

A meeting of the Board of Governors of the Federal Reserve System was held in Washington on Saturday, June 22, 1940, at 11:45 a.m.

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

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

The action stated with respect to each of the matters herein-after referred to was taken by the Board:

The minutes of the meeting of the Board of Governors of the Federal Reserve System held on June 21, 1940, were approved unanimously.

Letter to the board of directors of the "Farmers Trust Company", Franklin, Indiana, stating that, subject to conditions of membership numbered 1 to 6 contained in the Board's Regulation H, 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 Chicago.

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

"The Board of Governors of the Federal Reserve System approves the application of the 'Farmers Trust Company', Franklin, Indiana, for membership in the Federal Reserve System, subject to the conditions prescribed in

6/22/40

-2-

"the enclosed letter which you are requested to forward to the Board of Directors of the institution. Two copies of such letter are also enclosed, one of which is for your files and the other of which you are requested to forward to the Director, Department of Financial Institutions for the State of Indiana for his information.

"Since the amount of estimated losses classified in the report of examination for membership is small, the usual condition of membership regarding the elimination of estimated losses has not been prescribed.

"Since it is understood that in the State of Indiana trust funds deposited in the banking department of a bank are preferred claims in event of liquidation of the bank, you are authorized in accordance with the general authorization previously granted by the Board, with which you are familiar, to waive compliance with condition of membership numbered 6 until further notice."

Letter to the board of directors of the "Shelby Loan & Trust Company", Shelbyville, Illinois, stating that, subject to conditions of membership numbered 1 to 6 contained in the Board's Regulation H and the following special condition, 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 Chicago:

- "7. Prior to admission to membership, such bank, if it has not already done so, shall charge off or otherwise eliminate estimated losses of \$2,589, as shown in the report of examination of such bank as of May 25, 1940, made by an examiner for the Federal Reserve Bank of Chicago."

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

"The Board of Governors of the Federal Reserve System approves the application of the 'Shelby Loan & Trust Company', Shelbyville, Illinois, for membership in the Federal Reserve System, subject to the conditions prescribed in the enclosed letter which you are requested

6/22/40

-3-

"to forward to the Board of Directors of the institution. Two copies of such letter are also enclosed, one of which is for your files and the other of which you are requested to forward to the Auditor of Public Accounts for the State of Illinois, for his information.

"It has been noted that the bank has experienced rather serious difficulties in the recent past and is still regarded as a problem case by the supervising examiner for the Federal Deposit Insurance Corporation. While responsibility for the troubles is said to be chargeable to a former president of the bank, the ability of the present management to solve the problems is apparently subject to some question and remains to be proved. The Board has approved the application with the understanding that the Reserve Bank will give the bank close supervision, furthering the efforts of the supervising examiner's office toward a more efficient organization of the executive personnel and a more aggressive administration of the bank's affairs. It is requested in this connection that within six months after admission of the bank to membership a follow-up investigation, if not a complete examination, be made to determine the improvements effected and progress made in working out the bank's problems and that a full report be made to the Board. Any investigation or examination should, of course, cover the question of the attention being given to the large amount of charged-off assets as well as to the live assets of the bank."

Letter to Honorable Guy T. Helvering, Commissioner of Internal Revenue, reading as follows:

"This refers to your letter (IT:Rec:F:G-MSG) of May 2, 1940, relating to the credit claimed under section 26(d) of the Revenue Act of 1936 by Citizens and Southern Holding Company, Savannah, Georgia, in its income tax return for 1936.

"Upon the basis of the information contained in such tax return and the related papers, inspected at your Bureau by representatives of the Board, and the information otherwise available to the Board, the Board certifies that during the calendar year 1936 Citizens and Southern Holding Company devoted earnings or profits in the amount of \$5071.88 to the acquisition of readily marketable assets

6/22/40

-4-

"other than bank stock in compliance with section 5144 of the Revised Statutes."

Approved unanimously.

Letter to Mr. Lauchlin Currie, Administrative Assistant to the President, reading as follows:

"Your letter of May 28 addressed to Chairman Eccles requesting the views of the Board of Governors on the Mead Bill (S. 3867), which was introduced April 26, has been received.

"As you know, the Board considers it vital to obtain the necessary power to control a credit expansion if one should develop. The need for such powers has become more urgent in view of the fact that the accelerated defense program may carry the country's activity forward to a point where an inflationary development may become a proximate possibility.

"The Board is of the opinion, however, that the Mead Bill in its present form would not assure control over undue credit expansion. Since the banks' reserve requirements would depend on the ratio of their deposits to their capital accounts, they could evade the control provisions of the Bill by building up their capital accounts. Furthermore, the Board questions whether the deposit-capital ratio is a sound basis for determining a bank's reserve requirements. An unsound expansion of bank credit can be caused by expansion of credit at banks with adequate capital just as well as at banks with inadequate capital. Even as a measure of soundness the ratio of deposits to capital is not a satisfactory yardstick. A bank's capital is the cushion for absorbing losses that the bank may incur on its earning assets, and the adequacy of its capital cannot be measured by the relationship of capital to deposits alone, without reference to the character of the bank's assets or its indebtedness.

"The immediate effect of the enactment of the Mead Bill would most likely be a substantial liquidation of credit by banks with deposit-capital ratios above 12 to 1. If this ratio, the maximum provided by the Bill, were adopted by the Board, over 200 banks would be short of reserves by an aggregate amount of about \$1,000,000,000.

6/22/40

-5-

"Most of these would be large money-market banks that would have to borrow or liquidate assets in order to meet the new reserve requirements. Should the Board fix the ratio somewhere between 6 and 12 to 1, i.e., between the minimum and maximum limits contained in the Bill, many additional banks throughout the country, including banks in rural communities, would be short of reserves. In other words, in order to obtain an effective control over further undue credit expansion, it would be necessary to employ means which would tend to bring about a restriction in credit granted to many worthy commercial, industrial and agricultural enterprises.

"The pending Bill would make reserve requirements applicable to all banks insured by the Federal Deposit Insurance Corporation whether or not they be members of the Federal Reserve System. The Board favors this provision of the Bill. Without passing upon the question of the amount of assessment necessary to meet the requirements of the Federal Deposit Insurance Corporation, the Board would also favor the Bill's provision to exempt from assessment for deposit insurance the deposits that banks hold with the Federal Reserve Banks. On the same principle vault cash held by banks should also be exempted. While these two provisions are favored, the Board believes that they should not be enacted into legislation until Congress is prepared to undertake a comprehensive revision of Federal laws relating to bank reserves."

Approved unanimously, together with a similar letter to Mr. F. J. Bailey, Assistant Director, Legislative Reference, Bureau of the Budget.

Thereupon the meeting adjourned.

Whester Morrie
Secretary.

Approved:

Whester Morrie
Chairman.