A meeting of the Board of Governors of the Federal Reserve System was held in Washington on Monday, January 18, 1937, at 2:30 p. m.

PRESENT: Mr. Eccles, Chairman,
Mr. Ransom, Vice Chairman
Mr. Broderick
Mr. Szymczak
Mr. McKee
Mr. Davis

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. Parry, Chief of the Division of Security Loans
Mr. Smead, Chief of the Division of Bank Operations
Mr. Paulger, Chief of the Division of Examinations
Mr. Bradley, Assistant Chief of the Division of Security Loans
Mr. Dreibelbis, Assistant General Counsel
Mr. Solomon, Assistant Counsel
Mr. English, Special Assistant, Division of Security Loans
Mr. Dembitz, Research Assistant, Division of Security Loans

ALSO PRESENT: Mr. Charles R. Gay, President of the New York Stock Exchange
Mr. Dean K. Worcester, Executive Vice President of the New York Stock Exchange
Mr. Gayer G. Dominick, Member of the Governing Committee of the New York Stock Exchange
Mr. William H. Jackson, of the firm of Carter, Ledyard & Milburn, Counsel for the New York Stock Exchange

Mr. L. R. Rounds, Vice President of the Federal Reserve Bank of New York
Mr. Norman Davis, Representative of the Federal Reserve Bank of New York

Mr. David Saperstein, Director of the Trading and Exchange Division of the Securities and Exchange Commission
Mr. A. N. Davis, Assistant Director of the Trading and Exchange Division of the Securities and Exchange Commission

Chairman Eccles stated that this meeting had been arranged to afford the representatives of the New York Stock Exchange an opportunity to present fully to the Board the suggestion which the Exchange had made that it defer amending Regulation T, "Extension and Maintenance of Credit by Brokers, Dealers, and Members of National Securities Exchanges" so as to provide that customers shall furnish the margins required by the regulation not later than the close of business on the day upon which the transaction giving rise to the margin requirement is effected, and that the Board afford the Exchange an opportunity, through amendments to its rules, to attempt to eliminate the practice known as "in-and-out trading" under which the furnishing of the required margins is avoided.

Mr. Gay stated that it should be made clear that the New York Stock Exchange has the same attitude toward "in-and-out trading" as the Board evidenced by the proposed amendment to Regulation T; that the Exchange had no desire whatever to defend the practice; and that the Exchange would like to take such action as may be necessary to prevent the abuse. However, Mr. Gay said, it was felt that the amendment to Regulation T, as proposed by the Board, in effect would require customers placing open orders with brokers to furnish the required margin in advance; that this requirement would result in a substantial reduction of such orders, referred to as "G. T. C. orders", which he stated serve as a cushion to stabilize the market; and that, therefore, the amendment to the Board's regulation would result in accentuating the spread between bid and asked prices for securities on the Exchange and in an unstable market.

Mr. Dominick expressed agreement with Mr. Gay's statement and said that the proposal of the Stock Exchange had been made because it was felt that, while under the proposed rule of the Exchange "in-and-out trading" could be practically stopped within a reasonable time, the rule would not result in the discontinuance of open orders with their stabilizing influence on the market.

At the request of Mr. Gay, Mr. Worcester outlined the manner in which the rule proposed by the New York Stock Exchange would operate and, upon inquiry by Mr. McKee as to what penalties could be imposed by the Exchange for violation of the rule, Mr. Worcester said that the penalty might be anything from censure to expulsion from the Exchange, and that there was in progress an amendment to the constitution of the Exchange which would authorize the Business Conduct Committee to impose fines covering matters coming within its field, of which violation of the proposed rule would be one. Mr. Worcester also expressed the view in this connection that discipline by the Exchange would have advantages over criminal penalties.

Mr. Ransom inquired what, under the proposed rule of the Exchange, would constitute making "a practice of effecting transactions requiring such initial or additional margin and then furnishing such margin by liquidation of the same or other commitments", and Mr. Gay replied that the determination of what would constitute a practice would have to be arrived at on the basis of the experience of the Exchange in dealing with specific cases.

Mr. Jackson stated that it had been the experience of the Exchange that rules setting up broad standards had been found to be the most successful; that the Exchange could not determine in advance how it would handle specific cases; but that if, on the basis of the records furnished the Board by the Exchange, including records of decided cases, it was felt that the rule was not being given a sufficiently strict interpretation, the Board could so advise the Exchange. Upon inquiry from Mr. Parry, Mr. Jackson and Mr. Worcester agreed that, if the rule should be found not to be sufficiently effective in the form adopted the Exchange would stand ready to amend it.

