A meeting of the Board of Governors of the Federal Reserve System was held in Washington on Friday, July 15, 1938, at 12:00 noon.

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

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:

Telegrams to Messrs. Kimball and Post, Secretaries of the Federal Reserve Banks of New York and Philadelphia, respectively, Mr. Walden, First Vice President of the Federal Reserve Bank of Richmond, Mr. McLarin, Vice President of the Federal Reserve Bank of Atlanta, Messrs. Young and Stewart, Secretaries of the Federal Reserve Banks of Chicago and St. Louis, respectively, Mr. Ziemer, Vice President of the Federal Reserve Bank of Minneapolis, Mr. McKinney, President of the Federal Reserve Bank of Dallas, and Mr. Sargent, Secretary of the Federal Reserve Bank of San Francisco, stating that the Board approves the establishment without change by the Federal Reserve Bank of San Francisco on July 12, by the Federal Reserve Banks of New York, Richmond, Chicago, St. Louis, Minneapolis and Dallas on July 14, 1938, and by the Federal Reserve Banks of Philadelphia and Atlanta today, of the rates of discount and purchase in their existing schedules.

Approved unanimously.

Letter to the "First National Bank in Boulder", Boulder, Colorado, reading as follows:

"The Board of Governors of the Federal Reserve System has given consideration to your application for fiduciary powers, and grants you authority to act, when not in contravention of State or local law, as trustee, executor, administrator, registrar of stocks and bonds, guardian of estates, assignee, receiver, committee of estates of lunatics, or in any other fiduciary capacity in which State banks, trust companies or other corporations which come into competition with national banks are permitted to act under the laws of the State of Colorado, the exercise of all such rights to be subject to the provisions of the Federal Reserve Act and the regulations of the Board of Governors of the Federal Reserve System.

"This letter will be your authority to exercise the fiduciary powers granted by the Board pending the preparation of a formal certificate covering such authorization, which will be forwarded to you in due course."

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 June 16, 1938 with respect to four cases submitted by the San Francisco Stock Exchange involving questions under the Board's Regulation T.

"Case 1. It is understood that a member of a national securities exchange sells short on the exchange for his own account certain securities at a price of $1,000. The buying member later agrees to accept a due bill for the securities and a check for $1,000. Pursuant to the rules of the clearing house, the selling member delivers the due bill and the check to the clearing house, and the transaction is settled. As a part of the settlement, the selling member receives payment for the sale in the usual manner.

"The first question is whether the selling member is

"required by Regulation T to deposit $500 with the buying member as margin on the short sale. The second question is whether such a deposit of margin would be required if the short sale had been for the account of a customer.

"It seems that the transaction in question may properly be considered to consist of two parts, first, a sale of securities and its completion by delivery of the securities, and second, a borrowing of securities for the purpose of effecting the delivery. It appears that the method of settlement is such that the acceptance by the buying member of the due bill is in effect a loan of the securities for the purpose of completing delivery. It is understood that, as a practical matter, the buying member's books often would not differentiate between such a receipt of the due bill and the making of an ordinary loan of securities.

"Section 6(h) of Regulation T provides that creditors may borrow and lend securities for the purpose of making delivery in the case of short sales without regard to the other provisions of the regulation. The Board is of the opinion, therefore, that, in the case cited, the selling member need not deposit margin with the buying member and that it is immaterial whether the sale is for the member's own account or for the account of a customer.

"Case 2. It is understood that A and B are partners of a firm which is a member firm of a national securities exchange. Transactions in the account of C, a customer of the firm, on a given day create an excess of the adjusted debit balance of the account over the loan value of the securities in the account. The question is whether Regulation T permits A, in his individual capacity, to make an advance of cash to C in the amount of the excess. If the advance were made by A, neither his nor B's capital or drawing account would be reduced.

"The Board is of the opinion that partner A, who is a 'creditor' within the meaning of that term as used in Regulation T, may not make the advance to the customer without obtaining the deposit of margin prescribed by the regulation.

