A meeting of the Board of Governors of the Federal Reserve System was held in Washington on Thursday, May 3, 1945, at 3:00 p.m.

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

Mr. Morrill, Secretary
Mr. Carpenter, Assistant Secretary
Mr. Thurston, Assistant to the Chairman
Mr. Goldenweiser, Economic Adviser, Division of Research and Statistics
Mr. Parry, Director of the Division of Security Loans
Mr. Thomas, Director of the Division of Research and Statistics
Mr. Vest, General Attorney
Mr. Brown, Assistant Director of the Division of Security Loans

Chairman Eccles stated that since the Board of Governors last considered the question of increasing the margin requirements prescribed in Regulation T, Extension and Maintenance of Credit by Brokers, Dealers, and Members of National Securities Exchanges, and Regulation U, Loans by Banks for the Purpose of Purchasing or Carrying Stocks Registered on a National Securities Exchange, there had been no meeting of the Economic Stabilization Board until this morning. At that meeting consideration was given to a memorandum entitled "Speculative Capital Transactions in Corporate Stocks and in Urban and Farm Real Estate" which had been prepared by a special staff committee upon the request of Mr. Davis, Director of Economic Stabilization, at an earlier meeting of the Economic Stabilization Board. The summary of the findings and recommendations

contained in the memorandum was read by Chairman Eccles as follows, and Mr. Thomas stated that members of the special committee had previously discussed various parts of the program suggested in the memorandum with him and Mr. Parry:

> The major finding of this report is that the situation is threatening in all three areas, with the danger perhaps more acute in farm and urban real estate, less immediate in the stock market. The common problems, however, argue strongly for a frontal attack across-the-board; in particular, any tendency to single out one area (e.g., farm real estate) would properly be subject to attack as too narrow and too discriminatory. Within each area, selective action is advised, in order to secure the maximum positive results in curbing inflation with the minimum disturbance to the normal functioning of these markets.
>
> The specific recommendations conform to the pattern suggested by the Interdepartmental Tax Committee in its report of March 6, with a few additions. The recommendations include:
>
> (1) Strengthening of capital gains taxation, by
>
> (a) Extension to three years of the minimum holding period for computing long-term capital gains for the Federal income tax.
>
> (b) An increase in the present ceiling rate of 25 per cent on long-term capital gains.
>
> (2) Additional controls over terms of direct Government loans, Government-guaranteed loans and unguaranteed loans, through
>
> (a) Issuance of an Executive order and appropriate regulations setting minimum down payments and perhaps periods of amortization for urban and farm mortgage loans
>
> (b) Further increases in margin requirements on stocks.

(3) Tightening of controls over evictions by

(a) Increasing the period of notice required to six months.

(b) Requiring cash down payments of 33-1/3 per cent or more.

The recommendation to strengthen the taxation of capital gains is the only one which requires legislation and which applies uniformly in all three markets. The proposal to lengthen the present six-months holding period used in computing long-term capital gains, as the Interdepartmental Tax Committee states, will "rectify an overdose of leniency put into the 1942 law as an experiment." The additional suggestion for increasing the present ceiling of 25 per cent on taxation of long-term capital gains is designed to bring the rate on long-term capital gains more nearly into line with higher wartime rates on other income, and thus reduce this glaring loophole in the wartime tax structure. In addition, enactment of technical changes, one of which was formerly proposed by the Treasury, would be advisable to close certain other loopholes which now stimulate purchase of real estate for the purpose of tax avoidance. Because the proposed changes will require Congressional action, it is suggested that, if approved, they be submitted to the staff of the Joint Committee on Internal Revenue Taxation and the Treasury Department for elaboration of details.

Judging by the precedent of consumer credit regulation, the imposition of controls over farm and urban mortgage credit is within the wartime Executive powers conveyed by Section 5(b) of the Trading-With-The-Enemy Act (as amended by the First War Powers Act). It is, therefore, proposed that the President issue an Executive order vesting in the Director of Economic Stabilization (Board of Governors of the Federal Reserve System) the power to regulate the terms and conditions applying to all forms of mortgage credit. The details of the Executive order and the major features of the succeeding regulations should be worked out jointly with the Board of Governors, with the Department of Agriculture, and the National Housing Agency.

The proposed controls over evictions are within the present powers of the Price Administrator, since their

primary purpose is to prevent evasion of rent control. Since tightening of such regulations, however, will also help to restrain increases in housing values, a directive from the Director of Economic Stabilization would give additional support to the Price Administrator.

