

Minutes of actions taken by the Board of Governors of the Federal Reserve System on Wednesday, May 19, 1948.

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

Mr. Carpenter, Secretary
 Mr. Sherman, Assistant Secretary
 Mr. Morrill, Special Adviser
 Mr. Thurston, Assistant to the Board

Minutes of actions taken by the Board of Governors of the Federal Reserve System on May 18, 1948, were approved unanimously.

Memorandum dated May 18, 1948, from Mr. Leonard, Director of the Division of Examinations, recommending that the resignation of Leonard P. Eager, Jr., an Assistant Federal Reserve Examiner in that Division, be accepted to be effective, in accordance with his request, at the close of business June 4, 1948, 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 Mr. Dearmont, Federal Reserve Agent of the Federal Reserve Bank of St. Louis, reading as follows:

"In accordance with the request contained in your letter of May 12, 1948, the Board of Governors approves, effective June 1, 1948, the payment of salary to Mr. Edward A. Zehner, Alternate Assistant Federal Reserve Agent, at the rate of \$3,000 per annum."

Approved unanimously.

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Letter to the organizers of the "Peoples State Bank", Artesia, New Mexico, 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 Dallas:

- "4. At the time of admission to membership, such bank shall have a paid-up and unimpaired capital stock of not less than \$100,000 and other capital funds of not less than \$100,000."

The letter also contained the following special comments:

"Acceptance of the conditions of membership contained in this letter should be evidenced by a resolution adopted by the board of directors after the bank's charter has been issued. The board of directors should also adopt, at the same time, a resolution ratifying the action which has been taken in the bank's behalf in making application for membership in the Federal Reserve System. A certified copy of each resolution, together with advice of compliance with the condition to be complied with prior to admission to membership, should be transmitted to the Federal Reserve Bank. Arrangements will thereupon be made to accept payment for an appropriate amount of Federal Reserve Bank stock, to accept the deposit of the required reserve balance, and to issue the appropriate amount of Federal Reserve Bank stock to the bank.

"The time within which admission to membership in the Federal Reserve System in the manner described may be accomplished is limited to 4 months from the date of this letter, unless the bank applies to the Board and obtains an extension of time. When the Board is advised that all of the requirements have been complied

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"with and that the appropriate amount of Federal Reserve Bank stock has been issued to the bank, the Board will forward to the bank a formal certificate of membership in the Federal Reserve System."

Approved unanimously, for transmission through the Federal Reserve Bank of Dallas.

Letter to the Honorable O. C. Fisher, House of Representatives, reading as follows:

"This refers to your letter of May 8, 1948, addressed to Chairman McCabe, inquiring whether a certain bank purchase of notes from Fruehauf Trailer Company in 1945 complied with this Board's Regulation U, which relates to security loans by banks. This question was raised by Mr. and Mrs. Hirschie Johnson, who are residents of the district you represent in Texas.

"Transactions of the general type reported by Mr. and Mrs. Johnson have entailed administrative problems for the Board in the past, and we are glad to have this opportunity to outline our views on the status of such transactions under the regulation.

"As we understand the case presented, a bank on December 14, 1945, purchased promissory notes from Fruehauf Trailer Company which had been executed by certain of the company's directors and officers and delivered to the company in payment for shares of its authorized but unissued common stock which they had purchased on September 27, 1945. Each note was secured by pledge of the stock for which it was paid, and the stock was listed on the New York Stock Exchange. The question is asked whether the note purchase complied with Regulation U in view of the provision then effective that prohibited a bank from making any loan secured by stock for the purpose of purchasing or carrying a registered stock, such as the Fruehauf issue, in an amount greater than 25 per cent of the value of the collateral.

"A specific ruling as to whether Regulation U was violated in this case would depend on all of the facts involved. In particular, the answer to the question

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"would be influenced by whether there was any connection between the original loans made by the company and the subsequent bank purchase of the notes, and whether the company sold the notes to obtain funds for purchasing or carrying securities rather than for manufacturing purposes. A violation would be indicated, for instance, if there had been an agreement or understanding on the part of the bank, at the time the loans were originally made, that the bank would take them over at some future time. The original loans by the company, standing by themselves, naturally were exempt from a regulation which applies only to specified loans by banks. In this connection, it is of interest that the Securities Exchange Act of 1934, which authorized these regulations, specifically exempted 'a loan made by a person not in the ordinary course of his business.'

