

Minutes of actions taken by the Board of Governors of the Federal Reserve System on Wednesday, December 17, 1947. The Board met in the Board Room at 10:35 a.m.

PRESENT: Mr. Eccles, Chairman
Mr. Szymczak
Mr. Draper
Mr. Evans
Mr. Vardaman
Mr. Clayton

Mr. Carpenter, Secretary
Mr. Sherman, Assistant Secretary
Mr. Morrill, Special Adviser
Mr. Smead, Director of the Division of Bank Operations
Mr. Thomas, Director of the Division of Research and Statistics
Mr. Vest, General Counsel
Mr. Nelson, Director of the Division of Personnel Administration
Mr. Horbett, Assistant Director of the Division of Bank Operations
Mr. Townsend, Assistant General Counsel
Mr. Hackley, Assistant Counsel

Mr. Clayton stated that, in accordance with the action taken by the Board on November 21, 1947, a hearing had been held in the Board's offices on December 10 with respect to the proposed change in reserve city designations as announced by the Board in the Federal Register on October 24, 1947 in accordance with the action taken at the meeting of the Board on October 21, 1947, that a number of banks had been represented at the hearing by officers of banks in cities that would be affected and by members of Congress, and that he and Mr. Szymczak had been impressed

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by the value attached by the banks to the reserve city designation which they regarded as permanent and by their feeling, which was contrary to the view of the Board, that the action discontinuing the designation of certain cities would be inflationary. He went on to say that, after reviewing the proposed formula in the light of the discussion at the hearing on December 10, the committee recommended that the formula be put into effect as published in the Federal Register with the addition of a provision that the Board would also designate as a reserve city any city now classified as a reserve city, which was not covered by the formula, if a written request for the continuance of such a city as a reserve city was received from every member bank which had its head office or a branch in such city.

Mr. Szymczak stated that he agreed with the recommendation as presented by Mr. Clayton, that he would also recommend (1) that the effective date of the Board's action be March 1, 1948, and (2) that the action provide that, with respect to the cities which did not fall within the formula as published in the Federal Register, their reserve city status would be continued only during a period which would enable the Board to present the matter to Congress and Congress would have an opportunity to consider the entire question, at the end of which time if no action were taken by

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the Congress the reserve city status of such cities would automatically terminate.

Mr. Vardaman stated that he was opposed to any procedure which would let the decision of the banks in a particular city determine whether that city should be designated as a reserve city. He felt that the Board had responsibility for designating reserve cities and that its actions in that connection should leave no discretion with the member banks involved. He said he would prefer to take the position that at the request of a single member bank in a city, or of a bona fide business group, the Board would hold a hearing to determine the action to be taken. He also felt that the adoption of the arrangement proposed by Messrs. Szymczak and Clayton would permit a single bank to demand benefits from other banks in return for its request that the designation of the city be continued and that such a result was an undesirable one. He added that, however, if a majority of the Board felt that the additional provision recommended by Messrs. Szymczak and Clayton should be approved he would go along with that decision.

The other members of the Board were of the opinion that essentially the procedure proposed by Mr. Vardaman with respect to a hearing was carried out in the hearing held on December 10, 1947, and that, since the designation of a city as a reserve city

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would require member banks in that city to carry higher reserves, the designation of a city which did not come within the formula as published in the Federal Register should not be continued in the absence of requests from all member banks in the city.

Chairman Eccles asked if the Legal Division now saw any objection to an arrangement which would permit a city which did not come within the formula to continue as a reserve city if all member banks in the city requested that that be done.

Mr. Vest stated that such a provision had been suggested early in the discussions with the Board and that he saw no legal objection to such an arrangement with respect to cities which were already classified as reserve cities. He also said that if the Board should agree to consider a request by an individual bank to continue the designation of a reserve city, it would still be faced with the problem of deciding what action to take when the opinion was not a unanimous one on the part of all member banks, and that the application of some standard in making such decisions would be necessary if the existing situation, in which decisions had been made without a definite standard, was to be changed.