The final collapse of Germany will place new and serious pressures on the hold-the-line program. Even if higher capital values may be reasonably anticipated in the long run in some areas, rapid further appreciation during the war would be undesirable. Adoption and announcement of a program to curb inflation in the real estate and stock markets can provide a good occasion for the new President to reaffirm his determination to resist inflationary pressures and thus strengthen the backbone of the whole economic stabilization program.

Chairman Eccles made the further statement that no formal action was taken by the Economic Stabilization Board on the suggested program but that some of the members expressed approval of it, that Under Secretary of the Treasury Bell said that the Treasury would like to have an opportunity to consider the program from the standpoint of its possible effects on Treasury financing operations, that Mr. Purcell, Chairman of the Securities and Exchange Commission, and Mr. Wickard, Secretary of Agriculture, thought the program was satisfactory but preferred the capital gains tax as the best way to get at the problem, and that he (Chairman Eccles) had reviewed again the reasons why he thought the problem should be attacked through a tax on capital gains rather than through the medium of credit controls.

Chairman Eccles also said that he had a luncheon appointment with Mr. Davis tomorrow, at which time he expected to discuss the whole matter further, and that he would like to be in a position at that time

to tell Mr. Davis what action the Board was prepared to take with respect to an increase in margin requirements.

Chairman Eccles then read the portion of the memorandum above referred to which related particularly to further increases in margin requirements and which read in part as follows:

> At present levels the volume of stock market credit is probably not excessive. Any reduction, however, would help to restrain market increases by reducing the effective demand of margin traders. While there is much to be said for complete elimination of margin trading at the present stage in the market it would probably be preferable to increase margin requirements by gradual stages. When expansion in stock market credit coincides with increases in the level of the market, further increases in margin requirements would be desirable. When future increases are ordered, it may also be advisable to expand the coverage of the new requirements so that they not only apply to additions to new accounts, as at present, but also require proceeds of future sales to be used to bring undermargined accounts up to the new levels.

He stated that some of the members of the Economic Stabilization Board apparently favored action by the Board to put trading in registered securities on a cash basis and that he outlined the reasons why some of the members of the Board of Governors questioned the desirability of that action except as a part of a general program to combat inflation. There was further discussion, he said, of the suggestion that action should be taken by the Board to increase margin requirements as a necessary step which would be within existing statutory powers, before any further request was made of Congress for legislation to deal with the inflationary situation, and that some of the members of the Economic Stabilization Board felt that the taking of such action was highly

desirable. Chairman Eccles added that he had pointed out the necessity of being sure that any action taken by the Board would be in accordance with the program of the administration and that Messrs. Davis and Vinson indicated that if the Board should decide to take action they would be willing to clear the matter with the President.

There was a general discussion by the members of the Board of the situation in the securities markets and of the basis upon which action might be taken by the Board to increase margin requirements.

During the discussion, Mr. Draper suggested that Chairman Eccles advise Mr. Davis when he met with him tomorrow that the Board of Governors was prepared to increase from 50 per cent to 70 per cent the margin requirements now prescribed in Regulations T and U upon being advised that such action would be in harmony with the stabilization program of the Government. Mr. Draper made it clear that his suggestion contemplated action which would include a requirement not now in the Regulations that when there was a sale of securities from an undermargined account the proceeds of the sale would be used to the extent necessary to margin the remaining securities in the account on a 70 per cent basis.

There was a discussion of the possible significance of an increase in margin requirements to 70 per cent, and Mr. Parry stated that from the standpoint of the public the 70 per cent figure would be significant for three reasons: (1) it would raise margin requirements to a higher point than at any time in the past; (2) it would be the largest

increase ever made by the Board; and (3) the fact that the last increase was 10 per cent and the proposed increase would be 20 per cent would be a possible indication that the next increase would be to 100 per cent.

Mr. McKee inquired whether better control of the market could be obtained by increasing margin requirements by 10 per cent, accompanied by action by the New York Stock Exchange to require a 100 per cent margin on all securities selling at $20 or less.

Chairman Eccles stated that this suggestion was discussed at the meeting of the Economic Stabilization Board this morning and that Mr. Purcell had expressed the opinion that such action by the New York Stock Exchange would not have any lasting effect and would only serve to drive trading into securities selling at prices higher than $20 per share.

During a discussion of this point Mr. Thurston suggested that, as margin requirements were raised the necessity for legislation to tax speculative profits increased, so as to prevent the accusation that the policy of Government was merely closing the market to anyone who was unable to buy and sell for cash.

Mr. McKee stated that he would not favor any increase in margin requirements at this time because he thought that the program of the Government for combating inflation was not complete, that the amount of credit being used at the present time for the purpose of purchasing or carrying securities was not large enough to justify action by the

Board, and that, therefore, action to increase requirements as part of such a program would not be in harmony with the statute from which the Board's authority was derived.

