

A meeting of the Board of Governors of the Federal Reserve System was held in Washington on Tuesday, August 25, 1942, at 9:30 a.m.

PRESENT: Mr. Ransom, Vice Chairman
Mr. Szymczak
Mr. Draper
Mr. Evans

Mr. Morrill, Secretary
Mr. Bethea, Assistant Secretary
Mr. Carpenter, Assistant Secretary
Mr. Clayton, Assistant to the Chairman
Mr. Smead, Chief of the Division of Bank
Operations
Mr. Dreibelbis, General Attorney
Mr. Wyatt, General Counsel.

Before this meeting, the attention of the members of the Board had been called to a letter dated August 12, 1942, from Mr. Lichtenstein, Secretary of the Federal Advisory Council, stating that the next meeting of the Council would be held in Washington on September 13-15, 1942, and requesting a list of the topics that the Board would like the Council to discuss at that time.

Mr. Morrill was requested to advise Mr. Lichtenstein by letter that, aside from such matters as it was understood would be discussed at the meeting of the Council, the Board had no topics to suggest, but that the Board would like to be advised in advance of any questions which the Council wished to present to the Board so that they might be studied in the meantime.

Reference was then made to the consideration that had been given to the problem of participation by the Federal Reserve Banks in foreign accounts maintained by the Federal Reserve Bank of New York

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and to the letter addressed to the Federal Reserve Bank of Boston on December 3, 1941, in which it was stated that, since a committee had been appointed by the Presidents' Conference to study the questions which had been raised in connection with these accounts, the Board would defer any further consideration of the subject until the committee had submitted its report. The Presidents' Conference committee report, which was approved by the Conference at its meeting on June 22-23, 1942, for submission to the Board for such action as it deemed appropriate, contained the following recommendations:

1. That the Board of Governors be requested to consider the desirability of revising Section IV of Regulation N, Series of 1933, and the Board's "Procedure with Respect to Foreign Relationships of Federal Reserve Banks" (X-9774, sent to the Federal Reserve Banks with the Board's letter of December 29, 1936). It is further suggested that the Board of Governors avail itself of the services of the legal subcommittee in drafting the suggested revision of Regulation N and the letter (X-9774) "Procedure with Respect to Foreign Relationships of Federal Reserve Banks".

2. That it be understood and agreed between participating Federal Reserve Banks, with respect to the attached form of letter (approved in 1937 by the Board of Governors of the Federal Reserve System and all of the Federal Reserve Banks), unless or until such form of letter is modified or amended;

- (a) that such form of letter sets forth the terms and conditions governing the accounts maintained by the Federal Reserve Bank of New York for foreign central banks (while such form of letter has not been sent to the foreign governments for which accounts are maintained on the books of the Federal Reserve Bank of New York, the terms and conditions governing the operations in such accounts are believed to be substantially the same as those set forth in such letter with respect to similar operations in accounts of foreign central banks);

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(b) that the letters in such form, from the Federal Reserve Bank of New York to the respective foreign central banks, constitute the contracts of the Federal Reserve Bank of New York and other participating banks with such foreign central banks; and that the character of the obligations of the participating Federal Reserve Banks to the foreign central banks and foreign governments for which accounts are maintained on the books of the Federal Reserve Bank of New York is determined by reference to such form of letter;

(c) that such form of letter indicates the scope of the participations of the Federal Reserve Banks in the foreign accounts maintained on the books of the Federal Reserve Bank of New York (that is to say, a Federal Reserve Bank participating in a foreign central bank or foreign government account on the books of another Federal Reserve Bank is deemed to participate in all transactions in that account which come within the scope of this standard form of letter, but would not be deemed to participate in transactions which such other Federal Reserve Bank might execute for the foreign central bank or foreign government with the approval of the Board of Governors outside the scope of such standard form of letter, unless participation in such transaction were specifically offered to and accepted by such participating bank).

3. That it is neither necessary nor desirable to include in the form of letter referred to in (2) above, nor in correspondence leading to and following the opening of foreign government accounts, reference to the agency status of the Federal Reserve Bank of New York, or to participations of the other Federal Reserve Banks in foreign accounts.

4. That it is not practicable or desirable to use a standard form of letter in connection with the opening of foreign government accounts.

