A meeting of the Board of Governors of the Federal Reserve System with the Federal Advisory Council was held in the offices of the Board of Governors in Washington on Monday, May 20, 1940, at 10:15 a.m.

PRESENT: Mr. Eccles, Chairman
Mr. Szymczak
Mr. McKee
Mr. Davis
Mr. Draper
Mr. Morrill, Secretary
Mr. Carpenter, Assistant Secretary
Mr. Goldenweiser, Director of the Division of Research and Statistics
Mr. Parry, Chief of the Division of Security Loans

Messrs. Steele, Fraser, Loeb, Huntington, Brown, Ragland, Crosby, Evans, Harding, and Dick, Members of the Federal Advisory Council representing the First, Second, Third, Fourth, Seventh, Eighth, Ninth, Tenth, Eleventh, and Twelfth Federal Reserve Districts

Mr. Charles E. Rieman, President, Western National Bank, Baltimore, Maryland, representing the Fifth Federal Reserve District in the absence of Mr. Robert M. Hanes

Mr. Walter Lichtenstein, Secretary, Federal Advisory Council

Mr. Brown stated that in the present critical period the Board must be faced with a number of important problems and that the Federal Advisory Council as a whole, through its executive committee, or the individual members of the Council, would be glad to hold itself in readiness to give any advice or assistance that would be useful to the Board, and that it was felt by the members of the Council that if,
when the Board adopts policies, it would explain them to the Council, its members would be in a position as operating heads of banking institutions in their respective districts to explain those policies to the country. Members of the Board expressed appreciation of the cooperative expressions of the Council.

Mr. Brown also said that the Council was working on a statement with respect to the topic suggested by the Board on the subject of easy money and that the Council would like to know whether, in view of the present unsettled situation resulting from war developments during the last few days, the Board still desired to have the members of the Council undertake a statement on the business prospects for the next three months. In connection with the latter topic Mr. Brown said that because of the confused situation resulting from the outbreak of total war in Europe it was felt by the members of the Council that there was no basis upon which anything like a reliable business forecast could be made for as far ahead as ninety days.

Chairman Eccles suggested that if there were sufficient time during the meeting of the Council with the Board tomorrow there might be some discussion of the current business situation.

Mr. Brown thanked the Board for sending to the members of the Council the banking studies prepared by the staff in connection with the Wagner Resolution and requested that, in order to save the time of the members of the Board and the Council, the Board designate someone
with whom a committee of the Council could meet and present such com-
ments and suggestions as the Council may have to make with respect to
the studies.

The statement was also made by Mr. Brown that the Council would
be interested in learning the Board's opinion on the Jones Farm Credit
Bill (H.R. 8748). Mr. Brown referred to the fact that Mr. Davis ap-
peared before Committees of Congress in connection with this bill last
week and inquired whether he had appeared as a member of the Board.
Mr. Davis replied that he had appeared as a member of the Board but
that he had made it clear that he was not necessarily expressing the
views of the Board and that he would be glad to hand to the members of
the Council copies of the statement which he made. He also outlined
briefly the consideration which he had given to the subject matter of
the bill in recent weeks and stated that he did not think there was any
likelihood of the bill passing in anything like its present form at
this session of Congress. Chairman Eccles said that the Board as such
had not taken a position on the bill, but comments by the members of
the Board made it clear that they were in general agreement with Mr.
Davis' statement before the Congressional Committees.

Mr. Brown stated that the Council felt very strongly that the
bill should not be enacted for the reason that it would permanently
remove commercial banks from the field of farm mortgage lending and
that, therefore, the Council would like to know whether the Board felt
a recommendation from it to be transmitted to the Congressional Com-
mittees and presumably given some publicity would be useful in strengthen-
ing sentiment against some of the principles implicit in the bill.
In the discussion which followed it was indicated as the consensus of
the members of the Board that inasmuch as there appeared to be little
likelihood of the bill being passed at the present session of Congress
no purpose would be served by adopting a resolution for transmission
to Congress at this time. However, Chairman Eccles suggested that, if
the Council desired, it might adopt a recommendation to be left with
the Board to be sent to Congress and released to the press at a time
to be determined upon.

Mr. Brown inquired whether there were any questions with re-
spect to the Government securities market or other matters which may
be urgent at this time that the Board would like to have the Council
consider in addition to those already on the agenda. There was a
discussion as to the possibility of passage of the various bills re-
ferred to in the agenda at this session of Congress and Chairman Eccles
stated that, while it could not be said that none of them would be en-
acted at this session, it did not appear at the moment that they would
be passed. However, he observed that the Steagall Federal Deposit
Insurance Corporation bill (H.R. 8638) and the Federal Home Loan Bank
bill (S. 2098) might still be pressed for passage before Congress
adjourns.

