A meeting of the Board of Governors of the Federal Reserve System was held in Washington on Thursday, August 31, 1944, at 10:30 a.m.

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

Mr. Bethea, Assistant Secretary
Mr. Carpenter, Assistant Secretary
Mr. Clayton, Assistant to the Chairman
Mr. Smead, Director, Division of Bank Operations
Mr. Vest, Assistant General Attorney

Chairman Eccles reviewed the informal discussions which he and Mr. Clayton had had with Colonel Mechem of the War Department, Mr. Hinckley, Director of Contract Settlement, and Colonel McKinney, of Mr. Hinckley's office, with respect to the maximum interest rate and guarantee and commitment fees to be prescribed by the Board at the time of the issuance by it of Regulation V as revised in connection with the program for financing the claims of contractors, subcontractors, and others arising out of the termination of war contracts. He said that the Services had been strongly of the opinion that the maximum rate on termination loans should be 5 per cent, that they should share in commitment fees, and that the guarantee fees should be higher than he had thought would be appropriate in the circumstances. He added that the principal reason for the desire of the Services for high guarantee fees was to enable them to accumulate as large a fund as possible from which to pay any losses that might be incurred in connection with their guarantees.

ASER

Chairman Eccles also reported that yesterday Colonel McKinney called Mr. Clayton to say that, if the Federal Reserve could see its way clear to agree to a maximum interest rate of 4-1/2 per cent instead of 4 per cent, Mr. Hinckley would concur in all the other proposals insisted upon by the Chairman, namely, (1) no sharing of the commitment fee, (2) the maximum commitment fee to be 1/4 instead of 3/8 per cent per annum, with an alternative maximum of a flat fee of not to exceed $50, and (3) the lower and simpler schedule of guarantee fees. While Colonel McKinney said that the Services would prefer not to make these concessions, he would undertake to clear the compromise program with them so as to assure that there would not be any disagreement. Mr. Clayton asked Colonel McKinney to call him back when he had cleared the matter with the Services and Colonel McKinney had reported later in the day that it had been so cleared. Chairman Eccles went on to say that in all the circumstances he felt that the Board should accept this compromise and that that would be his recommendation.

In the discussion which ensued, reference was made to the fact that loans made under the Regulation V procedure for war production involved a larger possibility of loss than loans made for the purpose of financing the claims of contractors in connection with the termination of war contracts, so that ordinarily the latter class of loans should carry a lower rate, but that, on the other hand, it was important

that the rate on termination loans be high enough so that the banks would be interested in making them. It was pointed out that if the maximum interest rate were 5 per cent with 25 per cent of the interest earned being payable to the guarantor as a guarantee fee for a 90 per cent guarantee, as had been suggested by the Services, the net rate to the bank would be 3.75 per cent whereas if the rate were 4-1/2 per cent with 20 per cent of the interest earned payable to the guarantor, as was now proposed, the net return to the bank would be 3.6 per cent, so that the net difference to the lending bank in the two rates would be only .15 per cent.

Reference was also made by Chairman Eccles to the responsibility of the Board for the determination of rates and fees in connection with termination loans, and it was stated that under the provisions of section 4 of the proposed revised Regulation V it was contemplated that the rates of interest, guarantee and commitment fees, and other charges would be prescribed by the Board with the concurrence of the Director of Contract Settlement. Chairman Eccles said that the Contract Settlement Act of 1944 placed the responsibility for policies and procedures in connection with the settlement of war contracts in the Director of Contract Settlement and that the Federal Reserve Banks were authorized to act as fiscal agents of the Services in facilitating the financing of contractors in connection with claims arising out

FRASER

of the termination of war contracts. The arrangement, he said, under which the Board prescribed the rates of interest and fees on termination loans was possible only because the Director of Contract Settlement was willing to give the responsibility to the Board, and he (Chairman Eccles) now felt that the Board should not be in a position of having its actions subject to veto by another agency in circumstances of this kind. He thought that it would have been better if the procedure had required that the rates of interest and fees be fixed by the Director of Contract Settlement after consultation with the Board, and it was his suggestion that, after the program now in contemplation had been approved and was in operation, the Board propose to Mr. Hinckley that the procedure be changed to provide that the rates of interest and fees be prescribed by the Director of Contract Settlement after consultation with the Board or by the Board after consultation with the Director of Contract Settlement.