5. That it be understood and agreed between participating Federal Reserve Banks that the rights and obligations as between them with respect to expenses, losses, and income incident to any participated foreign accounts (whichever Federal Reserve Bank might be the operating bank) are as follows:

(a) The net expenses of operating the foreign accounts maintained on the books of the operating bank and participated in by other Federal Reserve Banks (after deducting any amounts received in reimbursement of out-of-pocket expenses including labor costs in connection

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with the handling of gold) are shared by all participating banks, the other participating Federal Reserve Banks reimbursing the operating bank for their respective pro rata shares, calculated on the basis of their participation percentages determined as hereinafter described in 6(a).

(b) When income is received from the operation of participated accounts, for example, from the guarantee of payment of bankers acceptances purchased for account of foreign central banks, such income should be distributed on the same pro rata basis among all participating Federal Reserve Banks.

(c) Any losses for which the Federal Reserve Banks would be liable to the foreign central banks or foreign governments would also be shared on the same pro rata basis by all participating Federal Reserve Banks, unless a loss were due to the negligence of the operating bank, in which event that bank would bear the entire amount of such loss.

6. That the following operating and accounting procedures be followed with respect to participated accounts:

(a) Basis for determining percentages of participation. That the practice be continued whereby it is determined, as of the first of each year, what percentage the capital and surplus of each participating bank bears to the total capital and surplus of all participating banks, and the participation percentages thus determined for the respective participated accounts establish the pro rata shares of each participating bank in such respective accounts throughout that year; except to the extent that such participation percentages may be varied by reason of withdrawals from participation as hereinafter provided in 6(b); except that each participating bank's share of the total deposit liability in participated accounts will at all times be the amount actually shown on its books, which will (as hereinafter described in 6(c)) be adjusted from time to time as nearly as possible to these participation percentages.

(b) Withdrawal from participation.

That withdrawal from participation should be conditional upon the withdrawing bank giving notice of withdrawal to the Board of Governors, the operating bank, and each other participating bank, which notice of withdrawal must be received by the operating bank at least thirty days prior to the effective date of such withdrawal; that such withdrawal should constitute withdrawal from participation in all participated accounts, but should not

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terminate the withdrawing bank's responsibility for expenses and losses incurred with respect to transactions undertaken in the participated accounts prior to withdrawal; and that when such withdrawal is effective the withdrawing bank's participation should be automatically assumed by the other participating banks and a new computation made of the participation percentages of the remaining participating banks.

That refusal to participate in a new account should not require withdrawal from participations in all participated accounts; and that in the event of the refusal by a bank to participate in a new account, the participation refused by such bank should be automatically assumed by the other participating banks.

(c) Transfers through Inter-district Settlement Fund to adjust deposit liability of participating Federal Reserve Banks in connection with participated accounts. That transactions in participated dollar accounts be effected without any immediate change in the foreign deposit liability of the participating banks other than the operating banks; and that, in order periodically to adjust the foreign deposit liability of the respective participating banks as nearly as practicable to their participation percentages computed as provided in 6(a) above, transfers be made through the Inter-district Settlement Fund between the operating bank and the other participating banks on Wednesday of each week, and more frequently whenever there is a net change (since the last adjustment) of \$10,000,000 or more in the aggregate of the deposit liabilities in all participated foreign accounts unless it is anticipated that such change will be offset by further transactions before the next weekly adjustment. (This is substantially the procedure now followed.)

(d) Periodic reports from operating bank to participating banks.

That the operating bank should send to each participating bank by mail weekly, as of the close of business each Wednesday, a statement including the following information:

- (1) The amount due to each foreign depositor in a participated deposit account, and each participating bank's share, adjusted as described in 6(c) above, in the total deposit liability in all participated accounts.

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- (2) The amount of the contingent liability, if any, for the guarantee of bankers acceptances purchased for each participated account, and each participating bank's pro rata share in the total thereof.
- (3) The amounts of earmarked gold and securities held in custody in participated accounts.
- (4) The amounts of the deposits "Due from" foreign central banks, earmarked gold or investments in bills abroad, or outstanding foreign loans on gold, and each participating bank's pro rata share in the total thereof.

