

A meeting of the Board of Governors of the Federal Reserve System was held in Washington on Tuesday, April 9, 1940, at 10:30 a.m.

PRESENT: Mr. Ransom, Vice Chairman
Mr. McKee
Mr. Davis
Mr. Draper

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. Paulger, Chief of the Division of Examinations
Mr. Dreibelbis, Assistant General Counsel
Mr. Williams, Assistant Counsel

At Mr. Ransom's request, Mr. Williams reported on the legislative status of (1) bill H.R.6971 and S.2098 to amend the Federal Home Loan Bank Act, the Home Owners' Loan Act of 1933 and Title IV of the National Housing Act, (2) the Wagner resolution, S. Res. 125, and (3) the Jones Farm Credit bill, H.R.8747 and S.3509. He stated that it appeared that the first bill would be taken up on the floor of the House this week but that there were no plans for its immediate consideration by the Senate Banking and Currency Committee and that, if the bill passed the House, the Senate Committee probably would want to hold further hearings on it.

With respect to the Wagner resolution, Mr. Williams said that he had been informed that an economist to assist the committee

4/9/40

-2-

in directing the hearings had not been selected and that the questionnaire being prepared by the Senate Banking and Currency Committee to be sent to various agencies of the Government and other interested parties could be expected some time next week.

In connection with the Jones Farm Credit bill, Mr. Williams said that it was expected that a sub-committee of the House Committee on Agriculture would give consideration next week to the views expressed at the recent hearings by representatives of the American Bankers' Association and others as to the bill, that it was not yet determined whether further hearings would be held on the bill, but that it was expected that a decision would be reached next week as to whether the bill should be reported out at this session, and, if so, in what form. In this connection it had been indicated that if reported out it would be materially amended.

Mr. Ransom stated that, in accordance with the action taken at the meeting of the Board on April 5, 1940, he talked over the telephone with Mr. Brown, President of the Federal Advisory Council, with regard to the statement submitted by the Council at its meeting on November 21, 1939, with respect to bill H.R.6971 to amend the Federal Home Loan Bank Act and related legislation, that at Mr. Brown's request copies of the statement were sent by messenger to the Chairmen of the Banking and Currency Committees of the House and Senate yesterday and Mr. Brown was so advised by telegram, and

4/9/40

-3-

that it was understood from the conversation with Mr. Brown that he would send copies of the statement direct to the other members of the Banking and Currency Committees.

Mr. Ransom also stated that, as requested at the meeting of the Board on April 5, 1940, Mr. Dreibelbis had revised, and the individual members of the Board who were present had approved in the revised form, the report addressed to Chairman Wagner of the Senate Banking and Currency Committee on bill S.2098 to amend the Federal Home Loan Bank Act and related legislation. He (Mr. Ransom) suggested that the approved report be held in the Secretary's Office until Messrs. Dreibelbis and Williams had ascertained that the Banking and Currency Committee of the Senate was going to give consideration to the bill and had notified the Secretary's Office to that effect at which time the report would be forwarded to Senator Wagner by messenger.

Unanimous approval was given to Mr. Ransom's suggestion.

The report, as thus approved, read as follows:

"This is in reply to your letter requesting an opinion as to the merits of S. 2098, a bill 'To amend the Federal Home Loan Bank Act, Home Owners' Loan Act of 1933, Title IV of the National Housing Act, and for other purposes.'

"The Board is concerned by the broad implications of the bill in respect to the probable effect of its enactment upon the banking and credit structure of the country. Certain of its provisions would expand the permissible activities of Federal Savings and Loan Associations and

4/9/40

-4-

"other member institutions of Federal Home Loan Banks far beyond their original character as local mutual thrift and home-financing associations and would allow them to transact a large amount of general banking business. Other provisions would, by affording preferential insurance facilities to the shares of such associations, lend a degree of liquidity to them comparable to that of bank deposits. By thus, on the one hand, expanding the types of business in which such associations could engage so as to include a large amount of general banking business and, on the other, making it possible for them to compete with savings banks and savings departments of commercial banks and other financial institutions on favored terms, the enactment of the bill would tend to establish a separate and complete banking system. The question presented is so important that it would seem that Congress would be justified in studying this particular step carefully in its relation to the whole credit and banking structure, as a part of a comprehensive review of our banking, credit and monetary system such as is contemplated by S. Res. 125.

"It may be helpful to point out in some detail certain sections of the bill which the Board believes raise the foregoing question of the probable effect of the bill's enactment upon the banking and credit structure of the country.