In reply to an inquiry from Mr. McKee, Mr. Worcester stated that under the amendment proposed by the Board the broker would be required, in case he did not already have the necessary margin, to obtain the necessary margin on the day the transaction was effected or be subject to a criminal penalty and that, because of the uncertainties of the situation, the broker would in such cases be unwilling to take this risk; whereas, under the rule proposed by the Stock Exchange, the customer would be given a reasonable time in which to learn that margin is in fact needed and the amount thereof and in which actually to furnish the necessary margin. It would be the purpose of the Exchange, moreover, he said, to furnish the Board with full information as to cases where the margin requirements were not actually met by the deposit of cash or collateral.

Mr. McKee stated that, as the proposal of the Exchange would place on it the responsibility of policing the transactions of its members in

this respect, the representatives of the Exchange should state for the Board's information any measures which they propose to adopt to discharge that responsibility.

Mr. Gay referred to the records and reports proposed to be required by the Stock Exchange rule and said that if these indicated that the rule was not being observed in any case the accounts of the member could be checked. Mr. Gay also stated, in response to an inquiry from Mr. Broderick, that the accountants of the Exchange are accustomed to making inspections of the books of out-of-town members of the Exchange as well as of New York members.

Mr. Parry inquired what, if any, action had been taken by other stock exchanges in connection with this matter and Mr. Worcester volunteered the opinion that they were waiting to see what the decision would be with respect to the proposal of the New York Stock Exchange and that, if it were followed, they undoubtedly would adopt similar rules with respect to transactions on their respective exchanges. In this connection, Mr. Worcester stated that in most cases members of the New York Stock Exchange are also members of other stock exchanges, that the rules of the New York Stock Exchange applied to all transactions of the kind under consideration effected by such members regardless of the security or the exchange through which it is purchased or sold, and that the great majority of margin transactions in the United States are handled through these firms.

Chairman Eccles inquired what would be the objection to requiring

that all transactions on securities exchanges be handled on a strictly cash basis, and Mr. Gay expressed the opinion that such a requirement would be decidedly contrary to the public interest. There was some discussion of this point.

Chairman Eccles stated that it should be definitely understood that, if the Board should decide to defer adoption of the proposed amendment to Regulation T in order to afford the New York Stock Exchange a reasonable opportunity to make its proposal effective, such action would not commit the Board in any way; that the Board would still be free to put the amendment to Regulation T into effect at any time that in its judgment such action should be taken; and that if it were found desirable, for reasons other than those now under consideration, to adopt the amendment before the Stock Exchange had had a reasonable opportunity to show what could be accomplished under the amended rules of the Exchange, the Board would be at liberty to do so. The representatives of the Stock Exchange stated that they fully understood that such would be the case.

In connection with a discussion of the records which would be required to be kept by the members of the Exchange and the reports to be furnished by them, Messrs. Gay and Worcester stated that the placing of adequate information before the Board with respect to the administration and possible violation of the stock exchange rule was an established part of the proposal of the New York Stock Exchange.

In reply to a question from Mr. Parry, Mr. Worcester stated that no amendment of Regulation T would be required at this time in order to

enable the Exchange to discharge its commitment.

Thereupon the representatives of the Stock Exchange withdrew from the meeting.

There followed a general discussion of the suggestion of the New York Stock Exchange, during which Mr. McKee asked Mr. Rounds for a statement of his views as to whether the proposed rule would be effective. Mr. Rounds stated that he felt that the proposal represented a genuine effort on the part of the Exchange to meet the situation and that if it were made clear that the Board would be ready to adopt the proposed amendment to Regulation T at any time that the rule of the Exchange was not effective or was not properly enforced, it might have the desired result. Even if it were felt by the Board, Mr. Rounds said, that there was a real question whether the proposal would produce satisfactory results, the Board would be justified in permitting the Exchange to put it into effect, thereby affording the Exchange an opportunity to cooperate in meeting the problem. He added that the proposed amendment to Regulation T would result in considerable misunderstanding between brokers and their customers as to why the changed requirements were imposed and that the responsibility for such misunderstanding was one which need not be assumed by the Board at this time. There were reasons to believe, Mr. Rounds stated, that the Exchange would do everything it could to make its proposal effective, and, if, after a trial, it was found that it did not produce satisfactory results, the Board would still be in a position to adopt the amendment to Regulation T.