That the operating bank should inform each participating bank by telegraph each Wednesday of the amount of such participating bank's share, as of the close of business on that day, in the following:

The total deposit liability referred to in 6(d)

(1) above;

The total contingent liability referred to in 6(d) (2) above; and

The totals of the respective assets referred to in 6(d) (4) above;

and should also inform each participating bank by telegraph each Wednesday of the aggregate amount of earmarked gold, and the aggregate amount of securities, held in custody in all participated accounts, as referred to in 6(d) (3) above.

(e) That all published statements which contain items representing foreign accounts carry explanatory statements in the form of footnotes appended to the figures of the bank or banks operating the participated foreign accounts reading as follows:

"After deducting \$

other Federal Reserve Banks."

participations of

7. It is recommended that each such participation (in deposits abroad, earmarked gold or investments in bills abroad, or foreign loans on gold) should be a matter of agreement between the Federal Reserve Banks in the particular case, after participation has been approved by the Board of Governors. Similarly, since withdrawal from such participation would involve, in effect, a sale of assets by the withdrawing bank to other participating banks, such withdrawal should also be a matter of agreement between participating Federal Reserve Banks, subject to the approval of the Board of Governors.

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Under date of August 7, 1942, Messrs. Smead and Dreibelbis submitted a memorandum to the Board recommending (1) that the Board approve recommendation 6(e) contained in the committee report with the understanding that the footnote referred to therein would not be appended to the item "Other bills discounted" to indicate that it included foreign loans on gold, or to any other item in the condition statement of the Federal Reserve Banks which normally related to domestic operations but which on occasion might include some foreign items, and (2) that the Board authorize the staff to prepare, for submission to the Board with a recommendation, suggested revisions of Regulation N, Relations with Foreign Banks and Bankers, and the statement of procedure adopted by the Board with respect to foreign relationships of Federal Reserve Banks. The memorandum also submitted a draft of letter to the Presidents of the Federal Reserve Banks reading as follows and stated that, if the Board approved the recommendations contained in the memorandum, Messrs. Smead and Dreibelbis would like, for their guidance in carrying out the recommendations, to discuss the matter with the Board:

"Reference is made to the 'Revised Report of Presidents' Conference Committee on Foreign Accounts' of May 4, 1942. The Board has directed the staff to draft a suggested revision of Regulation N and the letter (X-9774) 'Procedure with Respect to Foreign Relationships of Federal Reserve Banks'. Following the suggestion in the report, members of the staff will avail themselves of the services of the Legal Subcommittee which acted for the Conference Committee.

"The change recommended in the weekly condition statement of Federal Reserve Banks, contained in paragraph (e)

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"on page 7 of the report, has been approved by the Board and will be made in the condition statement to be issued as of Wednesday, September 2, 1942."

Mr. Szymczak stated that when the Presidents' Conference Committee on Foreign Accounts was appointed Mr. McKee was designated by the Board as its representative to sit with the committee, and that before he left on his vacation he had noted on this file his concurrence with the recommendations made by Messrs. Smead and Dreibelbis. Mr. Szymczak also said that, under the rearrangement made on July 3, 1942, of assignments to individual members of the Board of various subjects requiring consideration or action by the Board, he had been assigned the subject of transactions with foreign banks and governments, that therefore it had been necessary for him to hold the file on the report of the Presidents' Conference committee and discuss it with Messrs. Smead and Dreibelbis so that he would be familiar with the background of the report, and that he was in agreement with the recommendations that they had made.

In the discussion which ensued, Mr. Dreibelbis stated that, if the letter referred to above were approved by the Board, it would be more or less committed to the recommendations contained in the committee report. He also said that the important questions involved in the committee's recommendations were (1) whether the present undisclosed agency status of the Federal Reserve Bank of New York should be continued, (2) how the participations of the Federal Reserve Banks should be shown in published statements, (3)

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what the rights and obligations of the Federal Reserve Banks were in accepting such participations, and (4) the right of a Federal Reserve Bank to withdraw from participation. Mr. Dreibelbis added that the proposed revision of Regulation N and the statement of procedure with respect to foreign relationships would establish rules under which the contracts of participation by the Federal Reserve Banks would be made and their rights and privileges would be generally defined, and that it was believed that this arrangement would largely meet the objections which had been raised in the past to accepting participations in these accounts.