"Case 3. This relates to a broker who conducts a regular security brokerage business in Canada, acquires membership in a national securities exchange in the United States, and buys and sells both registered and unregistered securities for Canadian and American customers. It involves interpretations of the Act and questions of

"the extraterritorial effect of statutes, and would depend in each instance upon the particular facts of the case. In the circumstances, the Board feels that it should not attempt to generalize upon the subject.

"Case 4. It is understood that customer A and her sons B and C each has an account with a member of a national securities exchange. Each account is operated separately although the mother furnishes all capital. Profits on the sons' transactions are taken by them, but if there is any loss, the mother absorbs it. A guarantees the accounts of B and C. On May 27, 1938, B and C made purchases requiring under Regulation T the deposit of $1,400 and $1,200, respectively, as margin. On May 31, 1938, A made a purchase requiring a margin deposit of $1,700.

"On June 1, 1938, A deposited in her account registered securities having a current market value of $5,250, and B liquidated securities in his account having a current market value of $2,700. The broker, acting in good faith, considered that the deposit and liquidation satisfied the requirements of Regulation T for the deposit of margin in all three accounts, with the exception of $70. On June 2, 1938, A purchased registered securities having a current market value of $1,400. At this time, the maximum loan value of the securities in all three accounts combined exceeded the combined adjusted debit balance by $2,500, after deducting the $70 not yet deposited in connection with the previous transactions. The $70 was deposited in cash on June 3, 1938. The question presented is whether any deposit of margin must be obtained in connection with the $1,400 purchase on June 2, 1938.

"From the facts as stated, it would appear that in this case there were three separate accounts, the accounts of B and C, and the account of A which guaranteed the first two. If this is the case, a deposit of margin in the guarantor's account could not serve the same purpose as a deposit of margin in the guaranteed account or a liquidation in such account.

"In order for a guarantee to be effective under section 6(c) the guarantor's account must contain the necessary excess margin for the transactions in the guaranteed account at the time such transactions are effected, and the necessary adjustments must be made pursuant to section 6(c) at that time, because when the need for a deposit of margin

"has arisen in an account sections 3(b) and 3(e) of the regulation require that there be either a deposit of margin in the account where the transaction was effected or a liquidation therein. The obtaining of a guarantee, or a deposit of margin or liquidation in a guarantor's account, is of no avail in such circumstances.

"It is understood that at the time of the transactions in the guaranteed accounts of B and C the maximum loan value of the securities in the account of guarantor A did not exceed the adjusted debit balance of the account. Therefore, the margin required by the regulation should have been deposited in the guaranteed accounts, or the appropriate liquidation effected therein.

"Actually, however, securities having a loan value of only $2700 were liquidated in the account of B. This transaction released margin of $1,080 leaving $320 still to be deposited. In the account of C, no deposit or liquidation was effected.

"The deposit in the account of A on June 1, 1938 of registered securities having a current market value of $5,250 more than satisfied the requirements of the regulation in connection with the purchase in her account on May 31, 1938.

"The facts stated do not clearly indicate whether the maximum loan value of the securities in A's account exceeded the adjusted debit balance of the account by $560 or more on June 2, 1938 when the $1,400 purchase was made. Such, however, is to be assumed from the fact that when the $5,250 market value of registered securities was deposited in the account on June 1, 1938 only $2,834 was required in connection with the previous transaction. If this assumption is correct, no deposit of margin was required in connection with the purchase on June 2, 1938; but, as indicated above, this would depend upon the status of A's account (including adjustments for the guarantees) rather than upon the combined loan value of the securities in all three accounts.

"While the foregoing opinions regarding the accounts of A, B and C appear to be correct, given the facts as stated, it may be that other circumstances not revealed would lead to different results. In the first place, the actual arrangements between the broker and A, B, and C may have constituted one single account with A, divided into three parts for convenience. In that case, the

"requirements of the regulation would seem to have been satisfied. Secondly, any failure by the broker to comply with the regulation may have resulted from such a mistake made in good faith as is referred to in section 6(k) of the regulation. In that case, the broker should take whatever action may be practicable in the circumstances to remedy the mistake."