"Sections 1, 2, 8, and 11 of the bill would materially expand the permissible activities of such associations.

"Section 1 would liberalize the class of collateral securities upon which Federal Home Loan Banks are authorized to make advances to their member institutions. At present, mortgages are restricted to 'home mortgages'. This section would completely eliminate any such restriction and would support any past or future enlargement of the lending powers of State-chartered member associations, as well as Federal Savings and Loan Associations by authorizing advances upon the security of any first mortgage.

"Section 2 would further extend the list of eligible collateral to a materially different class of securities, which would include not only obligations of the Federal Savings and Loan Insurance Corporation and of the Federal Home Loan Banks, but also any other obligations acceptable to the Federal Home Loan Bank Board which a member association might lawfully have available.

4/9/40

-5-

"Section 8 of the bill would allow Federal Savings and Loan Associations, under proper authorization from the Federal Home Loan Bank Board, to place 15 per cent of their assets (in addition to 15 per cent now allowed to be invested in first mortgages with no restrictions) in residential mortgages of any sort - not necessarily 'home mortgages' - within a 50 mile radius. This may be a justifiable change, but the restrictions of that section would apply only to Federally-chartered institutions. The lending powers of State-chartered institutions are governed by State law and the amendments proposed in section 1 would therefore encourage the latter to expand their activities to other fields instead of continuing as local mutual thrift and home-financing associations. Therefore, it would be desirable to place in section 1 restrictions upon advances by the Federal Home Loan Banks similar in terms to those which would be placed in section 8 upon the types of mortgages in which Federally-chartered associations are authorized to invest.

"Section 8 also would allow Federal Savings and Loan Associations to invest their assets in any securities that are legal investments for fiduciary and trust funds and are approved by regulations of the Federal Home Loan Bank Board. This might be justified as permitting associations to employ idle funds when satisfactory home mortgage loans are not available; but there appears to be no reason for permitting Federal Home Loan Banks to make advances upon such securities, as is done in section 2, if such securities are to be merely temporary investments and the associations are to continue as home-financing institutions.

"Section 11 of the proposed bill would change the name of the 'Federal Savings and Loan Insurance Corporation' to 'Federal Savings Insurance Corporation' thereby giving additional impetus to the transformation of the character of Federal Savings and Loan Associations from a system of local mutual thrift and home-financing associations into a separate banking system.

"Sections 14 and 15 of the bill would afford preferential insurance facilities to the shares of such associations, lending to them a degree of liquidity comparable to that of a bank deposit. The underlying reason for including these particular sections in the bill seems to be based upon an assumed analogy between shares and other liabilities of Federal and other savings and loan

4/9/40

-6-

"associations and savings deposits of savings banks and the savings departments of commercial banks.

"Section 14 would reduce the premium for insurance for Federal and other insured associations from the present rate of $1/8$ of one per cent to $1/12$ of one per cent.

"Section 15 of the bill, in the event of a default by an insured institution, would permit the payment of insured accounts to each insured member either by making available a transferred insured account in another insured institution or 'in such other manner as the Board of Trustees may prescribe.' It would permit, if the Board of Trustees so decided, the full payment of insured accounts in cash rather than in the manner now provided, to wit: 10 per cent cash, 50 per cent of the remainder within one year and the balance within three years in negotiable noninterest-bearing debentures of the Corporation.

"While it is true that $1/12$ of one per cent is the current rate of the Federal Deposit Insurance Corporation, the risks of the two types of insurance and the rates which should accordingly be charged for such insurance are not comparable. Such associations for the most part, are mutual in character. Their assets are normally on a long-term basis. Their liabilities are evidenced largely by obligations purchased by individuals seeking to acquire and hold an investment rather than to make a deposit.

"The Federal Deposit Insurance Corporation insures only the deposits of banks, and the net worth of banks, represented by the shareholders' interest in the banks' capital and surplus funds, protects depositors and the Corporation. Generally speaking, there is no comparable cushion in the case of the Federal Savings and Loan Insurance Corporation, whose member institutions are largely mutual in character and which insures withdrawable or repurchasable shares, investment certificates, or deposits. Ordinarily, therefore, a smaller percentage of losses on the part of one of its insured institutions will expose the Federal Savings and Loan Insurance Corporation to loss than will follow in the case of the Federal Deposit Insurance Corporation. Furthermore, the uninsured portion of deposits in insured banks, upon which banks pay premiums, is much greater than the uninsured liability in building and loan associations, which means that if the premium collected by the Federal Deposit Insurance

4/9/40

-7-

"Corporation was calculated with respect to the deposits insured rather than all deposits the rate of the Federal Deposit Insurance Corporation would actually be higher than 1/12 of 1 per cent.

