

A meeting of the Board of Governors of the Federal Reserve System was held in Washington on Friday, May 7, 1937, at 11:30 a. m.

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

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

Consideration was 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 May 6, 1937, were approved unanimously.

Telegrams to Messrs. Kimball, Clark and Young, Secretaries of the Federal Reserve Banks of New York, Atlanta and Chicago, respectively, stating that the Board approves the establishment without change by the New York bank on May 6, 1937, and by the Atlanta and Chicago banks today, of the rates of discount and purchase in their existing schedules.

Approved unanimously.

Telegram to Mr. Thomas, Federal Reserve Agent at the Federal Reserve Bank of Kansas City, reading as follows:

"Referring your April 27 letter, Board approves appointment of T. Bruce Robb as Alternate Assistant Federal Reserve Agent at your bank at his present salary of \$4,500 per annum, effective May 1, 1937, with the understanding that Mr. Robb will be placed upon the Agent's payroll and will be solely responsible to you for the proper performance of his duties. When not engaged in the performance of his duties

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"as Alternate Assistant Federal Reserve Agent he may, with the approval of the Federal Reserve Agent and the President, perform such work for the bank as in your opinion is not inconsistent with his duties as an Alternate Assistant Federal Reserve Agent. Mr. Robb should execute the usual oath of office and surety bond in the amount of \$50,000 and he should not enter upon the performance of his duties as Alternate Assistant Federal Reserve Agent until the bond has been examined by your counsel to determine whether its execution complies fully with the rules printed on the reverse side of form of bond 182, following which the bond should be forwarded to the Board promptly for approval."

Approved unanimously.

Letter to Mr. Wood, Vice President of the Federal Reserve Bank of St. Louis, reading as follows:

"Reference is made to your letter of April 28, 1937, relative to the inquiry of the St. Louis County Bank, Clayton, Missouri, whose application for membership was approved April 23, 1937, as to the applicability to the operations of the recently organized General Realty Company of condition of membership numbered 3, which reads as follows:

3. Such bank shall not engage as a business in issuing or selling either directly or indirectly (through affiliated corporations or otherwise) notes, bonds, mortgages, certificates, or other evidences of indebtedness representing real estate loans or participations therein, either with or without a guarantee, indorsement, or other obligation of such bank or an affiliated corporation.

The bank has asked specifically whether, under the provisions of the condition of membership, the realty company (1) may service the real estate loans which had been sold by the bank or take such other steps as may seem desirable in the refinancing and reselling of such loans, and (2) may engage for its own account in the sale of the ordinary type of real estate note. You also request to be advised whether, upon the admission of the bank to membership, the realty company will become an affiliate of the bank within the meaning of section 2(b) of the Banking Act of 1933.

"The realty company is said to have been organized to relieve the bank of its other real estate, to take over the servicing of the real estate loans which had been sold by

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"the bank prior to the discontinuance of that practice, and to take over the insurance department of the bank. As shown by its articles of incorporation, the powers of the realty company are, broadly, to transact a general real estate, real estate loan, and insurance agency business.

"According to the report of examination of the bank as of January 4, 1937, the General Realty Company was organized in November 1936 with a paid-in capital of \$42,500, represented by 425 shares of preferred stock, and with 1,000 shares of non par common stock, for which no cash was received. Under an agreement between the bank and the company, the common stock has been or will be issued to trustees under a voting trust agreement; and the trustees, in turn, have issued or will issue to the stockholders of the bank on a pro rata basis voting trust certificates representing the beneficial interest in the common stock of the company. The three trustees under the voting trust agreement were appointed by the bank and are directors of the bank, and vacancies among the trustees are to be filled by the bank. Of the five directors of the realty company, two are directors of the bank and one an officer.

