

A meeting of the Board of Governors of the Federal Reserve System was held in Washington on Tuesday, October 6, 1936, at 10:30 a. m.

PRESENT: Mr. Eccles, Chairman
Mr. Ransom, Vice Chairman
Mr. Broderick

Mr. Morrill, Secretary
Mr. Bethea, Assistant Secretary
Mr. Carpenter, Assistant Secretary
Mr. Clayton, Assistant to the Chairman
Mr. Thurston, Special Assistant to the Chairman
Mr. Wyatt, General Counsel
Mr. Paulger, Chief of the Division of Examinations
Mr. Goldenweiser, Director of the Division of Research and Statistics
Mr. Gardner, Research Assistant, Division of Research and Statistics

Mr. Ransom referred to the Board's letter of September 18, 1936, to Mr. Max Lowenthal, Counsel for the Senate Committee on Interstate Commerce, and to telephone conversations which he had had with Mr. Lowenthal and Mr. McConnaughey, Assistant Counsel for the Committee, with respect to a further arrangement under which the services of Mr. George H. Folsom, assistant examiner in the Board's Division of Examinations, would be made available to the Senate Committee on Interstate Commerce. In this connection Mr. Ransom read a memorandum prepared by him in which he had summarized Mr. Lowenthal's statements to him over the telephone as follows:

"Mr. Lowenthal states that he considers Mr. Folsom's services so essential to the successful completion of their

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"work that he would be willing to personally pay him in order to retain his services if the Board is considering the question of cost to the Board in this connection. He stated that he would like to have him reassigned to them for a period of a week or ten days, during which time he would undertake to present to Chairman Eccles in person the necessity for continuing Mr. Folsom's connection with the Committee's work; that they will need him until at least January or February and would prefer to have him assigned for an indefinite period; that, as a matter of fact, they would be very much better off today had they not had him at all and had used a man of inferior ability unless his services are to be continued with them. He states that he does not want to see the Committee go into its hearings half prepared, and that Mr. Folsom's services are absolutely essential if they are to be prepared for the hearing, and that he will want to continue him with the Committee until the hearing on the first group of reorganizations is completed.

"He states that in the beginning he explained to Chairman Eccles that they felt that these reorganizations have an immediate importance to banks as the holders of a large volume of railroad securities and that there was the further and broader question of the relationship of the railroad structure to general business conditions, his thought being that, if another depression is to be avoided, there should be the fullest understanding of the problem of railroad financing and the reorganization of railroad securities, and that the Committee's work was being approached so far as he was concerned in a constructive way, seeking to correct conditions and not criticize individuals or individual situations; that he felt confident that they would be able to persuade the Board to allow them to retain Mr. Folsom for a further period if he was able to present the question to the Board, or at least to the Chairman of the Board, with whom he had discussed the matter in the beginning."

Mr. Ransom said that he had advised Mr. Lowenthal that, as stated in the Board's letter of September 18, 1936, Mr. Folsom's services were needed in connection with certain important work upon which the Board's staff was engaged, that if he were not available for that work it would be delayed or the Board would be put to the

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necessity of incurring additional expense in connection therewith, that as it did not appear that the services of Mr. Folsom were indispensable to the Committee the Board did not feel justified in reassigning him to the Committee, but that notwithstanding these representations Mr. Lowenthal had persisted in his request that Mr. Folsom be made available.

During a discussion of the matter Mr. Folsom was called into the meeting and stated that he felt that the attorney on the Committee's staff who had succeeded to his work would be able to carry it on with the assistance of the three attorneys in New York who were engaged in compiling the assembled data and who had been members of the Committee's investigating staff as long as Mr. Folsom; that all of the information which he (Mr. Folsom) had assembled was available in the files of the Committee; and that a further continuance of his services was not necessary for a satisfactory completion of the Committee's work. Mr. Folsom also stated that his personal preference would be to devote his time to the special assignment given him as a member of the staff of the Board's Division of Examinations.

Mr. Eccles suggested that, in view of all the circumstances and Mr. Lowenthal's insistence that Mr. Folsom's services were essential to the successful completion of the Committee's work, the Board might agree to a compromise arrangement under which the services of Mr. Folsom would be made available to the Committee on a part time

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basis for the purpose of directing the final completion of the work in which he had been engaged for the Committee.