Following a discussion of Mr. Vardaman's position and of possible alternative actions available to the Board, Chairman

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Eccles suggested that the recommendations of Messrs. Szymczak and Clayton be adopted except that the continuation of reserve cities which did not come within the formula as published in the Federal Register should not be made contingent upon the adoption of legislation by Congress.

Question was raised as to what the situation would be if, after a city was continued as a reserve city upon the unanimous request of all member banks in the city, one of the banks changed its mind and asked that the designation be terminated. It was stated that the formula as published in the Federal Register did not specifically provide for changes in the designations but it was understood that the Board would review the situation every two or three years.

There was agreement that provision should be made in the action of the Board for an automatic reapplication of the standard at the end of each three-year period based upon official reports of condition in the two-year period ending on June 30 of the year preceding such third year. This would mean that any city which as of March 1, 1948, was designated as a reserve city would continue as such for a period of three years and that if a designation were terminated on March 1, 1948, the termination would be permanent unless the city at the beginning of another three-year

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period came within the formula as published in the Federal Register.

Mr. Szymczak said that the System Research Advisory Committee had been requested to prepare for consideration by the Board a recommendation as to desirable changes to be made in the law with respect to the basis for computing member banks' reserves and that it would be his suggestion that, having the possibility of such changes in mind, the Board's action provide for the termination at the end of three years of the designation of any cities which, at the request of all member banks located in such cities, would now be continued as reserve cities unless action were taken by Congress in the interim to provide otherwise.

The other members of the Board agreed that the System Research Advisory Committee should present as promptly as possible its recommendations with respect to desirable changes in the law but questioned the desirability of making the continuation of reserve cities contingent upon action by the Congress.

At the conclusion of the discussion Messrs. Szymczak and Clayton were requested to draft and submit to the Board for further consideration a statement of the standard to be adopted by the Board for the classification of reserve cities and to incorporate therein provisions which would (1) continue the designation as a reserve city of each city which did not come within the formula as published in the Federal Register if all member banks in that city requested such continuation, and (2) automatically reapply the standard at the end of each three-year period from March 1, 1948.

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Mr. Evans stated that further consideration had been given to the appointment of a Class C director of the Federal Reserve Bank of Cleveland, for the three-year term beginning January 1, 1948, and that the Personnel Committee recommended that Mr. A. Z. Baker, President, The Cleveland Union Stock Yards Company, Cleveland, whose term will expire at the end of December, be reappointed for a three-year term beginning January 1, 1948, with the understanding that the Personnel Committee would continue to look for a man to appoint as a Class C director when the next vacancy occurred who could succeed Mr. Klages as Deputy Chairman in 1949 and Mr. Brainard as Chairman in 1950 when their terms expired. The principal reason for the recommendation was that, while Mr. Baker had not been regular in his attendance at meetings, he was a good director and because of the number of other changes in the Cleveland board, it was believed that his service should be continued for another term.

There was a discussion of the Committee's recommendation and it was agreed that if possible it would be desirable to appoint the possible successor to Messrs. Klages and Brainard this year so that he would have had a year's service before appointment as Deputy Chairman, and that the Personnel Committee would undertake to find such a man.

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Mr. Evans then stated that the Personnel Committee recommended the appointment of Mr. Mercer Brugler, President of The Pfaudler Company, Rochester, New York, as a director of the Buffalo Branch for the three-year term beginning January 1, 1948. He stated that Mr. Brugler was recommended by Deputy Chairman Myers of the Federal Reserve Bank of New York, that Mr. Folsom, presently a director of the Buffalo Branch, also recommended Mr. Brugler highly, and that he appeared to be a man interested in public affairs who would contribute substantially to the Buffalo Branch. He added that Mr. Brugler is a trustee of the Rochester Savings Bank, and that the appointment was recommended on the condition that Mr. Brugler give up that position.

It was voted unanimously to ask Mr. Myers by wire to ascertain whether Mr. Brugler would accept the appointment if tendered with the understanding that it would be necessary for him to resign his present position as a director of a mutual savings bank.

At this point all of the members of the staff with the exception of Messrs. Carpenter, Morrill, and Thomas withdrew from the meeting.