Mr. Evans stated that he favored Mr. Draper's suggestion.

Mr. Eccles said that he had preferred for some time an increase in margin requirements to 100 per cent, for the reason that he did not think that there should be any use of credit during the war period for the purpose of purchasing or carrying securities, but that he would be willing to approve an increase to 70 per cent if that were the wish of the other members of the Board.

Mr. Szymczak expressed the thought that an increase in margin requirements to 70 per cent might be interpreted in the market as a signal for greatly increased market activity, that therefore it might be better to increase requirements to 100 per cent in a single step, but that, if it were the wish of the other members to approve an increase to 70 per cent, he would concur in that action.

Mr. Ransom said he would favor an increase first to 70 per cent and then if necessary to 100 per cent, for the reason that such action probably would be more effective than an increase to 100 per cent in one step.

There was a discussion of the question whether it would be better from the standpoint of the clerical work involved in calculating margins if the increase were to 66-2/3 per cent instead of 70 per cent, and Mr. Parry stated that 65 or 70 per cent would be easier to calculate

than 66-2/3 per cent.

At the conclusion of the discussion Chairman Eccles stated that it appeared that a majority of the Board would favor Mr. Draper's suggestion, and that when he met with Mr. Davis tomorrow he would advise him that the Board was prepared to increase from 50 per cent to 70 per cent the margin requirements now prescribed in Regulations T and U upon being advised that such action would be in harmony with the stabilization program of the Government, and that the Board's action would include a requirement not now in the Regulations that when there was a sale of securities from an undermargined account the proceeds of the sale would be used to the extent necessary to margin the remaining securities in the account on a 70 per cent basis.

At this point Mr. McKee left the meeting.

Mr. Ransom suggested that the members of the Board present express their views on the recommendation contained in the memorandum referred to above with respect to strengthening the capital gains tax by (a) an extension to three years of the minimum holding period for computing long-term capital gains, and (b) an increase in the present ceiling rate of 25 per cent on long-term capital gains. All of the members present expressed agreement that the enactment of additional legislation for this purpose would be highly desirable and that Chairman Eccles might so advise Mr. Davis when he met with him tomorrow.

In connection with the suggestion that the President issue an

executive order vesting in the Director of Economic Stabilization or the Board of Governors of the Federal Reserve System power to regulate the terms and conditions applying to all forms of real estate mortgage credit, Chairman Eccles stated that at the meeting of the Economic Stabilization Board he had expressed vigorously the opinion that this was not the most effective way to handle the problem, that the Board had given considerable study to the form of an executive order and the regulations that might be issued under it and that it involved problems that would be difficult to surmount from an administrative standpoint.

There was a discussion of the question whether the Board should be in the position of suggesting that, if such an executive order was to be issued the authority to administer the credit aspects of the order be placed in another agency, since that would only serve to add to the confusion in the field of credit administration and conflicting jurisdictions of Government agencies. It was the consensus of the members present that, if the order was to be issued, the Board of Governors should be given the responsibility for its administration.

Chairman Eccles raised the question whether the executive order should be issued to the Director of Economic Stabilization with authority to delegate the administration of the order to the Board of Governors or whether it should be issued directly to the Board. The

suggestion was made that because of the responsibilities of the Farm Credit Administration and the National Housing Agency and, possibly, other Government agencies in the real estate credit field, it might be well for the order to be issued to the Director of Economic Stabilization in the first instance, but placing the actual administration of the order in the Board of Governors, and authorizing the Director to require the cooperation of the other Government agencies in carrying out the provisions of the order.

This suggestion was acceptable to all of the members of the Board present and it was understood that when Chairman Eccles met with Mr. Davis tomorrow he would make substantially the following statement:

> The Board does not think that an executive order of the kind contemplated is the way to meet the problem; that such an order would deal with effects rather than causes and, therefore, would not be very effective; that there is a question, which it would be desirable to discuss with appropriate members of Congress, whether an executive order should be issued for a purpose of this kind which might well be the subject of legislation by Congress; but that if it is decided to issue the order it is felt that its administration should be placed in the Board of Governors as the agency primarily concerned with credit control and that the order should be so framed as to place the authority in the Director of Economic Stabilization, should name the Board of Governors as the administrative agency to carry out the purposes of the order, and should authorize the Director of Economic Stabilization to require cooperation by other interested Government agencies in making effective the policies determined under the order. If the decision should be made to issue the order, the Board, drawing on its experience in the field of consumer credit administration, would like to have an opportunity to draft an executive order and an outline of the regulations that might be issued thereunder so that there would be some assurance

that the order and the regulations would be practicable from an administrative standpoint.