At the conclusion of the discussion Mr. Ransom moved that he be authorized to advise Mr. Lowenthal over the telephone that, while the services of Mr. Folsom were very necessary in connection with the Board's work, the Board was willing to agree to an arrangement under which his services would be made available to the Senate Committee on Interstate Commerce for the purpose of directing the preparation of the material which he has assembled for the Committee, with the understanding that he was to determine the amount of time necessary for this purpose with a view to giving as much time as possible to his work for the Board, that he would be relieved of the Committee work as rapidly as possible in order that he might devote all of his time to an important assignment given him by the Board, that such an arrangement might continue, if necessary, until not later than February 1, 1937, and that in no event would Mr. Folsom be called upon as a witness at any of the hearings held by the Committee or to appear at such hearings in any other capacity.

Carried unanimously, with the understanding that, after Mr. Ransom had advised Mr. Lowenthal by telephone of the Board's position, it would be confirmed in a letter to be sent by the Secretary to Mr. Lowenthal.

At this point Messrs. Paulger and Folsom left the meeting.

Mr. Ransom stated that, in accordance with the action taken at the meeting of the Board on September 22, 1936, he had taken up with President Harrison of the Federal Reserve Bank of New York the question of a suitable date for a conference between the Board and

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Messrs. Harrison, Sproul and Knoke of the Federal Reserve Bank of New York, for the purpose of discussing the procedure to be followed with respect to relationships and transactions entered into by the Federal Reserve Bank of New York with foreign banks or bankers under the provisions of section 14(g) of the Federal Reserve Act and that it had been tentatively agreed that the conference could be held on some date between October 14 and 17, 1936. Mr. Ransom also referred to the situation which had arisen in connection with the monetary understanding between the United States, Great Britain and France which had been made public on September 25, 1936, and to the discussion of this matter with the Secretary of the Treasury at the meeting on September 29, 1936, and suggested that before the date of the conference with the representatives of the Federal Reserve Bank of New York is set, the Chairman should confer with the Secretary of the Treasury for the purpose of arriving at an understanding under which the Board of Governors may be kept currently advised of fiscal agency activities carried on by the Federal reserve banks for the Treasury Department in order that the Board may be in a position at all times to discharge the responsibilities placed upon it by the Federal Reserve Act.

Mr. Ransom stated that, following the meeting with the Secretary of the Treasury on September 29, members of the Board and the senior members of the staff had discussed the question of cooperation

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with the Treasury Department in the exchange of information which would enable the Board and the Department to better discharge the respective responsibilities resting upon them and that he had dictated the following memorandum as an expression of his personal approach to the question:

"If effective cooperation in the public interest is to be achieved, it is necessary that the Board should at all times be in possession of such information as will enable it to discharge its duties in relation to those broad questions of Treasury policy in (1) those matters wherein the Board is charged with formulating policies of its own under its statutory responsibilities and (2) those matters which relate to its supervisory authority over the Federal reserve banks when these banks are dealing with foreign banks or bankers. When the Board is given such information it can correlate the operations of the Federal reserve banks and can be sure that these banks are complying with the mandatory provisions of the statutes which govern them in such dealings. Possession of such information further serves to make available to the Treasury helpful cooperation on the part of the Board in relation to those aspects of these matters wherein the Board is in possession of information not immediately available to the Treasury."

There followed a general discussion of matters to be taken into consideration in working out an arrangement between the Treasury Department, the Federal reserve banks and the Board under which the Board will be furnished with the necessary information to enable it to discharge its responsibilities, at the conclusion of which the Chairman stated that he had an appointment with the Secretary of the Treasury this afternoon and would take the matter up with him in the light of the discussions at this meeting with a view to

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working out a satisfactory procedure following which consideration could be given to a date for the proposed conference with the representatives of the Federal Reserve Bank of New York.

At this point Mr. Dreibelbis, Assistant General Counsel, joined the meeting.

