

A meeting of the Board of Governors of the Federal Reserve System was held in Washington on Wednesday, April 27, 1938, at 11:30 a.m.

PRESENT: Mr. Eccles, Chairman  
 Mr. Szymczak  
 Mr. McKee  
 Mr. Davis  
 Mr. Draper

Mr. Morrill, Secretary  
 Mr. Bethea, Assistant Secretary  
 Mr. Carpenter, Assistant Secretary  
 Mr. Clayton, Assistant to the Chairman

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 April 26, 1938, were approved unanimously.

Memorandum dated April 27, 1938, from Mr. Foulk, Fiscal Agent, stating that the sum of \$300 was due as salary to Mr. Charles S. Hamlin, Special Counsel to the Board, at the time of his death, and requesting authority to pay this amount to Mrs. Hamlin. The memorandum had been approved by Mr. Draper on behalf of the Personnel Committee.

Approved unanimously.

Letter to Mr. Newton, President of the Federal Reserve Bank of Atlanta, reading as follows:

"Referring to your letter of April 23, 1938, in order to clear the Board's records with respect to the salary of Mr. Malcolm H. Bryan, as Vice President of your bank, Mr. Bethea suggested to you when you were in Washington recently that you submit a formal recommendation for approval of the salary fixed for Mr. Bryan. It is understood that Mr. Bryan's salary was fixed at \$7,500 per annum by the directors of your bank after you received Chairman Eccles' letter of February

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"10, 1938, addressed to Mr. Neely, advising him that the Board of Governors was willing to approve a salary at the rate of not to exceed \$7,500 per annum, if fixed at such rate by your Board.

"In accordance with the action taken by your directors the Board approves a salary at the rate of \$7,500 per annum for Mr. Bryan, effective April 12, 1938."

Approved unanimously.

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

"In accordance with the request contained in your letter of April 21, the Board approves the appointment of Henry Benner as an examiner on a temporary basis for the Federal Reserve Bank of Philadelphia. Please advise us of the date the appointment becomes effective."

Approved unanimously.

Letter to the board of directors of "The Huron County Banking Company", Norwalk, Ohio, stating that, subject to the conditions of membership numbered 1 to 3 contained in the Board's Regulation H, and the following special conditions, the Board approves the bank's application for membership in the Federal Reserve System and for the appropriate amount of stock in the Federal Reserve Bank of Cleveland:

- "4. Such bank shall make adequate provision for depreciation in its banking house and furniture and fixtures.
- "5. As soon as practicable, such bank shall 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.
- "6. Prior to admission to membership, such bank, if it has not already done so, shall charge off or otherwise eliminate estimated losses totaling \$3,305.67 in loans and discounts and other real estate and depreciation of \$5,000.00 in defaulted

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"bonds, all as shown in the report of examination of such bank as of March 5, 1938, made by an examiner for the Federal Reserve Bank of Cleveland."

Approved unanimously, together with a letter to Mr. Fleming, President of the Federal Reserve Bank of Cleveland, reading as follows:

"The Board of Governors of the Federal Reserve System approves the application of 'The Huron County Banking Company', Norwalk, Ohio, for membership in the Federal Reserve System, subject to the conditions prescribed in the inclosed letter which you are requested to forward to the board of directors of the institution. Two copies of such letter are also inclosed, one of which is for your files and the other of which you are requested to forward to the Superintendent of Banks of the State of Ohio for his information.

"In the report of examination for membership the examiner classifies \$8,700 of the bank's investment in bank premises as estimated loss, such classification being based upon a verbal appraisal of the property by the officers of the bank. In his comments, however, the examiner points out that the bank recently made a charge-off of \$17,600 to provide for the accumulated depreciation at the rate of 2 per cent per annum from the date the property was acquired, and states that in view of this adjustment and the intention of the management to reduce the carrying value of the building as rapidly as earnings will permit, the management feels that a further charge-off on the investment should not be required at this time. In view of the circumstances, and in accordance with the suggestion contained in Mr. Fletcher's letter of March 30, the elimination of the \$8,700 classified as estimated loss in banking premises is not required as a condition of membership. It will be expected, however, that under the provisions of condition of membership numbered 4, which is a continuing condition, and in accordance with the expressed intention of the management, the bank will make adequate provision for depreciation in banking house and furniture and fixtures.