After extended discussion it was agreed that the proposed schedules of fees and maximum rate of interest were a satisfactory solution. During the course of the discussion Chairman Eccles presented and there was read the following draft of letter to Mr. Hinckley:

ASER

8/31/44

"Under the provisions of section 4 of Regulation V of the Board of Governors, as amended in the form approved by you on August 8, 1944, the Board of Governors proposes to establish, subject to your concurrence, effective at the time the amended Regulation itself goes into effect, the following schedule of guarantee fees (charged by the guarantor) and commitment fees (charged by the financing institution) with respect to T loans:

GUARANTEE FEES
ON TERMINATION LOANS GUARANTEED PURSUANT
TO THE CONTRACT SETTLEMENT ACT OF 1944

Per cent of loan guaranteed	Guarantee Fee (Per cent of interest payable by borrower on guaranteed portion of loan)
80 or less	10
85	15
90	20
95	30
Over 95	50

MAXIMUM COMMITMENT FEE
THAT MAY BE CHARGED BORROWER BY FINANCING INSTITUTION
1/4 of 1 per cent per annum[1]
or
A flat fee of not to exceed $50.00[2]

"It is the intention of the Board to provide, as is the case with respect to V and VT loans, that no termination fee, service fee, or other fee of a similar character, except charges covering out-of-pocket expenses may be charged a borrower by a financing institution.

"The Board also proposes, with your concurrence, to fix a rate of four and one-half per cent per annum as the maximum interest rate on T loans.

1/ To be based on average daily unused balance of the maximum principal amount of the loan.

2/ Without regard to the amount or maturity of the commitment.

FRASER

"As you know, these schedules of fees and the maximum rate of interest have been discussed at great length with the Armed Services and the Maritime Commission and with your own staff. There has been substantial divergence of thought so that the foregoing proposals represent some concessions on the part of all. In general, as compared with the schedules relating to V and VT loans, the fees have been substantially lowered, the schedules simplified, the sharing of the guarantor in the commitment fee eliminated, and the maximum rate of interest lowered by one-half of one per cent. All of this should help to popularize the program and reflects the spirit of the Contract Settlement Act which recognizes the obligation of the Government to provide prompt and equitable interim financing to contractors pending final settlement of their claims.

"In order to achieve greater uniformity, it is proposed that the new schedules of guarantee and commitment fees and the maximum interest rate of four and one-half per cent be made applicable to guarantees of V and VT loans executed on the new forms which have been prepared by the Services and the Board of Governors and which it is contemplated will be made effective at the time the T program is put in operation.

"In the opinion of the Board of Governors, the foregoing proposals are calculated to further the objectives of the Contract Settlement Act and are both practical and equitable. We would appreciate advice as to whether you concur in them."

There was some question whether the application of the new schedule of fees and maximum interest rate to V and VT loans executed on the new forms had been specifically cleared with representatives of the Services, and it was understood that Mr. Clayton would discuss this point with them before the letter was sent.

Chairman Eccles suggested that if the letter were satisfactory to the members of the Board present the views of Messrs. McKee and Evans be ascertained by telephone and, if a majority of the members of the

FRASER

Board approved the letter, that it be sent to Mr. Hinckley.

Messrs. Ransom and Draper stated that the letter was satisfactory to them. Thereupon, Chairman Eccles' suggestion was approved unanimously.