Mr. Goldenweiser stated that he had received a request from Senator Millikin of Colorado that he be furnished with the amounts of gold held by the Federal Reserve Bank of New York under earmark for various foreign countries and that he had told the Senator that it had been the long-standing policy of central banks not to give out such information as it would tend to encourage withdrawal of the gold for shipment abroad or its conversion into dollar balances to be held in commercial banks. The Senator was not satisfied with this answer, Mr. Goldenweiser said, and asked that his request be submitted to the Board.

> It was agreed that Mr. Goldenweiser should advise the Senator that the relationship between the Federal Reserve Banks and their depositors was confidential in the same sense that the relationship between commercial banks and their customers was confidential and that it was not the policy of the Board to give out the information requested for the reasons that Mr. Goldenweiser had stated. It was also understood that Mr. Goldenweiser would point out that the total amount of earmarked gold held by the Federal Reserve Banks and the total amounts of gold reserves held by the respective foreign countries were published in the Federal Reserve Bulletin.

Mr. Vest stated that Messrs. Agnew and Fayerweather had challenged in the United States District Court for the District of Columbia the action taken by the Board removing them as directors of the Paterson

National Bank, Paterson, New Jersey, and that it was proposed to file a motion tomorrow to dismiss the complaint on the grounds, (1) that the Court was without jurisdiction to entertain a suit against the Board which is an instrumentality of the United States, (2) that the Court is without jurisdiction to issue a writ of certiorari for the purpose outlined in the bill of complaint, and (3) the complaint fails to state any claim upon which relief can be granted.

At this point Messrs. Goldenweiser, Parry, Thomas, Vest, and Brown withdrew from the meeting.

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 May 2, 1945, were approved unanimously.

Memorandum dated April 30, 1945, from Mr. Paulger, Director of the Division of Examinations, submitting the resignation of L. E. Skees as a Federal Reserve Examiner in that Division, effective as of the close of business on April 30, 1945, and recommending that the resignation be accepted as of that date and that appropriate payment be made for the accumulated annual leave remaining to his credit at that time.

The resignation was accepted as recommended.

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

"The Board of Governors approves the cancellation of pages numbered 1, 2, and 3 of the personnel classification plan of the Savannah Agency as requested in your letter of April 30, 1945."

Approved unanimously.

Letter to Mr. Meyer, Assistant Cashier of the Federal Reserve Bank of Chicago, reading as follows:

"The Board of Governors approves the change in the personnel classification plan of the Detroit Branch, involving an increase in the maximum annual salary for the position of Officer's Secretary, as submitted with your letter of April 25, 1945."

Approved unanimously, together with a letter to the Wage Stabilization Division, National War Labor Board, transmitting a certificate of the Federal Reserve Bank of Chicago with respect to the salary increase at the Detroit Branch.

Letter to Mr. Flanders, President of the Federal Reserve Bank of Boston, reading as follows:

"This refers to your letter of April 13, 1945, written in response to our letter of March 29, regarding the financing of small business enterprises in the reconversion period.

"It is assumed that the questions raised in your letter relate to the position the Federal Reserve System should take in considering applications for guaranteed loans under the proposed Wagner-Spence bill (S. 511 and H.R. 591), should it become law. In this connection, we should like to point out that the present Section 13b was enacted in 1934 to take care of a situation existing during a severe depression. As legislation designed to combat deflation and aid in business recovery at a time when banks were seeking liquidation of loans, Section 13b served a useful purpose. The situation now is entirely different, however, and the present Section 13b should be repealed.

"The next problem we will shortly be faced with is how best to assist a substantial number of our smaller and inadequately financed business enterprises to make the transition from war- to peace-time operations smoothly. It is generally taken for granted that some form of Government participation in the extension of credit to business is essential and inevitable in the reconversion and postwar period. We believe the Wagner-Spence bill would meet the need and at the same time encourage and preserve private enterprise in the field of banking. During the war the goal of Government participation in financing industry was to obtain vast quantities of war materials quickly. In a similar sense the goal during the early postwar period is to assure prompt reconversion to civilian production.

"Commercial banks have made wide use of V loans in providing financing for war production. Well over half of all the war production credit made available by banks was in guaranteed loans. The banks are now also taking advantage of the T loan. These V and T loans, however, will mature and must be paid when war production is over and the Government has settled with business for materials delivered and for claims resulting from cancelled contracts. This will be the precise time when the program of full employment could easily be jeopardized through a failure to provide needed credit to all businesses having reasonable prospects of success under peace-time conditions.