"Individuals invest in the obligations of building and loan associations because they expect a higher rate of return than can be obtained in savings banks and the savings departments of commercial banks. Furthermore the rates of return permitted to be paid and actually paid by the associations upon their insured obligations are higher than the rates of interest permitted to be paid upon savings deposits. Investors in the associations should not expect to obtain the same degree of liquidity as in the case of a savings deposit because such associations, at the present time, are not expected to be and are not regarded as being, as liquid as banks. If their obligations are to be given the liquidity contemplated by this legislation, the discrepancy in the rate of return between such obligations and savings deposits will constitute another serious competitive disadvantage for national and State banks and will result either in the growth of unsound banking practices or in mortality among the institutions competing with the favored Federal and other savings and loan associations.

"For the foregoing reasons the Board of Governors is of the opinion that the enactment of the bill would not be in the public interest."

Mr. McKee then referred to the action taken at the meeting of the Board on April 2, 1940, when he was requested to discuss further with Mr. Wingfield, Assistant General Counsel, the draft of report to the Chairman of the Banking and Currency Committee of the Senate relating to the Investment Company Act of 1940. In that connection, Mr. McKee reviewed the discussions which he and Mr. Wingfield had had with representatives of the Securities and Exchange Commission with respect to the suggested amendment to the bill which would eliminate any material overlapping in supervision by the

4/9/40

-8-

Securities and Exchange Commission and the Board of Governors of investment companies which are also holding company affiliates and which have obtained voting permits from the Board, and stated that it was hoped that a form of amendment would be agreed upon and that, if that were accomplished, it would not be necessary for the Board to make a report on the bill.

There ensued a further discussion of the draft of report considered at the meeting on April 2 and it was agreed that Mr. Wingfield should be requested to redraft the letter along the lines suggested at the discussion and to re-submit it to the Board for consideration, it being understood that it would be held pending the outcome of discussions with representatives of the Securities and Exchange Commission regarding the suggested amendment.

In response to an inquiry from Mr. Davis, Mr. Williams said he did not think there was any likelihood of hearings being held by the Senate Banking and Currency Committee on the Jones Farm Credit bill at this session unless the bill passes the House and is sent to the Senate. Mr. Davis suggested that the Board, for reasons which he outlined, should not undertake to make a report on the bill to the House Committee on Agriculture, but should have a report ready for submission to the Senate Banking and Currency Committee when it appears that consideration will be given to the bill by that Committee. He added that members of the Board's staff were working on a draft of report which would be submitted to the Board in due course.

4/9/40

-9-

There was then presented a draft of letter to the presidents of all Federal Reserve banks, asking that they prepare and send to the Board as soon after May 1 as possible information with respect to the condition of member banks in their respective districts which are problem or near-problem cases. The draft of letter had been circulated among the members of the Board for their information before consideration at this meeting.

In the discussion of the letter which followed, it was pointed out by Mr. Paulger that the information requested was similar to that obtained on earlier occasions, and the question was considered whether a procedure should be established under which the information called for would be sent to the Board periodically or currently as to each bank as the report of examination of the member bank is received at the Reserve bank.

It was understood that Mr. Paulger would revise the letter and resubmit it to the Board for consideration and that it would be taken up again at a meeting when all of the members of the Board are present.

At this point Messrs. Thurston, Paulger, Dreibelbis, and Williams left the meeting and the action stated with respect to each of the matters hereinafter referred to was then taken by the Board:

The minutes of the meeting of the Board of Governors of the Federal Reserve System held on April 8, 1940, were approved unanimously.

4/9/40

-10-

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

"In accordance with the request contained in your letter of April 6, the Board approves the appointment of Herschel R. Johnson as an examiner for the Federal Reserve Bank of Chicago, and, as requested in your letter of April 5, the Board approves also the appointment of Matthew Francis Lynch as an assistant examiner.

"Please advise us of the effective dates of the two appointments."

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

"There is enclosed herewith a letter addressed to Mr. J. H. Durrell, Senior Vice President of The National City Bank of New York, interposing no objection to a proposal of such bank to open temporary 'Tellers Windows' in Havana, Cuba, for the purpose of accommodating visitors in connection with the International Conventions of the Rotarians and the Lions Club. It will be appreciated if your Bank will deliver the enclosed letter to Mr. Durrell at The National City Bank.

"There is also enclosed a copy of such letter, together with a copy of the incoming letter, for your files."