There was presented a letter dated October 2, 1936, from Mr. Sproul, First Vice President of the Federal Reserve Bank of New York, reading as follows. Copies of the letter and the communications referred to therein had previously been furnished to the members of the Board:

"Under cover of our letter of October 1, 1936, we sent you a copy of the reply (dated September 14, 1936) of the Hungarian National Bank to our letter of August 25, 1936, concerning the central bank credits to the Hungarian National Bank, as transmitted to us by the Bank for International Settlements with its letter of September 17, 1936, copy of which also was sent to you. You will note that the Hungarian National Bank, in its letter of September 14, 1936, states that it is not able to accede to the proposal of this bank as regards resuming transfer of capital repayments; that the Bank for International Settlements in its letter of September 17, 1936, states that we shall be advised in due course of the comments of the other participants in the consolidated credits upon our proposals for such transfer of capital repayments; and that the Bank for International Settlements further states that it would like to have our views as early as possible in order that they may be placed before its board at its next meeting, October 12, 1936.

"Our directors considered these communications at their meeting yesterday. They were of the opinion that before taking final action with respect to a renewal of the credits for as long a period of nine months, upon the terms requested by the Hungarian National Bank, we

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"are entitled to have before us the comments of the other participants in the credits concerning our proposals for some transfer of payment upon the principal at this time. In order that time might be gained in which these comments could be received and our position further considered, the directors propose suggesting to the Bank for International Settlements that the consolidated credit agreement be renewed for a period of one month from October 18, 1936. The directors also propose suggesting that the renewal of one month be on the modified terms agreed to by the Hungarian National Bank with respect to the requested renewal for nine months, including payment of interest at the rate of 1% per annum on the first as well as on the second syndicate credit, and payment in blocked pengoes, value October 18, 1936, of an amount equal to 2% on the principal of the second syndicate credit.

"Our board of directors voted, subject to the approval of the Board of Governors of the Federal Reserve System, to authorize the officers to convey these proposals to the Bank for International Settlements, and we have today sent a telegram to the other Federal reserve banks which are participants in the credits, copy of which is enclosed, asking their assent. We shall advise the Board as soon as the replies of the other Federal reserve banks are received and we shall then appreciate receiving the Board's approval of the action of our directors."

Upon motion it was agreed unanimously that upon receipt of advice from the Federal Reserve Bank of New York that the other Federal reserve banks had agreed to the proposed renewal of the central bank credits to the National Bank of Hungary for a period of one month from October 18, 1936, the Secretary should advise the New York bank that the Board approves the action of the directors of the bank in authorizing such a renewal on the terms proposed.

Attention was also called to a letter dated September 29, 1936, from President Harrison of the Federal Reserve Bank of New

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York, reading as follows. Upon receipt of the letter on September 30, copies had been furnished to the members of the Board:

"On April 27 last, foreign exchange control was decreed by the Polish Government, following a flight of capital from the country believed to have been due to the cumulative effects of political changes consequent upon the death of the late Marshal Pilsudski. On May 7, last the Polish Government instituted a licensing system for commodity imports as a means of re-enforcing the exchange control. Finally, on June 25, Polish Commissioners then present in the United States communicated to the Joint Fiscal Agents of the Republic of Poland Seven per cent Stabilization Loan of 1927, the decision of the Polish Government, 'for the time being,' to suspend transfer of service due on that loan and to make such service in zlotys deposited to the credit of the Fiscal Agents in blocked account at the Bank Polski, Warsaw. No communique announcing a general suspension of service on the foreign debt of Poland has come to our attention, nor is such a communique believed to be contemplated, but it would appear that suspension of transfer of service on all Polish foreign debt could be effected through the operations of the exchange control laid down on April 27, within the discretion of the control authorities. So far as we are aware, the only official explanation of the decision to suspend transfer of service was given in a radio address made in July by an official of the Finance Ministry who said, according to a report from the United States commercial attache in Warsaw, dated July 13, that 'continuation of the service on debts contracted on particularly adverse terms would have led to a heavy depletion of gold reserves.'