"The management of the bank appears to be of the opinion that the provisions of condition of membership numbered 3 would be applicable to the operations of the General Realty Company only in the event the company is technically an affiliate of the bank. While it appears that, upon the admission of the bank to membership, the realty company may be an affiliate of the bank within the meaning of section 2(b) of the Banking Act of 1933, it is not necessary to determine that question in connection with the bank's inquiry. The question of whether the operations of the General Realty Company would be in violation of the condition of membership does not depend upon the existence of a technical affiliate relationship, as an 'affiliated corporation', for the purpose of the condition of membership, does not necessarily have to be a technical affiliate. Conditions of membership similar to condition numbered 3 in this case have, as you know, been uniformly prescribed by the Board for some time. The condition was adopted as a standard condition of membership in the interest of sound banking, as it was recognized that, although banks may have been under no legal liability on loans sold without recourse, the public in many cases assumed the existence of a moral responsibility on the part of the selling bank, and did so even in cases where the sales had been made through associated corporations. In some cases great difficulty was experienced by the banks which found it advisable to recognize the responsibility and to repurchase mortgages which had gone into default or

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"otherwise proved unsatisfactory, and in other cases embarrassment and loss of confidence resulted if demands for reimbursement by the investors were refused. It is felt, therefore, that, unless the St. Louis County Bank takes all possible steps to divorce the General Realty Company from the bank and to disassociate the company from the bank in the minds of the public, it would be in violation of condition of membership numbered 3 for the company to engage generally in the business of selling real estate loans to the public.

"However, the condition of membership was not intended to restrict the bank in discharging its responsibility for continuing to service the loans it had sold or to interfere with such steps as may seem necessary or desirable in connection with the refinancing of any such loans. Therefore, since such activities, even if performed by the bank, would not be in violation of the condition of membership, there is no objection under the condition of membership to the General Realty Company taking them over from the bank, regardless of the relationship of the bank and the company."

Approved unanimously.

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

"Reference is made to your letter of March 17, 1937, regarding the manner in which the Wachovia Bank and Trust Company, Winston-Salem, North Carolina, has been reporting the assets of its bond and insurance departments in reports of condition. It is understood that it has been the practice of the bank to treat its bond department and its insurance department as entities separate from each other and from the bank and to show in its statements of condition only the net control figures of the respective departments.

"The Board has no objection to the maintenance of whatever accounts the bank may desire to carry as a matter of internal accounting, provided the records are such as to reflect the true condition of the bank, but feels that the reporting of net control figures of the two departments in required reports of condition is not proper and that reports so rendered do not reflect the true condition of the bank. Reports of condition submitted to the Board should include under appropriate captions all actual assets and liabilities of the bank, regardless of how carried on the bank's departmental records. The Board has taken this position in similar

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"cases in the past and the banks involved have made appropriate changes in the method of preparing reports.

"Reference is made also to your comments regarding the purchase of stocks by the Wachovia Bank and Trust Company from certain trust estates which it is administering. You state that it was necessary to acquire the stocks to prevent threatened litigation against the bank and it is assumed that the litigation was threatened because of a potential liability which the bank has incurred to the trusts in connection with such stocks. You request advice as to whether a State member bank is justified in acquiring stocks under such circumstances and in holding them for a reasonable time to protect itself from loss.

"The Board has heretofore taken the position that the provisions of section 9 of the Federal Reserve Act and section 5136 of the Revised Statutes of the United States do not prohibit a State member bank from acquiring stocks held by it as collateral to a loan, if such acquisition is necessary to reduce loss or to eliminate the possibility of loss on the loan, but that a disposition of such stocks should be made as soon as is reasonably practicable. The Board feels that these provisions of law likewise do not preclude a State member bank from acquiring stocks in order to effect a bona fide adjustment or compromise in the discharge of a potential liability which the bank has incurred to trusts in connection with such stocks, and the Board will not raise any question with regard to such acquisition, provided the stocks acquired are disposed of at the first favorable opportunity. It is assumed, of course, that in any case the bank, in view of all the facts existing, will be justified under established trust principles in carrying out the transaction with a trust it is administering."

Approved unanimously.

