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 Tuesday, September 21, 1948, at 10:45 a.m.

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

Mr. Carpenter, Secretary
Mr. Riefler, Assistant to the Chairman

Messrs. Spencer, Burgess, Williams, McCoy, J. T. Brown, E. E. Brown, Penick, Atwood, Kemper, Woods, and Odlin, members of the Federal Advisory Council from the First, Second, Third, Fourth, Sixth, Seventh, Eighth, Ninth, Tenth, Eleventh, and Twelfth Federal Reserve Districts, respectively.

Mr. Prochnow, Secretary of the Federal Advisory Council

At its separate meeting, before this joint meeting, the Federal Advisory Council approved statements with respect to the matters which were to be discussed with the Board of Governors and yesterday copies of these statements were furnished to the members of the Board for consideration in accordance with the procedure agreed upon by the Council and the Board on December 3, 1946. At this joint meeting the discussions with respect to the topics were substantially as follows:

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Monetary Policy

1. The House Banking and Currency Committee has twice reported favorably and the House in the recent special session approved a proposal to restore the former ratio of required gold certificate reserves held by Federal Reserve Banks of 40 per cent against Federal Reserve notes and 35 per cent against Federal Reserve Bank deposits. In view of the possibility that this proposal may again be advanced in the Congress, the Board would like to know what the attitude of the Advisory Council would be toward it.

2. In the light of developments in the monetary and credit field since the Council met with the Board in April, what is the Council's judgment as to the effectiveness of policies of restraint so far adopted and what would be the Council's recommendations as to appropriate further action?

3. The use of Federal Reserve powers to raise reserve requirements.

4. The policy of supporting the government security market, especially in relation to sales by insurance companies.

Items two to four on the agenda, which are of the greatest importance, are so closely inter-related that the Council believes it best to consider them first and together.

Although there are many soft spots in the economy at present, the members of the Council feel that there is not as yet convincing evidence that the turn has been made, and that it is still the duty of the monetary authorities to take active measures to combat the inflationary trend.

On previous occasions the Council has emphasized that the primary causes of the inflation are largely outside the sphere of Federal Reserve policy, and include large government expenditures, especially for defense, foreign aid and veterans' assistance; the support of farm prices at high

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levels; government guarantees for housing at excessive costs; and repeated wage increases which have not been accompanied by comparable increases in production.

Specifically in relation to the questions raised by the items two to four on the agenda, the following statements represent the views of the Council at the present time:

A. The Council believes the increases which have taken place in the rediscount rate and in the certificate rate have been particularly helpful toward reducing the demand for credit by making both bankers and borrowers aware of the dangers in the present situation. Further increases in the rediscount and certificate rates should be considered if credit expansion continues.

B. It is too early to appraise the full effect of the recent increase in reserve requirements. The first effect has been to cause member banks to sell government securities to the Federal Reserve Banks. In view of the already large holdings of the Federal Reserve Banks, this action has raised the question in many peoples' minds of the future level of government bond prices and the future ability of the Federal Reserve Banks to maintain pegged prices.

Under present circumstances, of existing conservative lending policies by banks, the near absence of excess reserves, and Federal Reserve and Treasury policies of pegged prices for government securities, the Council reiterates its position that the increase of reserve requirements of banks is not a suitable instrument of credit control.

C. The Council is concerned with respect to the selling of government securities by insurance companies and other investors, in many cases to relend at higher rates. This selling is encouraged by pegged prices at a level which may offer the seller a profit as compared with the purchase price.

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All the members of the Council feel that owing to the size of the debt and its position in our whole economy, government bonds must be supported. A majority of the Council favors presently maintaining the peg at par, but not at a premium, on the long term 2-1/2 per cent bonds. A minority of the Council favors even greater flexibility.

D. In relation to item one on the agenda, apart from the tense international situation, the Council favors in principle raising the required gold reserves from the present ratio. However, in view of the present international situation, the proper timing of an increase in required gold reserves is of the utmost importance and demands the most careful consideration. It is impossible that any legislative action will be taken before the organization of Congress in early 1949, and the Council will be glad to review this question later in the light of the situation then.

For the purpose of amplifying the above statement, President Brown made substantially the following comment:

"The increase in reserve requirements recently approved by the Board of Governors went into effect September 16 for country banks and will go into effect on September 24 for reserve and central reserve city banks. September 16-18 is a period in which bank deposits generally increase for the reason that depositors build up balances for the purpose of paying income taxes. It takes several days for checks drawn in payment of income taxes to clear and this has resulted in the banks having increased deposits at a time when the increased reserve requirements took effect at country banks and many of the banks have sold securities to meet the increased requirements. It will be difficult to appraise the effects of the Board's action for several weeks. Many banks feel that, in addition to having to provide the additional required reserves, they will lose correspondent bank deposits as well. As long as the present policy of supporting the Government security market is continued, any

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increase in reserve requirements will be met by sales of securities to the Federal Reserve Banks. However, all members of the Council feel that the Government security market must be supported. A very considerable majority of the Council favor maintaining the price of long-term bonds at par but do not see the necessity of maintaining them above par. Some members of the minority of the Council feel that a drop in price of a point or more would discourage insurance companies and others from selling because they would not want to show in their published statements or reports to directors that they had taken a loss. A majority of the Council feel that if par were broken on the long-terms it would create such uneasiness as to cause large sales of securities because of the fear that prices would go still lower and that this might well cause heavier redemptions of Series E bonds.