There was a further discussion of the appointment of a Class C director at the Federal Reserve Bank of Cleveland

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for the three-year term beginning January 1, 1948, and it was suggested that consideration be given to Mr. Charles P. Taft, lawyer, of Cincinnati, Ohio. Mr. Taft was favorably known to some of the members of the Board and his appointment was discussed in the light of the suggestion that if he were appointed he could serve during 1948 as a Class C director and could be appointed Deputy Chairman for the year 1949 to succeed Mr. Klages and designated as Chairman for the year 1950 to succeed Mr. Brainard.

During the discussion Mr. Szymczak expressed the view that it would be preferable to select as Chairman of a Federal Reserve Bank someone who lived in the city in which the Bank was located.

It was voted unanimously to ask Mr. Brainard by wire to ascertain from Mr. Taft if he would accept the appointment if tendered, and to make the appointment if he would accept.

Chairman Eccles referred to the discussion when the Presidents were in Washington at the time of the meetings of the Federal Open Market Committee and the Presidents Conference on December 8 and 9, 1947, when it was suggested that action to increase the discount rates in effect at the Federal Reserve Banks might be taken by the Banks in time for approval by the

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Board on Friday, December 19, for announcement after the market closed to become effective on Monday, December 22, 1947. The Chairman said that it had been expected that Mr. Sproul would come to Washington today for the discussions with the Treasury as mentioned at the meeting of the Federal Open Market Committee on December 9 with respect to the program to be followed in supporting the Government securities market, but that Mr. Sproul was ill and could not come.

Chairman Eccles also said that he had discussed the question of action on the discount rate with Mr. Sproul as President of the Federal Reserve Bank of New York and that it was felt that it would be preferable to defer action on an increase in rates until after the first of the year since nothing was to be gained by taking action just at this time and it would be undesirable to inject into the market the additional element of a change in the discount rate just at the time when transition was being made to a lower point at which the Government security market would be supported. In that connection, he outlined the program for support of the Government securities market which he and Mr. Sproul proposed to present to the members of the executive committee of the Federal Open Market Committee, and suggested that until that program was put into effect no action

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be taken with respect to increasing the discount rates at the Federal Reserve Banks. It was expected, Chairman Eccles added, that the board of directors of the Federal Reserve Bank of New York would meet on January 8 at which time action could be taken, if it was then thought to be desirable, to increase the discount rate. He made the further statement that if the members of the Board agreed with such an arrangement the Federal Reserve Banks should be advised by wire of the Board's views.

The other members of the Board expressed agreement with the arrangement outlined by Chairman Eccles and the following telegram to the Presidents of the Federal Reserve Banks was approved unanimously:

"While Presidents were in Washington recently there was discussion of the timing of an increase in the discount rates in effect at the Federal Reserve Banks, it being suggested that action might be taken by the Banks in time for approval by the Board on Friday, December 19, for announcement after the market closes to become effective on Monday, December 22. Since that time there has been further discussion of the matter and Board suggests it would be better if action were deferred until sometime in January. Board will communicate with you again."

At this point Mr. Thomas withdrew and the action stated with respect to each of the matters hereinafter set forth was taken by the Board:

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the Federal Reserve System on December 16, 1947, were approved unanimously.

Memorandum dated December 16, 1947, from Mr. Bethea, Director of the Division of Administrative Services, recommending that the resignation of Ralph L. Faust, a guard in that Division, be accepted to be effective, in accordance with his request, at the close of business December 26, 1947, with the understanding that a lump sum payment would be made for annual leave remaining to his credit as of that date.

Approved unanimously.

Letter to the board of directors of the "State Bank of Morton", Morton, Washington, 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 San Francisco:

- "4. Such bank shall increase the number of its directors to not less than five, the minimum number required in the case of all member banks under the provisions of Section 31 of the Banking Act of 1933 as amended."

Approved unanimously, together with a letter to Mr. Earhart, President of the Federal Reserve Bank of San Francisco, reading as follows:

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"The Board of Governors of the Federal Reserve System approves the application of the State Bank of Morton, Morton, Washington, 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 Supervisor of Banking for the State of Washington, for his information.

