

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, September 14, 1942, at 10:40 a.m.

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

Mr. Bethea, Assistant Secretary
Mr. Carpenter, Assistant Secretary
Mr. Clayton, Assistant to the Chairman
Mr. Thurston, Special Assistant to the Chairman
Mr. Goldenweiser, Director of the Division of Research and Statistics
Mr. Paulger, Chief of the Division of Examinations
Mr. Parry, Chief of the Division of Security Loans
Mr. Dreibelbis, General Attorney
Mr. Vest, Assistant General Attorney
Mr. Wyatt, General Counsel
Mr. Kennedy, Assistant Chief, Government Securities Section, Division of Research and Statistics
Mr. Berntson, Clerk in the Office of the Secretary

Messrs. Charles E. Spencer, Jr., George L. Harrison, William F. Kurtz, B. G. Huntington, Robert V. Fleming, H. Lane Young, Edward E. Brown, S. E. Ragland, Lyman E. Wakefield, W. Dale Clark, and George M. Wallace, members of the Federal Advisory Council representing the First, Second, Third, Fourth, Fifth, Sixth, Seventh, Eighth, Ninth, Tenth, and Twelfth Federal Reserve Districts, respectively

Mr. Walter Lichtenstein, Secretary, Federal Advisory Council

Mr. Ransom stated that Chairman Eccles and Mr. Evans were absent from Washington on vacation and that Mr. Szymczak was out of the City on official business of the Board.

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Mr. Brown stated that at its separate session yesterday the Council adopted a resolution with respect to the renegotiation of war contracts, which was not intended for publication, and that it wished to discuss the resolution and certain other matters with the Board of Governors.

The resolution was read by Mr. Lichtenstein as follows:

"The Federal Advisory Council is concerned about the possible danger that in the renegotiation of war contracts the credit position of a contracting concern may be altered to a point where credits extended in good faith to it may be endangered.

"The Council suggests to the Board of Governors that it use its influence to the end that a provision be included in the law to protect banks and others who have so extended credit by making any claim or debt due to the Government, by reason of a renegotiation, subordinate to the claims of bona fide creditors. As the law stands at present any debt due the Government has a priority over debts due other creditors."

Mr. Brown stated that the subject of renegotiation of war contracts was becoming increasingly important because of the fact that applications were being received for large Regulation V loans from contractors who have completed contracts which were subject to renegotiation, that the right of the Government to renegotiate any contract, whether presently existing or completed and paid for in full, might endanger credits subsequently extended, and that, unless something along the lines suggested in the Council's resolution were adopted, this situation might interfere with the ability of the Government to finance such contractors. He went on to say that the Council also felt the matter was one with which the Board should concern itself because of its responsibility for maintaining the solvency of banks and its interest in Regulation V loans.

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Mr. McKee suggested that either Colonel A. J. Browning, Director of the Purchases Division, Headquarters Services of Supply, War Department, or Mr. Maurice H. Karker, Chairman of the War Department Price Adjustment Board, be asked to appear before the Council and explain the War Department's views with respect to the matter.

Following a reference to the organization provided in the War Department for the review of prices on war contracts, and a discussion of the present law with respect to the renegotiation of contracts, during which it was emphasized that the step suggested by the Federal Advisory Council would require an amendment to the law, Mr. Harrison suggested the appointment of a joint committee of the Council and the Board to meet with representatives of the War Department. This suggestion was agreed to, and Mr. Clayton was requested to get in touch with Colonel Browning of the War Department and see if the meeting could be arranged today. Mr. Clayton left the room for that purpose and upon his return stated that Colonel Browning would not be available but that Charles O. Pengra, Counsel for the War Department Price Adjustment Board, would be available for a luncheon meeting. It was understood that the Board's War Loans Committee, consisting of Messrs. Draper, McKee, and Clayton (in the absence of Chairman Eccles), and Messrs. Brown, Spencer, Wakefield, and Wallace, representing the Federal Advisory Council, would meet with Mr. Pengra, and that if following the meeting the representatives of the Council thought it desirable to make changes in the resolution adopted by the Council they would be authorized to do so.

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Mr. Brown then stated that the Council would like to discuss with the Board the question of the absorption by banks of exchange and collection charges. Upon inquiry from Mr. Ransom as to whether the Council had any solution to suggest, Mr. Brown said that a large majority of the Council would favor the enforcement of Regulation Q, Payment of Interest on Deposits, to the point where the only exception with regard to the absorption of exchange charges would be where the bookkeeping costs involved in putting the charges through would be greater than the amount of charges. He also said that with increased rates on short-term funds it was now possible for banks to absorb exchange charges and make money on bank balances, that while the Boston, New York, Chicago, and San Francisco Districts were not confronted with the problem the remaining Federal Reserve Districts were, and that it was the feeling of the Council that some administrative action should be taken by the Board, the Comptroller of the Currency, and the Federal Deposit Insurance Corporation so that the present growing practice of using the absorption of exchange charges as a means of attracting bank deposits would be stopped.

Mr. Ransom stated that the difficulty arose because the language of the statutes under which the regulations of the Board of Governors and the Federal Deposit Insurance Corporation were issued were not identical and the Federal Deposit Insurance Corporation did not feel it could issue a regulation similar to that proposed by the Board. He also said that the actions to solve the problem would include an amendment to the law or a change in the position of the Federal Deposit

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Insurance Corporation, that if the matter were presented to Congress it might repeal the prohibition against the payment of interest on demand deposits rather than make the applicable provisions of law uniform, and that, therefore, it appeared that the most logical approach would be to take the matter up again with the Federal Deposit Insurance Corporation.