Mr. Smead stated that if the recommendations submitted by him and Mr. Dreibelbis were approved it would be his further suggestion that the text of the statement of condition of the Federal Reserve Banks as of September 2, 1942, contain the following sentence:

"A footnote has been appended to the New York figures of 'Due from foreign banks' and 'Deposits: foreign' to indicate the amount of participations of other Federal Reserve Banks in the accounts."

At the conclusion of the discussion, upon motion by Mr. Szymczak and by unanimous vote, the letter to the Presidents of the Federal Reserve Banks and the sentence submitted by Mr. Smead for inclusion in the text of the weekly statement of condition of the Federal Reserve Banks as of September 2, 1942, were approved.

During the above discussion, Mr. Paulger, Chief of the Division of Examinations, joined the meeting, and at the conclusion of the discussion Messrs. Dreibelbis and Wyatt withdrew. While the

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matter next referred to was being considered Mr. Thurston, Special Assistant to the Chairman, came into the room.

Mr. Szymczak presented a draft of letter to President Fleming of the Federal Reserve Bank of Cleveland which had been prepared in accordance with the decision reached at the meeting of the Board on Saturday, August 22, 1942, requesting additional information with respect to the borrowings, existing indebtedness, and check transactions of G. H. Wagner, Vice President of the Cleveland Bank. Following the reading of the letter, there was a discussion of the question whether the additional information desired should be obtained by (1) addressing a letter to Mr. Fleming, (2) sending a representative of the Board to Cleveland to discuss the matter with President Fleming, (3) asking President Fleming over the telephone to submit the desired information, or (4) having Messrs. Fleming and Wagner come to Washington. It was the feeling of the members of the Board that the best procedure would be for Mr. Szymczak to call President Fleming on the telephone, stating to him that the Board desired additional information and raising with him the question whether he would prefer to have a representative of the Board go to Cleveland for the purpose of obtaining the information or whether he would rather have sent to him a list of the items upon which additional information was desired by the Board.

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At the conclusion of the discussion, it was agreed unanimously that Mr. Szymczak should proceed in accordance with this suggestion, and that he should keep Mr. Brainard, Chairman of the Cleveland Bank, advised of what the Board was doing in the matter.

At this point, Messrs. Smead and Paulger withdrew and Mr. Parry, Chief of the Division of Security Loans, and Messrs. Thomas, Krost, and Musgrave of the Division of Research and Statistics joined the meeting.

Mr. Ransom referred to his memorandum of July 15, 1942, which had been circulated among the members of the Board and to which was attached a copy of a memorandum submitted under date of June 22, 1942, to the House Ways and Means Committee by Randolph E. Paul, Tax Adviser to the Secretary of the Treasury, on the subject of the repayment of debts under high tax rates. In his memorandum of July 15, Mr. Ransom requested that the members of the Board consider the memorandum from Mr. Paul, as well as a memorandum on the same subject prepared under date of July 14, 1942, by Messrs. Goldenweiser, Thomas, and Stark, of the Division of Research and Statistics, so that the Board might be prepared to discuss the matter if in the future Mr. Paul should invite the Board's views. Mr. Ransom said that, at the invitation of the Secretary of the Treasury, he and Messrs. Thomas and Krost attended a meeting at the office of the Secretary yesterday evening during which there was a discussion of some of the problems referred to in Mr. Paul's memo-

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random. Following statements by Messrs. Ransom and Krost in which they reviewed the matters considered during the meeting at the Treasury, Mr. Ransom said that no action was called for by the Board but that he was reporting the discussions to the members of the Board at the request of Secretary Morgenthau.

At this point, Messrs. Thurston, Parry, Thomas, Krost, and Musgrave left the meeting, and the action stated with respect to each of the matters hereinafter referred to was taken by the Board:

The minutes of the meeting of the Board of Governors of the Federal Reserve System held on August 24, 1942, were approved unanimously.

Letter to the board of directors of "The Colonial Savings Bank", Fremont, Ohio, stating that, subject to conditions of membership numbered 1 to 3 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 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 Colonial Savings Bank', Fremont, Ohio, for membership in the Federal Reserve System, subject to the conditions prescribed in 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 Superintendent of Banks for the State of Ohio for his information.