"In connection with the adjustments necessary in order to comply with that part of condition numbered 6 pertaining to the elimination of securities depreciation, it has been noted that both your examiner, in his report of examination, and the supervising examiner for the Federal Deposit Insurance Corporation, in his recent letter to Mr. Fletcher, refer to the \$18,800 reserve for securities depreciation as a

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"valuation reserve. In the report, however, the reserve is not treated as a valuation reserve but is included in the bank's capital account. The proper manner of treating valuation reserves, both by banks in their condition reports and published statements and by examiners in reports of examination of those banks, is known to your office and if the reserve in this case is a true valuation reserve it should be pointed out to the bank that no further adjustments are necessary in order to comply with that portion of condition 6 requiring the elimination of depreciation in defaulted bonds.

"There are listed in the confidential section of the report of examination for membership five savings accounts which do not conform to the definition of savings deposits as contained in the Board's regulations, and it is assumed of course that in the event the bank completes its membership such accounts will be brought into conformity with the regulations. In this connection, it has been noted that in the open section of the report the examiner refers to the list of nonconforming savings accounts appearing in the confidential section. Inasmuch as the confidential section of a report of examination is not made available to the bank examined, references in the open section to information contained in the confidential section hardly seem appropriate. It is suggested that this matter be brought to the attention of your examining staff."

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

"Reference is made to your letter of March 23, 1938, regarding Regulation T.

"It is understood that transactions effected on Monday in a general account resulted in a requirement of \$100 margin. On the day following, Tuesday, a certain quantity of a particular stock was purchased and later in the day the same quantity of the same security was sold, resulting in a net profit of \$150. There were no other transactions in the account on Tuesday.

"Sections 3(b) and 3(e) of the regulation read in part as follows:

'(b) General rule.--A creditor shall not effect for or with any customer in a general account any transaction which, in combination with the other transactions effected in the account on the same day, creates an excess of the adjusted debit balance of the account over the maximum loan value of the

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"securities in the account, or increases any such excess, unless in connection therewith the creditor obtains, as promptly as possible and in any event before the expiration of three full business days following the date of such transaction, the deposit into the account of cash or securities in such amount that the cash deposited plus the maximum loan value of the securities deposited equals or exceeds the excess so created or the increase so caused.

'A transaction consisting of a withdrawal of cash or registered or exempted securities from a general account shall be permissible only on condition that no cash or securities need be deposited in the account in connection with a transaction on a previous day and that, in addition, the transactions (including such withdrawal) on the day of such withdrawal would not create an excess of the adjusted debit balance of the account over the maximum loan value of the securities in the account or increase any such excess.

\* \* \* \* \*

'(e) Liquidation in lieu of deposit.\*--In any case in which the deposit required by section 3(b), or any portion thereof, is not obtained by the creditor within the three-day period specified in that section, securities shall be sold or covering or other liquidating transactions shall be effected in the account, prior to the expiration of such three-day period, in such amount that the resulting decrease in the adjusted debit balance of the account exceeds, by an amount at least as great as such required deposit or the undeposited portion thereof, any resulting decrease in the maximum loan value of the securities in the account.

'\* This requirement relates to the action to be taken when a customer fails to make the deposit required by section 3(b), and it is not intended to countenance on the part of customers the practice commonly known as "free-riding" or "three-day riding", to prevent which the principal national securities exchanges have adopted certain rules. See the rules of such exchanges and section 7(e) of this regulation.'