Some of the members of the Council suggested that this be done and some expressed the opinion that, if the Board would take action in the more important cases where it appeared that banks were violating Regulation Q, all member banks would fall in line.

Mr. Brown then stated that, in response to Mr. Ransom's request at the last meeting of the executive committee of the Council with the Board, Mr. Lichtenstein had made a summary of reports received from the members of the Council with respect to the extent to which the volume of single-payment loans was being reduced in the respective Federal Reserve Districts. A copy of the summary, together with copies of an analysis of the replies made by banks in the Cleveland District and a memorandum on the subject submitted by Mr. Wallace, have been placed in the Board's files. During the discussion of the summary, Mr. Parry said that, while the reports were not conclusive, they were indicative of a definite downward trend in the volume of single-payment loans. Comments by several members of the Council confirmed the statement made earlier in the discussion that the volume of all types of consumer credit was declining rapidly.

Mr. Brown then inquired whether the Board felt the Council could be helpful by reiterating its former position with respect to the

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silver question. He said the Council felt that at a time like the present, when there was a demand for silver for industrial purposes and the Treasury could dispose of its silver holdings without a loss, the war effort should not suffer by reason of the failure of the Treasury to take that step.

Mr. McKee said that the time when a recommendation of the Council on this matter would be presented might be of some importance, and the members of the Council agreed that the matter could be taken up again at a later date.

In this connection, Mr. Young stated that he had recently tried without success to obtain \$10,000 in nickels, dimes, and quarters from the Federal Reserve Bank of Atlanta and the New Orleans Branch, and he inquired whether more silver could be used in the minting of more of these coins to correct that situation. Mr. Ransom said the Board would look into the matter.

Mr. Brown then stated that a number of the Council members had been asked whether small banks should be urged to open war loan accounts, that the general feeling of the Council was that only banks in reserve cities with correspondent bank balances or banks with deposits subject to wide fluctuations should have war loan accounts, and that, while every bank in the System should know what a war loan account was, any attempt to influence banks unaccustomed to handling rapidly fluctuating balances to establish war loan accounts would be a mistake.

Messrs. Ransom and McKee stated that this matter had not previously been brought to the Board's attention, that, while it might have

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come up in the field, in connection with the sale of Treasury bills or the activities of the Victory Fund Committees, the suggestion had not come from the Board, and that the Board would make inquiry as to how it had originated.

Mr. Brown said the Council understood there had been discussions with respect to using the banks to do the work in connection with the collection of coupons used in the rationing of commodities, and that, while it was realized that the matter was still in the discussion stage, the Council felt that, on the basis of present discussions, banks were best able to do the work, that banks should not make a profit from the program but should be compensated for out-of-pocket expenses, that a representative committee of bankers should work out the technical details of the program with representatives of the Office of Price Administration, and that, if the banks undertook the task, consideration should be given to their requirements for additional machinery and manpower. In connection with the latter point, several of the members of the Council commented on the seriousness of the personnel problem facing the banks.

Mr. McKee stated that recently members of the Board and its staff met with representatives of the Office of Price Administration and Mr. Borden of the National City Bank of New York, at which meeting some of the problems involved were discussed, and that at that time the Office of Price Administration representatives advised that a plan worked out by them was to be tried out on an experimental basis in a selected area in the State of New York in the near future.

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Mr. Brown then referred to the discussions at the last meeting of the executive committee of the Council with the Board with respect to the monthly meetings of the executive committee and stated that the Council felt very strongly that the executive committee meetings with the Board were highly desirable and should be continued in view of rapidly changing world events, and that the Council would be glad to furnish the Board in advance of each meeting with a list of the topics that the committee would like to discuss.

Mr. Ransom stated that the decision whether the meetings were to be continued rested with the Council, and that if it felt the meetings were constructive and helpful that would seem to be the controlling factor. He emphasized, however, that it was very helpful to the Board to be advised beforehand of the subjects which the committee wished to consider at the meetings. Mr. Brown stated that arrangements had been made for each member of the Council to submit suggested topics for discussion at the meetings of the executive committee with the Board and that the topics in turn would be forwarded to the Board by Mr. Lichtenstein.

Mr. McKee referred to a conversation he had had recently in which the question was raised whether there was a place for surety companies in the war loans program as reinsurer of the risks taken by financing institutions in connection with war loans, and he expressed the opinion that if the program contemplated by Regulation V were going to be successful it would be necessary for financing institutions to retain a financial interest in all loans made by them and to see that the loans were properly serviced.

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Mr. Spencer commented that the ability of the banks to render such service would depend upon their being able to retain the necessary trained personnel, and members of the Council spoke in support of a statement by Mr. Fleming that the time was coming when banks would need the aid of the bank supervisory agencies in the banks' efforts to obtain the necessary personnel to render essential banking services.

Mr. McKee also stated that in several cases the rate on large Regulation V loans had been predicated in part on the eligibility of the paper for rediscount at a Federal Reserve Bank, and that he would appreciate it if the executive committee of the Council would give some thought to whether, from the standpoint of the objectives of the war loans program, it would be helpful if such paper were eligible for rediscount. In the discussion of this matter, it was pointed out that in any event the paper would be eligible as collateral for loans to member banks under section 10(b) of the Federal Reserve Act, and the members of the Council concurred in the opinion that the question of eligibility would not have any effect upon the rates charged on the paper.

Thereupon the meeting adjourned.



Assistant Secretary.

Approved:



Vice Chairman.