

A meeting of the Board of Governors of the Federal Reserve System was held in Washington on Wednesday, September 9, 1942, at 2:30 p.m.

PRESENT: Mr. Szymczak
Mr. McKee
Mr. Draper

Mr. Carpenter, Assistant Secretary
Mr. Thurston, Special Assistant to the
Chairman
Mr. Paulger, Chief of the Division of
Examinations
Mr. Dreibelbis, General Attorney
Mr. Cagle, Assistant Chief of the Di-
vision of Examinations

Mr. Szymczak stated that in accordance with the action taken at the meeting of the Board yesterday a draft of a letter to Mr. Brainard, as Chairman of the Federal Reserve Bank of Cleveland, had been prepared for consideration by the Board with respect to the indebtedness and check and other financial transactions of Mr. Wagner, who had resigned as Vice President of the Bank, and that, inasmuch as the regular meeting of the board of directors of the Cleveland Bank would be held tomorrow, it was desirable that the letter be sent today so that it could be considered at that meeting. The draft of letter was read and discussed and certain changes were suggested.

While the discussion was in progress, Mr. Ransom and Mr. Bethea, Assistant Secretary, joined the meeting, and at the conclusion of the discussion Messrs. Dreibelbis and Cagle withdrew to revise the letter in accordance with the suggestions that had been made. Mr. Paulger also withdrew from the meeting at this point.

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In response to an earlier telephone call received by Mr. Ransom's office from Mr. Sproul, President of the Federal Reserve Bank of New York, Mr. Ransom called Mr. Sproul on the loud-speaker telephone. After reviewing the present and prospective reserve position of member banks in New York City during the period of the forthcoming Treasury financing and the operations that might be necessary in the System open market account, Mr. Sproul stated that if he were to make a recommendation with respect to the timing of action by the Board of a further reduction of two percentage points in the reserve requirements of member banks in central reserve cities it would be that the reduction be announced on September 14, 1942, to become effective on September 18 or 19, which would be after the closing of the books, but prior to the payment dates on September 21 and 25, for the new Treasury securities.

During the conversation with Mr. Sproul, Mr. Smead, Chief of the Division of Bank Operations, and Mr. Thomas, Assistant Director of the Division of Research and Statistics, joined the meeting.

There was a discussion of the date upon which a further reduction in reserve requirements of central reserve city banks should be announced and made effective, and the whole matter was considered in the light of the Treasury financing program which contemplated that the subscription books for the new offerings of Treasury certificates and notes would be open for two days beginning September 10 and that the payment date for the certificates would be on September 21 and for the notes on September 25.

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Mr. McKee suggested that the Board give some thought to the desirability of action which would contemplate some reduction in reserve requirements for all banks as a means of increasing the proportionate amount of new issues of Government securities that would be purchased by interior banks and a like reduction in the purchases by banks in New York City and avoid the possible appearance at a later time that the Board was forced by circumstances to reduce reserve requirements for the country as a whole. It was felt, however, that in view of the existing volume of excess reserves of member banks outside of central reserve cities there was no necessity for a reduction at this time in reserve requirements for such banks.

While the discussion of this matter was in progress, Mr. Goldenweiser, Director of the Division of Research and Statistics, joined the meeting.

Mr. Goldenweiser suggested that the Board consider at this time a reduction in reserve requirements of member banks in central reserve cities to 20 per cent of demand deposits. He said that such action would fulfill any direct or indirect commitments that the Board might have with respect to action on reserve requirements and would leave it free to consider what its policy would be from that point on.

There was agreement on the part of the members of the Board that, inasmuch as a meeting of the Federal Open Market Committee would be held on September 28, 1942, at which the whole question of open market policy would be reviewed and at which time Chairman Eccles would

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have returned to Washington, no action should be taken by the Board beyond the informal understanding that reserve requirements of member banks in central reserve cities would be reduced by two percentage points sometime in September.