"Assuming that the bank purchase of the notes in the case presented was not in any way a subterfuge for the making of a prohibited loan, it appears to be in compliance with the regulation. If this assumption is true, the purchase of the notes by the bank was exempt because it was not a loan for the purpose of purchasing or carrying stock. Regulation U is designed, in accordance with the statutory mandate, to help prevent the excessive use of credit for the purchase or carrying of securities. It is not intended to regulate bank credit extended for purposes other than purchasing or carrying securities, such as, for example, general manufacturing purposes, and the credit is not subject to the regulation merely because it is secured by stock. Accordingly, if the bank purchase of notes in the present instance was not in fact a disguised loan for the regulated purpose, it does not appear to conflict with the general intent of the regulation.

"We recognize, of course, that the effectiveness of Regulation U could be substantially nullified if banks made a practice of avoiding it merely by going through the form of purchasing notes instead of the usual procedure of 'making' a loan. Such circumventions would clearly be in violation of the terms of the regulation, however, as for instance the requirement in section 3(a) that the bank exercise good faith in accepting a statement of the purpose of a loan. The Board and the Federal Reserve Banks have been alert to

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"observe any substantial abuses of this sort so that appropriate amendments might be adopted if the need for them became evident.

"We are enclosing a copy of Regulation U for your information, and shall be glad to comment further if there is any point we have not covered adequately."

Approved unanimously.

Letter prepared for Chairman McCabe's signature to Mr. E. F. Bartelt, Chairman, Interdepartmental Savings Bond Committee, Treasury Department, reading as follows:

"This will acknowledge receipt of your Circular letter No. 92, dated May 14, 1948, enclosing a copy of Executive Order 9953, dated April 23, 1948, establishing the Interdepartmental Committee for the Peacetime Voluntary Pay Roll Savings Plan and a copy of the President's letter, dated April 28, 1948, to the Heads of Departments, Agencies and Independent Establishments of the Government in support of the Security Loan Drive.

"Pursuant to the authority contained in Paragraph 1 of the above-mentioned Executive Order, I hereby designate Liston P. Bethea, Director of the Board's Division of Administrative Services, as my alternate to act for me in all matters relating to the Committee. As you know, Mr. Bethea served in a similar capacity on the Interdepartmental Committee created by Executive Order 9135, approved April 16, 1942, which Order has been superseded by Executive Order 9953 referred to above.

"With respect to the President's letter of April 28, 1948, there is enclosed for your information a copy of the Board's reply dated May 7, 1948, together with a copy of a memorandum to all employees of the same date, bringing the President's request to their attention."

Approved unanimously.

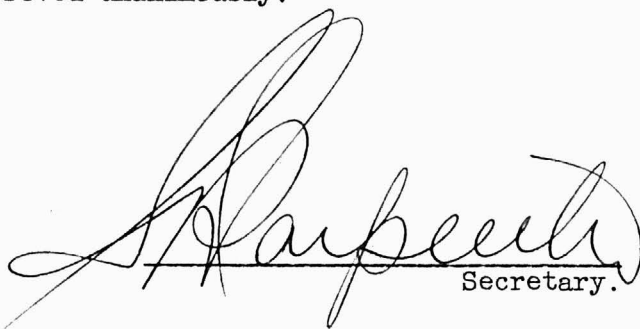
Letter to the Presidents of all Federal Reserve Banks reading as follows:

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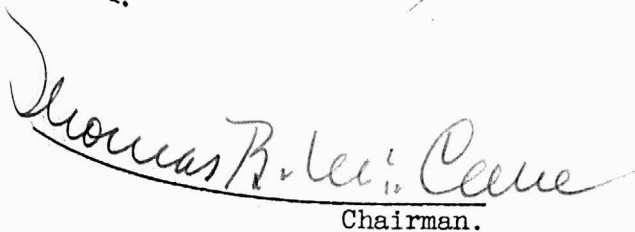
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"There are enclosed for your information copies of three tables showing the number of nonmember commercial banks eligible and ineligible for Federal Reserve membership on the basis of statutory capital requirements. These tables were compiled largely from the Reserve Banks' replies to the Board's telegram of May 3."

Approved unanimously.


Secretary.

Approved:


Chairman.