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"It is assumed that you will follow the matter of the bank's bringing into conformity with the provisions of law and the Board's regulations the savings accounts listed on page 16 of the report of examination for membership, and making the necessary correction in the certificate of deposit form.

"The information submitted indicates that Messrs. D. L. and A. R. Christy may have a claim against the bank in the approximate amount of \$41,000 constituting a subordinated obligation of the bank which should be reported under item 33(b) of its reports of condition. It is suggested that you make such further inquiry as may be necessary to determine definitely whether such an obligation exists and, if so, call to the bank's attention the necessity of reporting it under item 33(b)."

Letter to the board of directors of "The Exchange Bank and Trust Company", El Dorado, Arkansas, stating that, subject to conditions of membership numbered 1 to 3 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 St. Louis:

"4. Prior to admission to membership, such bank, if it has not already done so, shall charge off or otherwise eliminate estimated losses of \$600, as shown in the report of examination of such bank as of July 10, 1942, made by an examiner for the Federal Reserve Bank of St. Louis."

The letter also contained the following special comment:

"It has been noted that while the bank is authorized to exercise fiduciary powers, actually it is doing so to a very limited extent. At the time of the examination as of July 10, 1942, made in connection with the application for membership, only one small account, a corporate trusteeship, was being handled and it is said that the management

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"does not expect to accept any other trust business. In the circumstances, the application has been approved on the same basis as if fiduciary powers were not being exercised and attention is invited to the fact that if the bank should desire in the future to exercise such powers beyond the extent necessary in connection with the one account now being handled, it will be necessary under condition of membership numbered 1 to obtain the permission of the Board before exercising them."

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

"The Board of Governors of the Federal Reserve System approves the application of 'The Exchange Bank and Trust Company', El Dorado, Arkansas, for membership in the Federal Reserve System, subject to the conditions prescribed in 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 Bank Commissioner for the State of Arkansas for his information.

"It is assumed that you will follow the matter of the bank's bringing into conformity with the provisions of law and the Board's regulations the savings accounts listed on page 16 of the report of examination for membership."

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

"Reference is made to your letters of August 7 and August 18, with enclosures, regarding the proposed purchase by the Merchants State Bank, Rhinelander, Wisconsin, of the interest in bank premises and furniture and fixtures held by the trustees for waiving depositors and settlement with the trustees of claims for rentals on the property. There are no applicable conditions of membership or statutory requirements which make it necessary that the Board pass upon the proposed transaction; however, you have asked for the Board's views on the matter.

"According to the information submitted, it is planned to pay to the trustees the sum of \$32,000, of which it is intended to add \$22,500 to the carrying value of banking

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"premises and \$3,740 to the carrying value of furniture and fixtures, and the remaining \$5,760 will be charged to expense as rent. On completion of the settlement the bank premises will be carried at \$72,500, which amount, it is said, is not out of line with the value of the property, and furniture and fixtures will be carried at \$12,890, or a total of \$85,390 as compared with an adjusted capital account of \$212,900 as reflected in the report of examination as of July 13, 1942. The bank is reported in good asset condition and under capable management, it has no other real estate, and the capital account appears adequate in relation to deposits of approximately \$1,320,000. Unquestionably, the waiving depositors are entitled to an equitable settlement and it is said that the Liquidation Division of the State Banking Department has been insisting that a settlement be made.

"In view of all the circumstances, therefore, the Board sees no reason to interpose any objection to the transaction as proposed."

Approved unanimously.

Letter to the Comptroller of the Currency, reading as follows:

"It is respectfully requested that you place an order with the Bureau of Engraving and Printing, supplementing the order of June 17, 1942, for printing of \$60,000,000 of Federal Reserve notes of the 1934 series for the Federal Reserve Bank of San Francisco in the \$5 denomination."

Approved unanimously.

Memorandum dated August 24, 1942, from Mr. Wingfield, Assistant General Attorney, recommending that there be published in the September issue of the Federal Reserve Bulletin statements in the form attached to the memorandum with respect to the following subjects:

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Reserves
Central Reserve City Banks

Consumer Credit
Amendment to Regulation W
Interpretation of Regulation W

Foreign Funds Control
General Rulings and Public Interpretation

Approved unanimously.

Thereupon the meeting adjourned.

Chester Morrie
Secretary.

Approved:

W. A. Fraser
Vice Chairman.