"Mr. Charles S. Dewey, formerly Financial Adviser to the Polish Government, was good enough to supplement this information in the course of a call which he paid last week on his return from a Visit to Poland. In Mr. Dewey's view, the decision to suspend transfer of foreign loan service was taken with reluctance and has been received with regret by a considerable part of the banking and business community in Poland as well as by some of the more conservative officials

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"in Poland. The decision appears to be related to the fear of depleted reserves reported from Warsaw, and also, to some extent, to the feeling that Poland should not be paying variously from 6 to 8 per cent on her foreign public and mortgage bank loans when the Government is able to borrow at home, as it did this year, on a 4 per cent coupon. It is Mr. Dewey's impression that apart from the flight of capital the Polish balance of payments position is not such as to justify reduction of foreign debt transfer, and certainly not total suspension. In so far as trade alone is concerned, his impression appears to be confirmed by the results of recent years, which continue to show a 'favorable' surplus of exports over imports, with no significant change in import values between 1932 and 1935, and a decline of only 15 per cent in export values between these two years. The foreign trade figures for the first seven months of 1936, although expressed in undepreciated gold zlotys, are better than those for the corresponding months of 1935: exports are 10 per cent and imports 11 per cent greater; the 'favorable' export surplus, however, was somewhat smaller in January-July 1936 than in January-July 1935, being equivalent to \$5 million this year as against \$5.6 million last year.

"The United States has a stake in Poland which is affected by all three of the measures reported above - the exchange control, the control of import trade, and the decision to suspend transfer of debt service. The exchange control is likely to cause the building up of blocked zloty balances resulting from the proceeds of dividends due to American participants in the ownership of Polish industrial companies. According to estimates as of the beginning of 1936, American participation in the stock ownership of Polish companies was valued at approximately \$70 million and was equivalent to 22 per cent of total foreign ownership and to 10 per cent of total stock outstanding in Polish incorporated companies. In addition, the exchange control could possibly tie up American funds by the creation and accumulation of arrears of commercial payments owing to American exporters.

"The import control would probably be applied with particular severity to American merchandise for the reason that Polish trade with the United States has been persistently adverse to Poland, the 'unfavorable' balance having risen steadily from \$2.6 million in 1931 to \$15 million in 1935. Since, meanwhile, as much as 60 per cent of Polish commerce is understood to be subject to clearing and compensation agreements imposed

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"by other countries, the normal means of settling dollar balances through triangular payments have been very severely restricted. At the same time, partly due to the interjection of such agreements into Poland's trade channels, that country has built up a trade position which gives her 'favorable' balances with a number of other trading nations. Some of these are Poland's creditors on financial account, for example Great Britain, and it would be reasonable to expect that such countries might demand, and Poland might have to accord them, discriminatory treatment in the matter of financial debt in their favor and against the United States. On the score of trade, it is to be remarked that while our imports from Poland more than trebled between 1931 and 1935 in terms of zlotys, and increased from \$2.0 million in 1931 to \$9.3 million in 1935 in terms of our own monetary unit, Poland has meanwhile taken a larger place as a market for American goods. In 1931 she took \$4.6 million of our goods, which represented 0.19 per cent of our total exports in that year; in 1935 she took \$24.5 million of our goods, this representing 1.07 per cent of our total exports in that year. Whereas in 1931 Poland bought from us \$867,000 worth of raw cotton, equivalent to 0.27 per cent of our total cotton exports in that year, in 1935 she bought \$18 million worth of American cotton, equivalent to 4.71 per cent of our total cotton exports last year.

"Excluding debt arising out of the war, Polish Government foreign bonds outstanding as of April 1 last were estimated at approximately \$166 million. In addition, approximately \$20 million of bonds are outstanding in the name of three public bodies of Poland, - the Province of Silesia, the City of Warsaw, and the Land Mortgage Bank of Warsaw. Of the Polish Government external bonds, dollar bonds account for 84 per cent; indeed, with the exception of the Sterling tranche of the Stabilization Loan of 1927 and a seven per cent loan of 1924 denominated in lire, we know of no public bond issue offered outside Poland by a Polish public body which is not denominated in dollars. The Stabilization Loan of 1927, dollar service of which will go into default with the coupon of April 15, 1937, if present intentions are adhered to, is an issue to which special importance attaches by reason of the fact that it formed part of a comprehensive plan for the economic rehabilitation of Poland and the reform of the Polish monetary and credit system. While they had no responsibility for the loan, the Federal reserve banks, in associa-