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

"Reference is made to your letter of April 28, 1937 regarding certain questions which have been presented to you under Regulation U by Chemical Bank & Trust Company, New York, N. Y. You state these questions as follows:

- (1) May a bank, without regard to Regulation U, make a loan to a firm having membership in a national securities exchange on securities owned by the firm, if the purpose of the loan is to furnish

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"cash working capital for the conduct of the brokerage business of the firm; i.e., for purchasing and carrying securities for the account of customers but not for the firm's account?

'(2) May a bank, without regard to Regulation U, make a loan to a partner of such a member firm for the purpose of enabling such partner to make a capital contribution to his firm?

'(3) May a bank make either of the above loans if the firm maintains for the partner a margin account in which there is a debit balance?'

"While, as you indicate, all the facts involved in these cases are not entirely clear, upon the basis of the given facts and assuming the loans to be secured by stocks, the Board agrees with your view that the loans in each of the three instances referred to would ordinarily be subject to Regulation U. The situation represented by question numbered (1) seems to be quite similar to that covered in the Board's letter of April 5, 1937 (X-9862, Reg. U-13) and, on the principle stated in that letter, would seem to be a loan for the purpose of purchasing or carrying registered stocks. The other loans would seem to be subject to the regulation for substantially similar reasons.

"You refer to the question of whether or not it would be advisable to amend the regulation to exempt certain loans of the type here involved. Careful consideration has been given to the various aspects of the problem, including those phases of the matter discussed in your letter; and the problem will, of course, be given further study. It would seem to be preferable, however, for the present inquiry to be answered without regard to questions concerning such an amendment."

Approved unanimously.

Letter to Mr. Sargent, Vice President of the Federal Reserve Bank of San Francisco, reading as follows:

"Reference is made to your letter of March 27, 1937, regarding your examination program for the year 1937. It is noted that it has been difficult to work out satisfactory schedules for the examination of the State member banks in the various States in the district, and that the problem centers primarily in the five largest State member banks in California. You report that the State Banking Department concentrates its entire examining force for such examinations,

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"and that the State Department, although it cooperates to the best of its ability, is not always able to arrange the examination schedule to suit your convenience, with the result that it is not always possible to call in your examiners from other States and supply an adequate number of examiners to match the State examiners in the important assignments necessary in the examination of a large bank. You suggest two solutions, either or both of which could be employed:

1. To conduct independent examinations of some of the larger banks on dates that will fit into your own schedule, and/or
2. To examine two or three of the larger banks once every other year, accepting State reports for the odd years.

"You advise that in 1936 you made very complete examinations (including the trust departments) of the Wells Fargo Bank & Union Trust Co., and the American Trust Company, both of San Francisco, and that, in your opinion, the managements and conditions of these banks are such as to justify the acceptance of examinations made by the State for 1937, in lieu of your own examinations. You propose, therefore, unless the Board interposes an objection, to omit this year an examination of the Wells Fargo Bank & Union Trust Co., of San Francisco, and possibly the American Trust Company of San Francisco, and to conduct an independent examination of the California Bank, Los Angeles, if this should be necessary to permit you to complete your schedule of other examinations for 1937.

"In view of the reasons stated in your letter and of all of the circumstances, the Board will interpose no objection to your plan for this year so far as it concerns the Wells Fargo Bank & Union Trust Co., San Francisco, and the California Bank, Los Angeles. It is believed, however, that your annual examination of the American Trust Company, San Francisco, should not be omitted. This refers only to the examination program for the current year, and any modification of the general policy of regular examinations by the Federal Reserve Bank of each State member bank each year will depend upon the circumstances as they develop."

Approved unanimously.

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

"This refers to your letter of March 25, 1937, with

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"regard to the Board's letter of March 17 to Mr. Hill regarding the mortgage indebtedness of Mr. G. W. Shadle, an assistant examiner of your bank, to the Fidelity-Philadelphia Trust Company and Margaret J. Freeman, trustees under the will of Frank A. Freeman, deceased. In view of all the circumstances of this case, the Board has decided that it will not be necessary to make a report thereof to the local United States Attorney or to the Department of Justice."

Approved unanimously.

Thereupon the meeting adjourned.

Chester Morrie
Secretary.

Approved:

Wanda Freeman
Vice Chairman.