The remaining question for decision was one of timing of such a reduction, and various effective dates from September 5 to September 19 and dates of announcement from today to September 14, inclusive, were considered in the light of the forthcoming Treasury financing, including the agreed increase in the weekly Treasury bill offering beginning September 16. Some of the members of the Board were inclined to feel that action should be taken and announced immediately.

Mr. Ransom called Mr. Sproul on the telephone again and inquired as to his opinion with respect to (1) what, if any, effect an announcement before the Treasury financing operation of a reduction in reserve requirements of central reserve city banks would have on the financing, and (2) what effect such an announcement would have on the Treasury decision with respect to rates on the Series B tax notes.

Mr. Sproul's response to the first question was that the announcement would tend to increase the subscriptions of the New York banks to the new securities and, inasmuch as the new issues would be successful without such additional support, there was some advantage in postponing the announcement until after the books on the financing had been closed. In answer to the second question, Mr. Sproul said that the effect of the reduction would be so temporary that it could not have any bearing on the rates to be fixed for the tax note. Mr. Ransom also inquired whether

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Mr. Sproul felt that the increased bill offering would be taken without an announcement of a further reduction in reserve requirements, and Mr. Sproul stated that that could be taken care of through any necessary purchases for the System open market account and that that would be done.

During the discussion, it was pointed out that it would be desirable if the Board knew the views of the Treasury on timing due to questions of Treasury action on financing during this period. Mr. Ransom stated that the Treasury would prefer, if the Board should decide to take action on reserve requirements in September, to have the announcement on September 14.

At the conclusion of the discussion as to when action should be taken by the Board, it was agreed that the matter should be given further consideration at the meeting of the Board on Friday, September 11, 1942, at 9:30 a.m.

There was then presented the following revised draft of letter to Mr. Brainard, Chairman of the Federal Reserve Bank of Cleveland:

"The Board's attention has been directed to Mr. Fleming's letter of September 1, 1942, in which he advised Governor Szymczak of the resignation of Mr. George H. Wagner as Vice President of the Federal Reserve Bank of Cleveland.

"As Governor Szymczak explained to you after receiving Mr. Fleming's letter of August 19, 1942, the Board was not satisfied that sufficient facts had been developed with respect to Mr. Wagner's transactions. This feeling resulted

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"particularly from the nature of the statements in the anonymous letter which the Board received on June 15, 1942, apparently from some person employed by the Federal Reserve Bank of Cleveland, and the data set forth in a recent report of examination of a State member bank in Cleveland with respect to Mr. Wagner's borrowings. The anonymous letter was discussed with you and a copy was sent to Mr. Fleming on June 24, 1942.

"In order to have a better understanding of the situation, the Board sent Mr. Cagle, a member of its examining staff, to Cleveland to ascertain such facts as could be readily obtained in a brief investigation of the matter. Mr. Cagle has reported to the Board some facts which are startling and raise serious questions as to whether the matter should be closed without a full investigation and consideration of all pertinent facts by your board of directors.

"In his letter of September 1, 1942, to Governor Szymczak, Mr. Fleming states that Mr. Wagner's resignation was requested because he falsely reported to the Reserve Bank his indebtedness to member banks. There would seem to be no question that this is a fact, but there are also other important matters to which Mr. Fleming's letter makes only indirect reference. For instance, it appears that Mr. Wagner for several years had been handling his local bank account in such manner as to indicate questionable transactions of an important character. The following illustration is typical. On Monday, for instance, a check would be cashed about 9 or 10 A. M. and a corresponding amount of cash would be deposited to the account to meet payments on checks cashed or drawn on Saturday or Sunday. Tuesday's checks would be cashed and the proceeds deposited in sufficient amounts to meet the checks drawn on Monday, and so on to the next pay day. Sometimes the cash deposited on Tuesday would be exactly the amount of the two or three checks cashed or drawn on Monday, but usually the amounts increased from day to day. The process would start around the fifth of the month and build up to the pay day on the fifteenth, and again around the twentieth and build up to the pay day at the end of the month. The volume of transactions in his account was out of all proportion to his apparent financial condition and clearly indicated kiting operations. Many of the checks involved in the kiting operations were cashed at the Federal Reserve Bank of Cleveland. Indeed, it appears that in some months checks cashed at the Reserve Bank alone were considerably in excess of his salary.