Secretary's Note: On September 2, 1944, Mr. Carpenter called Messrs. McKee and Evans on the telephone to ascertain their views with respect to the schedule of fees and the maximum interest rate referred to in the proposed letter to Mr. Hinckley. After listening to a review of the developments which resulted in the compromise set forth in the letter, Mr. McKee stated that he was in favor of the proposed schedule of fees but that he thought it would be a mistake to reduce the maximum interest rate below 5 per cent for the reasons that (1) it was not certain that the possibilities of loss were not as great in connection with T loans as with V or VT loans, (2) while it was not expected that many loans would be made at the 5 per cent rate, there might be cases in which the investigation and supervision work done by a lending bank in connection with a loan would justify a 5 per cent rate, and (3) it was unwise at this time to raise the questions that might attend a reduction in the maximum rate. He added, however, that if the compromise rate of 4-1/2 per cent were the only thing possible in all the circumstances he would not object.

Mr. Evans stated that he was in favor of all of the proposals set forth in the letter to Mr. Hinckley.

A majority of the Board having approved these proposals, the letter was sent to Mr. Hinckley by messenger on the morning of September 2, 1944.

At this point, Messrs. Smead and Vest withdrew from the meeting, and the action stated with respect to each of the matters hereinafter referred to was then taken by the Board.

Memorandum of this date from Mr. Paulger, Director of the Division of Examinations, submitting the resignation of Miss Giovanna M. Mattare as a stenographer in that Division, to become effective as of the close of business on September 5, 1944, and recommending that the resignation be accepted as of that date.

The resignation was accepted as recommended.

Letter to Mr. McLarin, President of the Federal Reserve Bank of Atlanta, reading as follows:

"Receipt is acknowledged of your letter of August 23, 1944, regarding an inquiry which you have received from Mr. E. H. Sherry of the Home Improvement Company of Birmingham, Alabama regarding section 8(m) of Regulation W. The question is whether insulating board which is first nailed on the outside of a dwelling, following which an imitation brick roll type siding is nailed over the insulating board, is exempt under section 8(m)(2) which exempts any extension of credit to finance 'the installation of loose fill, blanket, or bat-type insulation or insulating board, within existing structures'.

"Virtually the same question was asked by Counsel for the Federal Reserve Bank of Richmond, and a copy of the Board's reply, dated August 12, 1942, is enclosed. As you will see, the Board gave the same answer as was given by representatives of your bank, that is, that the exemption was not applicable.

"Of collateral interest in this connection is the Board's letter of June 9, 1944, a copy of which is enclosed for your convenience."

Approved unanimously.

FRASER

Letter to Mr. Mangels, Vice President of the Federal Reserve Bank of San Francisco, reading as follows:

"This will acknowledge your letter of August 15, 1944, enclosing copies of correspondence with the Uintah State Bank, Vernal, Utah, relative to your report of examination of that bank as of June 5, 1944.

"We note also the comments of Mr. Siddoway, President of the bank, to the effect that the usefulness of Regulation W has already passed. We have received a number of comments of like nature particularly from bankers and others in the lending field, some of which say that it would be a good idea to abandon Regulation W quite promptly after the end of the European phase of the war. We have also received comments to the opposite effect and have noted some in the current writings of economists who have been writing about the problems with which we may be faced during the time we are changing over from a war economy to a peace economy. J. M. Clark, for example, in an article entitled, 'How Not to Reconvert', has recently made the following comment about this subject:

> 'There are similar chances to go wrong in the matter of credit controls. Restrictions on consumer credit, under Regulation W, are not very active at present; and this could easily lead to the conclusion that they are not needed any more. So it would be very easy to make the mistake of abandoning them, after which it might be next to impossible to restore them when the need arose -- as it inevitably would. Whether or not a general overall inflation occurs after the war, there is sure to be a market for consumer durables in which monetary demand is far in excess of the supply, for a considerable period.'

"We are always glad to be informed of opinions of Registrants and want to get as complete an understanding as possible of the reasons behind them."

Approved unanimously.

FRASER

8/31/44

Thereupon the meeting adjourned.

Assistant Secretary.

Approved:

Chairman.