Approved unanimously.

Letter to Mr. Parker, First Vice President and General Counsel of the Federal Reserve Bank of Atlanta, reading as follows:

"It is noted from your letter of July 9, 1938, that the bankers of Jackson, Mississippi, have invited your directors to meet in Jackson and that while the directors feel that generally speaking their meetings should be held in Atlanta and from time to time in a branch city, they feel that to accept the invitation would make for a closer relationship between the bank and its Mississippi members. The Board of Governors will interpose no objection to the holding of a regular monthly meeting of your Board of Directors in Jackson, Mississippi."

Approved unanimously.

Letter to Honorable Wayne C. Taylor, Assistant Secretary of the Treasury, reading as follows:

"This refers to your reply of March 23 to our letter of March 4, 1938, and to our letter of March 29, with respect to reimbursing the Federal Reserve banks for expenses incurred in redeeming adjusted service bonds.

"Mr. M. J. Fleming, President of the Federal Reserve Bank of Cleveland, who is Chairman of the Presidents' Conference Committee on Reimbursable Expenses, communicated with the other Federal Reserve banks recently with respect to the above matter and they have decided not to submit, at this time, monthly claims for reimbursement of their expenses incurred after June 30 in redeeming adjusted service bonds. They will, however, keep detailed

"records of their expenses in redeeming adjusted service bonds, and should such expenses amount to a substantial sum the question of reimbursement will again be taken up with you some time before the end of this year."

Approved unanimously.

Letter to Mr. B. L. Read, Fitch Investors Service, New York, New York, reading as follows:

"This refers to your letter of July 1 in connection with the manner in which a member bank of the Federal Reserve System, which has preferred capital stock outstanding with a retirable value of $50 and a par value of $20, reflects its capital account in published statements.

"Condition reports rendered by State bank members of the Federal Reserve System pursuant to the provisions of the Federal Reserve Act are submitted on Form F.R. 105, a copy of which is inclosed. You will note that State bank members are required to show on Form F.R. 105 under item 31, Capital account, not only the par value per share of preferred and common stock but also the retirable value per share of preferred stock.

"The Board's general instructions require that, in the case of State bank members with preferred stock outstanding, the single amount extended against sub-items (a), (b), (c) and (d) of item 31 be the sum of (1) the aggregate retirable value of the preferred stock, (2) the aggregate par value of the common stock, and (3) the amount of any capital notes and debentures outstanding, unless that sum is greater than the excess of the book value of the bank's assets over all of its liabilities (including reserves but excluding capital, surplus, and undivided profits). In the latter event, the excess of the book value of the bank's assets over all of its liabilities (including reserves but excluding capital, surplus, and undivided profits) must be shown in a single amount against sub-items (a), (b), (c) and (d) of item 31. The Board has authorized a modification of the above-described formula because in some States the capital account figures reported on Form F.R. 105 would differ from those reported to the State banking departments. Under the modified formula State bank members may, if they wish,

"use the par value of both common and preferred stock, rather than the par value of common stock and retirable value of preferred stock, in determining the amount to be shown against sub-items (a), (b), (c) and (d), provided that in such cases the caption 'Surplus' is amended to read 'Surplus over par value of capital stock'. Under either the general or the modified formula the equity of each class of stockholders on the basis of reported book values can be determined from condition reports rendered and published by State bank members pursuant to the provisions of the Federal Reserve Act.

"In this connection you may be interested to know that Section 345 of the Banking Act of 1935 contains the following provision:

> 'If any part of the capital of a national bank, State member bank, or bank applying for membership in the Federal Reserve System consists of preferred stock, the determination of whether or not the capital of such bank is impaired and the amount of such impairment shall be based upon the par value of its stock even though the amount which the holders of such preferred stock shall be entitled to receive in the event of retirement or liquidation shall be in excess of the par value of such preferred stock.'"

Approved unanimously.

Thereupon the meeting adjourned.

Chester Morrill
Secretary.

Approved: M S Eccles
Chairman.