Upon inquiry, Mr. Saperstein stated that he had not had an opportunity

to ascertain what the attitude of the Securities and Exchange Commission would be toward the proposal of the New York Stock Exchange but that he would present to the Commission the matters discussed at this meeting and advise the Board as promptly as possible whether the Commission would have any serious objection to agreement by the Board with the proposal of the New York Stock Exchange with the understanding that such agreement would not be regarded as committing the Board in any way. Mr. Saperstein suggested that if the Board decided to give favorable consideration to the Stock Exchange proposal it might be made more effective if the provision regarding making a practice were expressed in a way which he outlined.

Upon inquiry from Mr. McKee as to whether Regulation T should be rewritten or amended, Mr. Parry stated that the fundamental approach of the regulation need not be changed but that certain amendments might be found to be desirable. It was understood that such amendments, amounting in effect to a general revision, would be presented by Mr. Parry to the Board for consideration in the near future with a recommendation as to the action to be taken. In this connection attention was directed to the fact that each member of the Board had been furnished with a copy of a revision drafted by the Federal Reserve Bank of New York.

Messrs. Parry, Smead, Paulger, Bradley, Solomon, English, Dembitz, Rounds, Norman Davis, Saperstein and A. N. Davis left the meeting at this point.

Mr. Ransom referred to the conference this morning of members of the Board and its staff with bankers representing State banking associations

and clearing house associations in Florida, Alabama, Mississippi, Kentucky, Louisiana, Tennessee and the Cincinnati Clearing House Association, at which there was presented by the bankers a request that the Board defer the effective date of subsection 1(f) of Regulation Q, Payment of Interest on Deposits, until such time as uniformity between the provisions of the Board's regulation and the regulation of the Federal Deposit Insurance Corporation with respect to the absorption of exchange and collection charges as an indirect payment of interest on demand deposits can be achieved. Mr. Ransom stated that, pursuant to the action taken by the Board on December 11, 1936, subsection 1(f) of Regulation Q would become effective on February 1, 1937, and that, therefore, the Board should reach a decision promptly on the question whether it would take any further action in the matter.

The request of the bankers was discussed and reference was made to the possibility that if the subsection is permitted to go into effect it might result in a withdrawal of a substantial number of banks from membership in the Federal Reserve System and of a larger number of banks from the par list. In this connection, Chairman Eccles expressed the opinion that such a possibility should not influence the decision of the Board for the reason that the Board according to the advice of its counsel has no choice under existing law except to regard the absorption of exchange and collection charges in connection with the maintenance of deposit balances as an indirect payment of interest and that, if the Board's regulation should result in the withdrawal of banks from membership and from the par list, it would place the problem squarely before Congress for consideration of

what action it will take to correct the situation. The Board was advised that it was the view of its counsel that the existing law obligated the Federal Deposit Insurance Corporation to place in its regulation a provision substantially similar on this point to the provision contained in the Board's Regulation Q.

At the conclusion of the discussion, it was the consensus of the members present that, in the absence of a definite indication that the Federal Deposit Insurance Corporation would be willing to adopt in its regulation a provision similar to that contained in subsection 1(f) of Regulation Q, or, possibly, substantial evidence of legislative intention to amend the law, the Board should not defer further the effective date of the subsection.

At this point Messrs. Thurston and Dreibelbis 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:

The minutes of the meeting of the Board of Governors of the Federal Reserve System held on January 15, 1937, were approved unanimously.

Telegram to Mr. Powell, Secretary of the Federal Reserve Bank of Minneapolis, stating that the Board approves the establishment without change by the bank today of the rates of discount and purchase in its existing schedule.

Approved unanimously.

Letter to Mr. Gidney, Vice President of the Federal Reserve Bank of New York, reading as follows:

"Reference is made to Mr. Dillistin's letter of December 31, 1936, transmitting with favorable recommendation a request of the 'West Side Trust Company', Newark, New Jersey, for a

"further extension of time within which to complete compliance with the following condition of membership:

'21. Such bank shall, as soon as practicable and in any event within six months from the date of admission to membership, dispose of any loans which may be secured in whole or in part by its own stock or obtain the substitution of other adequate security for each such loan.'