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tion with fifteen foreign central banks, were concerned in the drafting of that plan and participated together, concurrently with the issue of the loan, in the extension of a stabilization credit to the Bank of Poland. Under the stabilization plan an American Adviser to the Polish Government was appointed and was elected to the Board of the Bank of Poland. It is true that in a statement made public by the Fiscal Agents on June 30, 1936 it was reported that more than 50 per cent of the October 15 coupons on the Stabilization Loan will probably be presented for payment in Warsaw. Undoubtedly, as in the case of a number of other foreign dollar issues, a large, though unascertainable, share of the bonds has been repatriated. Nevertheless, it would seem to us that it would be most unfortunate if the conditions of service of a loan offered under such auspices should not be met in full by the borrower, or if that is not possible, that some equitable and uniform adjustment of service on the loan should not be made.

"We have seen that default has taken place elsewhere on loans of this character, and we have seen, further, that discrimination against the United States has taken place in connection with the service of loans of this character. Since such discrimination has resulted in particular from foreign trade relations of the sort obtaining between Poland and the United States, i.e. a balance of trade heavily 'favorable' to the United States, and since Poland is blocked as to three-fifths of her trade from finding triangular funds with which to make debt service here, it has occurred to us that the State Department may wish to consider taking some action with regard to the threatened suspension of transfer of service on Polish dollar securities which might avert discriminatory treatment of United States investors. One form of action which might suggest itself under present conditions is the consideration of the advisability of negotiations for a commercial treaty with the Polish Government along the general lines of the treaties hitherto negotiated by the Secretary of State with a number of other foreign nations. It might be that pending the conclusion of such negotiations no discrimination against American creditors of Poland would take place, or even that the suspension of transfer on loans issued here might be deferred pending such negotiations. The hope of such deferment would not seem unreasonable if, as is reported, the recent difficulties in the balance of payments position have been due to a flight of capital, and if exchange

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"control becomes more effective as experience is gained in its administration.

"In announcing to the Fiscal Agents the Polish Government's decision to suspend transfer of service on the Stabilization Loan of 1927, the Commissioners of that Government expressed its desire 'that the conversations about the situation herewith created be resumed at a convenient moment.' In response thereto the Fiscal Agents made public a statement in which they declared inter alia 'that they are desirous of promptly entering into discussions with the (Polish) Government about the situation. . . .' It is understood that there is a possibility of a meeting of Polish creditors being called to convene in London some time in October, and it would seem to be desirable that the interests of all American investors in Polish Government securities be unified for representation at that time. In any event, should the Board of Governors decide to transmit these observations to the Secretary of State, I would appreciate it if he were informed of our readiness to act in this matter in any way which may be advisable."

After a discussion of what action might be taken by the Board in connection with this matter Mr. Gardner was instructed to discuss the situation referred to in the letter with the appropriate officials of the State Department and report to the Board any comments or suggestions that the Department may have to make with regard thereto.

In taking this action it was understood that Mr. Gardner would be free to permit the appropriate officials of the State Department to read President Harrison's letter.

Mr. Ransom referred to the action taken by the Board on December 28, 1935, in deferring the effective date of the definition of interest contained in subsection 1(f) of Regulation Q, Payment of Interest on Deposits, and stated that he was prepared to recommend at the next meeting of the Board at which all of the members are present that the defi-

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dition be made effective. He also stated that he was prepared to recommend at such a meeting that the Board liberalize the definition of savings deposits contained in subsection 1(e) of Regulation Q, and also that the Board approve a procedure, which he outlined briefly, for the preparation for consideration by the Board of a final draft of Regulation A, Advances to and Discounts for Member Banks by Federal Reserve Banks.

Mr. Wyatt stated that the attorney for Mr. John D. Montgomery, who had filed a bill in equity in the United States District Court for the District of Columbia to enjoin the members of the Board, the Secretary of the Treasury and the Comptroller of the Currency from the "further exercise of the power to coin money and regulate the value thereof other than in accordance with the provisions of the Constitution of the United States of America, etc.", had called on him and requested that he accept service of process in the suit on behalf of the Board members. Mr. Wyatt inquired whether the Board desired him to accept service and recommended that he be not so authorized.