"Today many enterprises engaged in war production are operating with the aid of Government credit supplied directly or indirectly through advance payments on war contracts, tax accruals, and V and T loans. A considerable portion of this credit extended for war purposes must be replaced with credit extended for reconversion and civilian production. War industries as well as enterprises which have been following their peace-time lines of endeavor will need to modernize their plant and equipment, and in many cases sales organizations will have to be rebuilt and civilian markets re-established. The disposal of surplus war inventories, machine tools, etc., no longer needed for war production purposes will present difficult problems. Many plants in which these machines and inventories are now located will want to take them over directly from the Government upon termination of war contracts. Arrangements for this should be made now with

"the proper procurement agencies, not after contracts are cancelled. The availability of adequate credit may be a vital matter in the negotiations. The reconversion period will be beset with many difficulties, but the availability of adequate credit to all worthy enterprises should not be one of them.

"The Wagner-Spence bill authorizes the Federal Reserve Banks to guarantee loans up to 90 per cent of their face value. If a commercial bank or other private lending institution is not willing to take as much as 10 per cent of the risk in a loan, it is doubtful that the loan should be made. Should the Wagner-Spence bill become law, it would be our thought that the regulations to be issued by the Board should be broad and drawn in such a way as to encourage the Federal Reserve Banks to follow a liberal practice in guaranteeing loans. It should not be necessary for the Federal Reserve Banks to analyze the credit position of prospective borrowers to the same extent they have under the present Section 13b, but rather that, in the absence of unusual conditions indicating a different course, they should adopt approximately the same practice that has been followed in guaranteeing war loans under Regulation V. In other words the Federal Reserve Banks should, in general, in the interest of reconversion and civilian production, be willing to guarantee any small and medium size loans on which our well-managed commercial banks are willing to assume 10 per cent or more of the risk, provided, of course, that the loans are made in good faith and not for the purpose of bailing out old loans. Under such a program it would be expected that a large percentage of the loans would carry the maximum 90 per cent guarantee, but the inducement would exist, through the schedule of guarantee fees, for the banks to assume as large a percentage of the risk as circumstances would justify. In this process we would hope, of course, that substantial losses would not be suffered by the Federal Reserve Banks, but the success of such a program should not be judged by the question of profit and loss alone.

"Recently Chairman Eccles was asked for a memorandum summarizing his views with respect to the Wagner-Spence bill by Mr. O. Max Gardner, Chairman, Advisory Board, Office of War Mobilization and Reconversion. A copy of Mr. Eccles' letter to Mr. Gardner, dated March 14, 1945, is enclosed for your information."

Approved unanimously.

Letter to Mr. Leach, President of the Federal Reserve Bank of Richmond, reading as follows:

"The Board has noted with interest the explanation in your letter of April 23 in regard to the proposal for a park in Charlotte, North Carolina, as a memorial to the residents of that city who have served in the present war.

"As you point out, while such a park might be a suitable memorial to men and women who have served their country during the war and might also be of great use and benefit to the people of Charlotte, it is obvious that those who have served in the armed forces will derive no peculiar benefit from the park, and that it is not closely related to the conduct of the affairs of the Bank. Moreover, there may be numerous other civic projects not only in your district but throughout the United States which might be based upon similar considerations.

"Consequently, the Board feels, as you evidently do, that it would not be warranted in authorizing a contribution from the funds of your Bank for this purpose. In this connection, the Board has asked me to express its appreciation of the analysis which you have made of the problem and the expression of your opinion concerning it."

Approved unanimously.

Letter to Mr. Lichtenstein, Secretary of the Federal Advisory Council, reading as follows:

"This letter is in response to yours of April 11, 1945, asking for a list of subjects which the Board wishes the Council to discuss at its forthcoming meeting in Washington on May 13-14, 1945. The Board would appreciate the views of the Council on the following matters:

1. From time to time in the past reference has been made to the practice adopted by certain large depositors of asking the depositary banks for more detailed information regarding the condition of the banks than is shown in their regularly published reports of condition. To what extent is this practice still being followed and what further action should be taken by the bank supervisory agencies in connection with it?

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"2. Upon recommendation of the American Bankers Association banks in various sections of the country have organized so-called 'credit pools'. What is the opinion of the Council as to the progress being made by these pools?

3. There has been considerable discussion of the inflationary developments in farm and urban real estate and other capital assets. How should these developments be dealt with?

"The usual arrangements are being made for luncheon for the Council on Monday, May 14. If we can be of any assistance to you or the members of the Council before the meeting or while the Council is here please let us know."

Approved unanimously.

Thereupon the meeting adjourned.

Chester Morrill
Secretary.

Approved: M S Eccles
Chairman.