"You present the question of whether this purchase and sale may be treated, to the extent of \$100, as a liquidation pursuant to section 3(e) in lieu of a deposit of that amount of margin, and as also permitting a withdrawal of \$50 on Tuesday pursuant to the second paragraph of section 3(b).

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"The Board agrees with your view that the purchase and sale of the same securities on Tuesday may be so treated. This follows from the fact that such purchase and sale would reduce by \$150 any excess of the adjusted debit balance of the account over the maximum loan value of the securities in the account. It seems proper to treat such reduction as consisting of two portions in the manner suggested.

"It should, of course, be noted, as indicated in the footnote to the provision, that section 3(e) was not intended to countenance on the part of customers the practice commonly known as 'free-riding' or 'three-day riding', to prevent which the principal national securities exchanges have adopted certain rules. If the transactions on Tuesday were treated as indicated above, the liquidation in lieu of a deposit of margin would, of course, have to be considered in connection with such exchange rules."

Approved unanimously.

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

"Reference is made to Mr. Gidney's letter of April 15, 1938, regarding Regulation T.

"It is understood that on a given day the adjusted debit balance of a customer's general account exceeds the maximum loan value of the securities therein. The account is 'long' 100 shares of XYZ, a registered nonexempt security. On the day in question the customer sells 100 XYZ and instructs the broker not to deliver his 'long' stock against the sale. This is the only transaction in the customer's account on that day. The question presented is whether any margin must be obtained because of the transaction.

"It is the view of the Board that the sale of XYZ stock with instructions not to deliver the stock held 'long' in the account constitutes a short sale of the XYZ stock within the meaning of section 3(d)(3) of the regulation which provides that the adjusted debit balance of the account shall include:

'the current market value of any securities (other than unissued securities) sold short in the account plus, for each such security (other than an exempted security), such amount as the Board shall prescribe from time to time in the supplement to this regulation as the margin required for such short sales, except that such amount so prescribed in the supplement need not be included when there are held in

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"the account securities exchangeable or convertible within a reasonable time, without restriction other than the payment of money, into such securities sold short;".

"In view of this provision, the current market value of the securities sold short should be added to the adjusted debit balance. Since the XYZ stock held in the account could be delivered at any time against the short position, however, 'there are held in the account securities exchangeable or convertible \* \* \* into such securities sold short.' Therefore, it would not be necessary to add any 'margin \* \* \* for such short sales.'

"Section 3(d)(7) of the regulation provides that there shall be deducted from the adjusted debit balance:

'the net proceeds of sale of any securities (other than unissued securities) sold for the account but for which payment has not yet been credited thereto.'

"The deduction made pursuant to section 3(d)(7) would, on the day of the short sale, exactly equal and offset the additional made pursuant to section 3(d)(3).

"Accordingly, there would be no change in the adjusted debit balance of the account and, since there also would be no change in the maximum loan value of the securities in the account, the transaction would neither release margin nor require that margin be obtained."

Approved unanimously.

Memorandum dated April 27, 1938, from Mr. Spurney, Building Manager, submitting final invoices from the F. H. Martell Co., Inc., for the contract work performed by them on the attendant's house, wall and fence on the Board's parking lot, and recommending, with the approval of Mr. Morrill, that final payment on the contract, in the amount of \$644.31, which included certain extras, be made by the Board. The memorandum had been approved by Mr. Draper on behalf of the Personnel Committee.

Approved unanimously.

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There were submitted, with the recommendation of the Office of General Counsel that they be approved for publication in the May issue of the Federal Reserve Bulletin, rulings with respect to the following subjects:

Sale of Securities Held in Account but not  
Delivered Against Sale

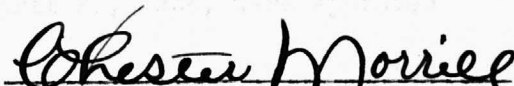
Effect of Purchase and Sale of Same Securities  
on Given Day

Approved unanimously.

Thereupon the meeting adjourned.

Approved:

  
Chairman.

  
Secretary.