Mr. Wyatt was instructed to advise the attorney for Mr. Montgomery that the Board was unwilling to authorize Mr. Wyatt to accept service.

Mr. Wyatt then stated that in cases of this kind the procedure usually followed was for the agency involved, upon being served, to refer the case to the Department of Justice for handling and he inquired whether the Board wished to have that procedure followed in this case.

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Mr. Wyatt was requested, in the event service of process is made upon the members of the Board, to prepare a letter in accordance with his suggestion to the Department of Justice for the signature of the Secretary.

At this point Messrs. Thurston, Wyatt, Goldenweiser, Dreibelbis and Gardner left the meeting and consideration was then given to each of the matters hereinafter referred to and the action stated with respect thereto was taken by the Board:

Telegrams dated October 5, 1936, to Mr. Ziemer, Vice President of the Federal Reserve Bank of Minneapolis, and Mr. McKinney, President of the Federal Reserve Bank of Dallas, stating that the Board approves the establishment without change by the respective banks today of the rates of discount and purchase in their existing schedules.

Approved unanimously.

Cablegram dated October 5, 1936, to Miss Sarah L. Brissenden, a stenographer in the Secretary's office, addressed to her in care of the American Embassy at London, England, reading as follows:

"Leave extended 15 days without pay. Board's policy of employing best person available to fill vacancies would prevent consideration of Kent transfer without interview and complete information as to training and experience. Advise promptly if and when you will return."

Approved unanimously.

Letter to Mr. Hill, Vice President of the Federal Reserve Bank of Philadelphia, reading as follows:

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"Careful consideration has been given to your letter and the inclosed opinion of counsel for your bank regarding the applicability of the Clayton Act to the service of Mr. Robert D. Kemp as a director of Union National Bank, Wilmington, Delaware, and as a member of the advisory committee of the Wilmington Trust Company.

"Your counsel states that the members of the advisory committee of the Wilmington Trust Company are elected by the board of directors; that they must be stockholders but not directors of the trust company; that their duties are to attend all meetings of the board of directors, to advise the board with respect to the business of the trust company, and to meet at such other times as may be requested by the president or the executive vice president for the purpose of advising the officers of the trust company with respect to its business; that the members of the committee have no vote at the meetings of the board of directors; that they have no authority to pass on loans or to act for the trust company or any officer thereof in the performance of any duty usually performed by an officer, or to bind the trust company in any way, their functions being merely advisory; and that, as compensation for their services, each member of the committee receives \$20 for each meeting attended.

"In view of the principles discussed in the Board's ruling published in the Federal Reserve Bulletin for 1917 at page 118, it appears that the members of the advisory committee are not 'officers' or 'directors' of the trust company. Moreover, in view of the fact that their services are not subject to the direction or control of the trust company but involve the use of independent judgment on their part, their functions being merely advisory, and in view of the fact that they are not employed on a full time basis or at a regular salary, it appears that they should not be regarded as 'employees' of the trust company.

"In the circumstances, it appears that the Clayton Act is not applicable to the relationships described in the first paragraph of this letter."

Approved unanimously.

Mr. Ransom reported that, in accordance with the action taken earlier during this meeting, he had called Mr. Lowenthal, Counsel for

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the Senate Committee on Interstate Commerce, on the telephone and had advised him of the position of the Board with regard to making the services of Mr. Folsom available to the Committee and that Mr. Lowenthal had agreed to the arrangement proposed by the Board. Mr. Lowenthal had given assurance, Mr. Ransom stated, that he will make arrangements to relieve Mr. Folsom as soon as possible of his work for the Committee, that he will not call upon Mr. Folsom to give more time to the work than is absolutely necessary, and that Mr. Folsom will not be expected to participate in any way in any hearings conducted by the Committee.

Thereupon the meeting adjourned.

Peter Moriel
Secretary.

Approved:

W. C. Steeles
Chairman.