest is also prohibited.'

"Pages 5 and 6, Section II(5)(a) and (b). It is suggested
that paragraph (a) be changed to read as follows:

'(a) Provide for the regular amortization of the premium paid,
so that the premium shall be entirely extinguished at or
before the maturity of the security and the security (in-
cluding premium) shall at no intervening date be carried
at an amount in excess of that at which the obligor may
legally redeem the security.'

"It is suggested that all of paragraph (b) be eliminated for
the following reasons: first, if followed it would result in un-
necessary bookkeeping, and would not be the most satisfactory way
of eliminating a premium from the bank's books, and, consequently,
should not be suggested by supervisory authorities; and, second, if
a bank should choose to eliminate its premium account by such
method it would be permitted to do so under paragraph (a). (Note:
It appears that the (1) in the next to the last line of paragraph
(b) should be (a))."

"Page 6, Section II(5)(b). It appears that the word 'not' be-
fore the word 'permissible' in the first line of the paragraph
should be stricken out. The word 'not' was omitted from the earlier
draft of the regulation.

"Page 10, first paragraph of section entitled 'Exceptions'.
If the suggestion made on page 2 of this letter that Sections III
'And IV be not published in the same document as Sections I and II is adopted, it is suggested that this paragraph be amended to read as follows:

'Transactions involving securities which are specifically exempted from the limitations and restrictions of paragraph Seventh of Revised Statutes 5136 by the terms of that section, are not subject to any of the provisions of these regulations.'

"However, if Sections III and IV are published in the same document with Sections I and II, and if you wish to make the provisions of paragraphs (5) and (6) of Section II and the provisions of Section III applicable to national banks, it is suggested that the paragraph be amended to read as follows:

'Transactions of State member banks involving securities which are specifically exempted from the limitations and restrictions of Paragraph Seventh of R. S. 5136 by the terms of that section are not subject to the provisions of these regulations. Transactions of national banks involving such securities are subject only to the provisions of paragraphs (5) and (6) of Section II, and to Section III of these regulations.'

"This change is suggested because of the opinion of the Board's Counsel that the limitations and restrictions prescribed by the Comptroller of the Currency under Section 5136 are not applicable to securities which are exempted by the terms of such section. Section 5136 provides that 'the limitations and restrictions herein contained as to dealing in, underwriting and purchasing for its own account, investment securities shall not apply to' certain obligations. It is the opinion of the Board's Counsel that the underlined words refer to limitations and restrictions prescribed by the Comptroller under the provisions of this section as well as to the limitation of 10 per cent of the bank's capital and surplus stated in such section."

Approved unanimously.

Thereupon the meeting adjourned.

[Signature]
Secretary.

[Signature]
Vice Chairman.