Approved unanimously, the letter to Mr. J. H. Durrell, Senior Vice President of The National City Bank, New York, New York, reading as follows:

"This refers to your letter of March 30, 1940, regarding the proposal of your bank to open temporary 'Tellers Windows' in Havana, Cuba, for the purpose of accommodating visitors in connection with the International Conventions of the Rotarians and the Lions Club.

"It is noted that the Rotarians are to hold their International Convention in Havana from June 10 through June 14, 1940, and in order to furnish special banking facilities for such occasions your bank proposes to open a temporary agency or 'Tellers Window' in the

4/9/40

-11-

"Central Gallego Building in which the Rotarians' headquarters is to be located and also one in the National Hotel. It is also noted that the Lions Club will hold its International Convention in Havana from July 23 through July 25, 1940, with headquarters at the Sevilla-Biltmore Hotel, and that you propose to open a similar temporary agency in that hotel for the accommodation of visitors.

"You state that the so-called 'Tellers Windows' will not receive deposits; but that they will cash travelers checks and bank drafts, pay checks on occasion, and sell or buy exchange and local currency. We also note that no one of the three temporary offices will be maintained for periods in excess of those stated above and that no additional equipment will be necessary except desks.

"If your proposal to furnish banking facilities is carried out as stated above, the Board will not interpose any objection thereto."

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

"This refers to your letter of March 28, 1940, transmitting the letter dated March 21, 1940, addressed to the Board of Governors of the Federal Reserve System by French American Banking Corporation, New York, New York, requesting that the Board increase from 12 to 15 times the Corporation's subscribed capital and surplus, the limit imposed upon the aggregate of all of the Corporation's acceptances outstanding plus the total of all deposits held by it, pending a definite determination as to the amount by which the Corporation's general reserves will be recoverable and the extent to which the surplus may be supplemented thereby. In transmitting the letter, you recommend that the requested increase in limitations be granted effective for one year, at the end of which time the present limitation would again become effective unless the Corporation should apply for and receive the Board's approval for a continuance of the higher limitation.

"The Board has given careful consideration to the application of French American Banking Corporation and to your recommendation made in connection therewith.

4/9/40

-12-

"However, it does not feel that it is desirable to change the formal limitation at this time.

"In view of the unusual circumstances now existing, the reported wide fluctuations in the volume of deposits with the Corporation, and the fact that, to a large extent, the increased deposits have been offset by balances with the Federal Reserve Bank of New York, the Board will interpose no objection, for the time being, should the Corporation's aggregate liability exceed the limitation prescribed in the agreement with the Board. This action is taken with the understanding that the Corporation will continue to maintain a condition of liquidity consonant with the nature of its liabilities, and upon condition that, as of the end of each month, the Corporation submit to the Board through the Federal Reserve Bank of New York a report showing as at the close of business for each day of the month (a) the amount of the Corporation's total deposits, (b) the amount of its acceptances outstanding, and (c) the amount of its collected balances, less any outstanding items of debit to such balances, with the Federal Reserve Bank of New York and the member banks with which its reserve funds are carried.

"It will be appreciated if you will advise the French American Banking Corporation of the Board's position in this matter."

Approved unanimously.

Letter to Mr. Worthington, First Vice President of the Federal Reserve Bank of Kansas City, reading as follows:

"Reference is made to your letter of April 3, 1940, with regard to the stocks of new Federal Reserve notes of the 1928 series.

"In view of the problem of vault space, the Board will offer no objection to cancellation and shipment to Washington for destruction of new Federal Reserve notes of the 1928 series at your branches. Should legislation be obtained authorizing the Treasury to replace the Federal Reserve notes of the 1928 series with notes without the gold clause, it is assumed that such authorization would include notes destroyed under the conditions set forth in your letter, provided an adequate record is

4/9/40

-13-

"kept of the serial numbers by denominations of the notes cancelled.

"In this connection, it may be mentioned that at certain other Federal Reserve bank branches steps have been taken to relieve the pressure for vault space by cancelling Federal Reserve notes of the 1928 series and sending them to Washington for destruction as outlined above."

Approved unanimously.

Letter to Mr. Clarke L. Fauver, Assistant Editor, Federal Home Loan Bank Review, Federal Home Loan Bank Board, reading as follows:

"In response to your letter of March 27, there is enclosed a statement showing (1) real estate loans on residential properties, and (2) residential properties owned, as reported by member banks at the end of December, 1938, and June and December, 1939, by States."

Approved unanimously.

Thereupon the meeting adjourned.

Chester Morrie
Secretary.

Approved:

Donald Hanson
Vice Chairman.