"In connection with condition of membership numbered 4, it has been noted that the bank has already made plans for the appointment of an additional director, contingent upon advice of favorable action on its application for membership. With the understanding that the required action will be taken within a reasonable time, the Board will not object to the admission of the bank to membership with only four directors.

"With respect to the suggested special condition of membership dealing with the bank's securities account, attention is called to the ruling of the Board contained in F.R.L.S. #7005, wherein the Board held that the provisions of section 5136 R. S. are not applicable to securities acquired by a bank before becoming a member of the Federal Reserve System and stated that it was not the general practice of the Board to require as a condition of membership that banks bring their securities accounts into conformity with section 5136 and the regulations issued thereunder. Accordingly, the special condition suggested by the Reserve Bank in regard to the applicant's investments is not being prescribed.

"If the examiner's remarks on page 2 of the report have been interpreted to mean that the bank should dispose of the 'excess investments' upon becoming a member bank, it is suggested that any incorrect impression should be clarified."

Letter prepared for Chairman Eccles' signature to the Honorable Edith Nourse Rogers, House of Representatives, reading as follows:

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"This is in reply to your letter of December 4, 1947, asking for our comments and recommendations regarding H. R. 4488, a bill to amend the Servicemen's Readjustment Act of 1944, as amended.

"The bill would authorize the Administrator of Veterans' Affairs to provide for the incorporation and supervision of 'veterans' homestead associations', which would be organized by veterans and would operate on a nonprofit basis to purchase and construct housing for veterans and make loans to veterans to purchase housing.

"Working capital for the associations would be provided initially by the Administrator, who would lend money to them at one-half of one per cent per annum. For this purpose the bill would authorize, in addition to such sums as may be necessary for his administrative functions, an appropriation of \$100,000,000 which would constitute a revolving fund.

"The Federal Works Administrator would be authorized to make grants covering one-half of the cost of streets, water works, sewers, schools and other facilities in connection with housing under the bill, for which purpose an appropriation of \$200,000,000 would be authorized.

"The associations would be authorized to issue bonds, in an amount equal to \$10,000 for each unit of housing constructed, acquired or financed by them, to the aggregate extent of \$2,000,000,000. Such bonds would be guaranteed as to principal and interest by the United States, and the interest would be exempt from Federal taxation. In addition, the net earnings of any association would be exempt from Federal, State and local taxation.

"The Administrator of Veterans' Affairs as fiscal agent for the associations would handle all matters connected with the issuance and sale of bonds.

"While we feel that the encouragement of associations financed in a sound manner might be of real help in achieving improved housing conditions, the Board believes that this bill should not be enacted in the present situation. One of the most inflationary factors at this time is excessively easy mortgage credit for housing. More than half of the current unprecendented volume of mortgage lendings is sponsored by the

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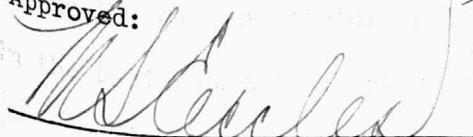
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"Federal Government under legislation enacted by Congress and this bill would add to the already generous provisions for mortgage credit. The Government must therefore assume much of the responsibility for any adverse effects of this type of lending under which sellers and builders of houses are enabled to make exorbitant profits, and families of moderate and low income are encouraged to assume mortgage debt beyond their ability to pay when the present inflationary period is over. In this connection, your attention is invited to my statement on housing finance before the Joint Committee on the Economic Report on November 25, 1947, of which a copy is attached.

"While it seems unnecessary to enter extensively upon a discussion of other aspects of the bill, we feel that, aside from the substantial additional appropriation of Government funds proposed for housing purposes without reimbursement, it provides for a loan rate for working capital purposes which is substantially below the cost of money to the Government, and for tax exemption which is not in harmony with governmental policy, particularly as expressed in the Act of February 19, 1941, of withdrawing tax exemption from all obligations issued after March 28, 1942 by the United States or any agency or instrumentality thereof. Moreover, it is not consistent with the heavy responsibilities of the Treasury for the management of the existing large public debt to place elsewhere in the Government the issuance and sale of the bonds which would be authorized by this bill."

Approved unanimously.

Approved:


Chairman.


Secretary.