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"Mr. Cagle reported that over a period of years extending through June 25, 1942, large deposits of currency were made from time to time in Mr. Wagner's bank account in addition to the deposits arising clearly out of kiting, salary, and loan transactions. Approximately ten such deposits were noted during the first half of 1942. A lesser, but considerable, number of such deposits were noted in prior years.

"It is understood that for a number of years it has been a part of the audit routine to review records of the bank with respect to checks cashed by officers and employees, especially if in large volume. Mr. Cagle reports that the volume of Mr. Wagner's checks cashed was the subject of comment as far back as when he was with the Pittsburgh Branch. It is understood that the auditor required his representative at Pittsburgh to make an informal report to him of Mr. Wagner's checks cashed during each fifteen-day period, particularly if they exceeded his salary for the same period. When Mr. Wagner returned to Cleveland in January 1938, the auditor's assistants there were instructed to make a similar report of any undue cashing of checks. Mr. Grayson advised that on a number of occasions, especially when Mr. Wagner's check cashing activities were above the average, he called the matter to Mr. Fleming's attention. One such instance was in April or May 1941, when Mr. Grayson was instructed by Mr. Fleming to obtain additional information through a review of Mr. Wagner's account and certain transactions in one of the member banks in Cleveland. As a result of these efforts and other information available to some of the officers of the Reserve Bank, Mr. Wagner's reports of financial obligations, and certain activities, were brought before a committee of directors in July or August 1941.

"Mr. Cagle was informed that it was a matter of common gossip among a considerable percentage of the older employees that Mr. Wagner was cashing a large volume of checks and was possibly financially involved.

"Summarizing the matter as it has been brought to the attention of the Board, it now appears that Mr. Wagner has been financially involved for several years. However, the facts with respect to such involvement do not appear to have been reflected in the records and files of the Reserve Bank and have not been brought to the attention of the Board's examiners in their annual examinations of the Reserve Bank. The Board had no indication of such situation until the receipt of the anonymous letter in June 1942. The burden of such involvement was carried partly through kiting transactions, a large portion of which originated in the Reserve Bank through the cashing of checks. The large volume of

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investigation, it being understood that, should it be found desirable at a later time to hold a special meeting of the board of directors of the Bank at which Mr. Szymczak would be present, such an arrangement would be made.

At this point, Messrs. Thurston, Goldenweiser, Smead, and Thomas 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 September 8, 1942, were approved unanimously.

Letter to Mr. Hays, Vice President and Secretary of the Federal Reserve Bank of Cleveland, reading as follows:

"In accordance with your request the Board of Governors approves the changes in the personnel classification plan of the Head Office and the Cincinnati and Pittsburgh Branches of your bank, as submitted with your letter of August 20, 1942."

Approved unanimously.

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

"As requested in your letter of August 27, 1942, the Board of Governors approves, effective as of September 1, 1942, the payment of a salary to A. J. Mulroney, Vice President, at the rate of \$15,000 per annum for the period ending March 31, 1943."

Approved unanimously.

Telegram to Mr. Bryan, First Vice President of the Federal Reserve Bank of Atlanta, reading as follows:

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"Retel there are no definite plans for general enforcement conference on Regulation W in the near future. Accordingly you may wish to have special representation for Regulation W at the Examiners' Conference when the whole question of enforcement policy will be open for discussion."

Approved unanimously.

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

"Replying your telegram September 4 concerning S-546 (a Regulation W interpretation). If coal to be used is such that, because of its physical characteristics, it cannot be hand-fired, as is the case with very fine coal, then stoker comes within exception (that stoker installed in connection with change of fuel, as from oil to soft coal or from hard coal to soft coal, qualifies only when stoker is necessary for mechanical reasons to burn the type of coal to be used)."

Approved unanimously.

Thereupon the meeting adjourned.



Assistant Secretary.

Approved:


Vice Chairman.