In connection with Mr. Brown's reference to possible urgent
Problems before the Board, Chairman Eccles stated that the principal problems created by the war situation were not within the field of responsibility of the Federal Reserve System, that such matters as the control of foreign property and funds of belligerent nations and their nationals and foreign exchange were being handled by the Treasury, that on these matters as well as the establishment of the Inter-American Bank, members of the Board's staff had participated in an advisory capacity but that the Board had no direct responsibility in connection with such matters, that the credit situation was one in which the System was without adequate powers to control reserve requirements and member banks were no longer borrowing from the Federal Reserve Banks, so that the discount rate was ineffective, that because of the restricted powers of the Federal Reserve Banks the field of industrial loans had largely been taken over by other agencies, and that the primary responsibility of the System at the moment was one of exercising a stabilizing influence in the Government securities market. He then reviewed briefly the situation in that market resulting from recent war conditions and stated that the System had been called upon to purchase less than $10,000,000 of securities as a stabilizing influence.

Chairman Eccles also referred to the Board's responsibility in connection with fixing margin requirements for the purpose of purchasing or carrying securities and stated that these requirements
were reduced in 1937 when the market declined sharply and that it was
generally felt at the present time that the existing margin of 40% was
a proper one for the reason that a lower requirement of say 30% might
encourage the purchase of securities in a situation where the spread
between the margin required by the Board and the maintenance margin
required by banks and brokers would be so small that if there were a
market decline of as much as five points the broker would be forced
to demand additional collateral or sell the borrower out.

Chairman Eccles inquired whether other members of the Board
had any suggestions to make to the Council as to matters which it
might consider at its separate meeting.

Mr. Draper stated that he felt that the Mead bill which would
expand the power of the System to make industrial loans would not be
given further consideration at this session of Congress but that con-
siderable attention was being paid to a suggestion made by Chairman
Frank of the Securities and Exchange Commission under which corpora-
tions would be created to purchase securities of new and more or less
speculative enterprises. Chairman Eccles stated that he had received
a confidential draft of a bill embodying the Frank proposal on which
his views had been requested before the bill is introduced, that he
expected to have a discussion on the draft in the next day or two,
and that he hoped legislation of this character could be avoided at
this session of the Congress.
Mr. McKee stated that he felt there was an opportunity for banks to extend substantial amounts of commercial credit to small business establishments with limited capital which receive orders from the Government, provided such establishments could assign their claims against the United States as collateral for loans from banks and that, therefore, he would suggest that the Council give further consideration to the recommendation adopted by it in November 1938 on this subject.

Mr. McKee also suggested that the Council consider the advisability of an amendment to Regulation U which would exempt from the margin requirements of the regulation loans by banks on registered stocks which are required to be amortized at a rate within the ability of the borrower to pay from funds which he has reasonable expectation of having available, it being understood that the regulation would limit the amount and maturity of any such loan. Mr. McKee read a draft of an amendment to Regulation U along the lines of his suggestion.

Mr. Brown suggested that consideration might also be given to a further amendment to Regulation U which would expand the permission now granted to a bank to take over from another bank an under-margined loan made for the purpose of purchasing or carrying registered stocks so as to permit a bank to take over such a loan from a broker; that his bank had received a number of applications for such loans recently which it would have been glad to take had it not been for the
Prohibition in the regulation; and that it appeared to him that such action would tend to take the pressure off the securities markets in periods of sharp decline. There was a discussion of these suggestions as well as the further suggestion by Mr. Evans that flexible margin requirements be adopted which would automatically increase margins in times of a market advance and reduce them in periods of market decline.

At Mr. McKee's request Mr. Parry reviewed the reasons why Regulation U had not permitted the transfer to a bank from a broker of an undermargined loan made for the purpose of purchasing or carrying registered stocks and stated that he knew of no reason why such permission should not now be granted. He also explained briefly why the statutory margin formula prescribed in the Securities Exchange Act of 1934 had been abandoned by the Board.

Mr. Szymczak stated that it had been suggested that consideration might be given by the Council to a procedure under which the members of the Council would meet with the boards of directors of the respective Federal Reserve Banks before as well as after meetings of the Federal Advisory Council for the purpose of discussing with the directors the matters considered by the Council at its meetings. In this connection Mr. Szymczak read extracts from the Congressional Committee reports on the original Federal Reserve Act with respect to the functions of the Federal Advisory Council.

Copies of Mr. Davis' statement regarding the Jones farm credit bill and of the press statement issued by the Senate Committee on
Banking and Currency relating to the questionnaire under S. Res. 125 were furnished to the Council for its use. It was stated by Mr. Lichtenstein that the Council had already received copies of the printed questionnaire.

Thereupon the meeting adjourned with the understanding that the members of the Council and the Board of Governors would meet again tomorrow following the conclusion of the Council’s separate meeting.

Chester Merriell  
Secretary.

Approved:  
Chairman.