"The bank was admitted to membership on January 6, 1934, and the Board has granted five previous extensions of the time within which the bank might comply with the provisions of the condition, the last of which expired on December 31, 1936. Since admission to membership, however, the bank has made substantial progress in disposing of its own stock held as collateral.

"According to the information submitted, only 364 shares (out of a total of 43,000 outstanding) are still held by the bank as security to loans, and these shares are held as part collateral to loans of four of the individuals who assumed their liability on the indebtedness to the bank of Nathan Builder, Trustee in connection with which the stock was acquired as collateral. In view of all of the circumstances, therefore, and Mr. Dillistin's recommendation, the Board extends to December 31, 1937, the time within which the West Side Trust Company may comply with the provisions of condition of membership numbered 21.

"The bank reports that on August 14, 1936, it acquired 1,000 of the shares of its stock formerly held as part collateral to a loan, and in this connection it has been noted that Mr. Dillistin has called the bank's attention to the fact that under the applicable provisions of law the bank will be required to dispose of such shares within 6 months from the date of acquisition. It is assumed, of course, that you will follow the matter to a conclusion and will advise the Board when disposition of the stock has been accomplished."

Approved unanimously.

Memorandum dated January 12, 1937, from Mr. Morrill submitting for the approval of the Board, with the approval of Dr. Miller, a proposed letter to Mr. Paul P. Cret, Architect for the Board's new building, agreeing to the employment of Mr. Cret's services in connection with the furniture and furnishings of certain areas in the new building which were listed in the proposed letter. The memorandum stated that while the list did not

include the cafeteria, it might become desirable to add the cafeteria to the list and, if so, a recommendation would be submitted to the Board that the letter be supplemented so as to include that area. The proposed letter to Mr. Cret read as follows:

"This refers to your letter of December 19, 1936, containing your proposal with respect to services to be rendered by you in connection with the furniture and furnishings of certain spaces in the building now being constructed for the Board of Governors of the Federal Reserve System.

"It is understood that the spaces referred to are the following:

2nd Floor

a. Oval entrance to Board Members' section
b. Reception Room
c. Board " "
d. Conference "
e. Board Library
f. Governor's (now Chairman's) suite, including Assistant to the Chairman
g. 8 suites designated on the contract drawings for seven Board members and the 1 additional suite (designated D-91 & D-92)
h. Gallery of monumental stairs (any benches or necessary furniture, etc.)

1st Floor

i. The Constitution Avenue entrance hall (a chair, table or some other provision should be made for a guard)

4th Floor

j. The entire private dining room suite including the 3 dining rooms and lounge and elevator lobby.

"It is understood that your fee for the performance of the services described in your letter will be 10 per cent of the total cost to the Board of all items of furniture, furnishings, rugs, draperies, lamps, venetian blinds, desk equipment, and other similar articles which are furnished, with the approval of the Board's Secretary, for the spaces above specified, pursuant to plans, schedules and specifications prepared by you and approved by the Board's Secretary, which are not included in or provided for in the contract between the Board and George A. Fuller Company for the construction of the building. In addition, the Board will reimburse you for traveling and subsistence expenses to the same extent and under the same conditions as provided in Article 5(e) of your agreement with the Board dated June 5, 1935, namely, the amount of all actual and necessary traveling and subsistence expenses (not exceeding five dollars ($5.00) per person per day in addition to the actual

"cost of transportation) incurred by you and your professional and technical employees when traveling on duty in performing the services in question, provided that all travel for which expenses are reimbursable must be approved by the Board's Secretary. Payment of the above fee and reimbursements will be made upon completion of the services in question.

"As you know, the law requires that contracts entered into by Government establishments shall contain a provision that no member of or delegate to Congress or resident commissioner shall be admitted to any share or part of the contract or to any benefit that may arise therefrom, and it is understood, of course, that the requirements of such provisions will be observed in the present connection.

"With the above understandings, the Board of Governors of the Federal Reserve System accepts the proposal contained in your letter of December 19, 1936, referred to above. Please confirm by letter addressed to the Board that your understanding agrees with the foregoing."

Approved unanimously.

Thereupon the meeting adjourned.

Chester Morrill
Secretary.

Approved:

M S Eccles
Chairman.