On the question of raising the gold reserve requirements of the Federal Reserve Banks, the members of the Council believe that if we were living in reasonably normal times an increase in such requirements would have a cautionary effect both on the Board and on the Federal Reserve Banks as the excess reserves of the Federal Reserve Banks decreased. On the other hand, we realize that in the present situation, particularly if people become convinced that war is likely or if war should actually break out, the requirements would have to be lowered again and, if they were not the public would not understand action reducing reserves below requirements and paying a penalty, even though such a situation would have no practical effect. If a majority of the Council had to vote today, they probably would oppose the legislation. However, the matter cannot be acted upon by the Congress until March or April next year. What the international situation will be at that time is not known and for that reason the Council would like to defer reaching a conclusion on the matter until a later meeting.

At the conclusion of his statement, President Brown asked if any of the other members of the Council had any comments to make at this point but there was no response.

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Chairman McCabe read the following response of the Board to the Council's statement on the four topics set forth above:

Concerning the economic situation, the Board's general view coincides with that of the Council, namely, that despite soft spots in the economy at the present time, the outlook is on balance inflationary and that "it is the duty of the monetary authorities to take active measures to combat the inflationary trend." The Board continues to recognize that there are special factors outside the field of banking and credit that have promoted inflation. In addition to those listed by the Council, the Board would include high corporate profits and it would like to emphasize greatly the position created by the disappearance of the Federal surplus. This surplus during the past two years has been the most powerful anti-inflationary factor in the picture, but it has been offset by other factors, notably by the expansion of bank loans. In the absence of a budget surplus, an expansion of bank credit in the coming year similar to that of the past year would have much greater inflationary effects.

The Board has considered the suggestion of the Council that the peg on the long-term 2-1/2 per cent bonds be maintained at par without a premium. The Board is in agreement with the majority of the Council that the long-term yield on Treasury bonds should be maintained for the foreseeable future at a 2-1/2 per cent yield level, but believes that under present circumstances removal of the small premium would very probably have undesirable consequences. It may be that the establishment of support levels at exactly par last year would have been wiser, but removal of this small difference at the present time might undermine confidence in the whole support pattern.

The Board notes that a minority of the Council is in favor of a more flexible policy with respect to the support program, and agrees that greater flexibility in the short-term market is a desirable objective. Increases in certificate rates and discount rates to date are beginning moves toward this objective which the System initiated.

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The Board has long recognized that the maintenance of support for the bond market has greatly limited the effectiveness of credit-control methods. It feels that recent increases in short-term rates have been helpful, particularly in inducing the banks and others to buy short-term securities to absorb excess reserves. In the presence of strong demands for credit, however, higher short-term rates cannot be relied upon as adequate in restricting credit expansion.

The Board recognizes that increased reserve requirements with a complete peg in the Government securities market have less restraining effect than would otherwise be expected. It wishes to call to the Council's attention that one of the principal purposes of requesting Congress to give additional power to the Board to increase member bank reserve requirements was the need for absorbing additional reserves being created by the inflow of gold, by purchases of securities from nonbank holders, and by a possible return flow of currency. The current use of this authority will have the effect of increasing member banks reserve requirements by about 2 billion dollars. Since the System has purchased more than this amount of securities from nonbank holders during the past two months and will probably purchase substantial additional amounts in the immediate future, the higher requirements should not result in any net reduction in the earning assets of commercial banks. Although some banks will need to sell some Government securities in order to meet the change, the effect of the increase will be to prevent additional reserves which have become available from increasing the ability of banks to expand credit but not to reduce the lending capacity of the banks below previous levels.

The Board has noted the Council's position on raising the required gold reserves from the present ratio. Its own thinking on this matter has been fully expressed in memoranda or testimony to the Banking and Currency Committees of the Congress.

Chairman McCabe said that just before this meeting he had read the above statement over the telephone to Mr. Sproul, Vice

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Chairman of the Federal Open Market Committee, because of his close relationship to the Government security market, and that Mr. Sproul had said that he was in entire agreement with the statement.

President Brown questioned whether the Council would be willing to say (as the above statement does) that "the outlook is on balance inflationary" and referred to the fact that the comment in the Council's statement was "that there is not as yet convincing evidence that the turn has been made". President Brown also said that the comment in the Council's statement that it favored maintaining Government security prices at par but not at a premium, had reference particularly to the premiums of more than 8/32s which were being paid by the Federal Reserve Banks for some issues of securities purchased in the market and that these premiums were larger than the "small difference" indicated in the Board's statement.

Chairman McCabe responded that at the last meeting of the executive committee of the Federal Open Market Committee there was a long discussion of the System's present policy with respect to supporting the Government security market and that the members of the committee reached the unanimous conclusion that that policy should not be changed at this time and that even a drop of as much as 8/32s would have a very unsettling effect and would undoubtedly result in increasing the volume of securities that the System would have to buy.

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Mr. Williams asked if there had been any conferences with the insurance companies with respect to sales by such companies of restricted issues.

Chairman McCabe replied that he had had informal conversations with executives of insurance companies, but that no formal or general conference had been planned.

Mr. Williams said that in view of the attractive terms under which bonds had been sold to insurance companies he wondered whether there had been any serious attempt to remind them of their obligation to hold such securities.

At this point Mr. Fleming, a member of the Federal Advisory Council from the Fifth Federal Reserve District, entered the meeting.

Addressing himself to Mr. Williams' statement, Mr. Eccles said that restricted issues had not been made any more attractive to insurance companies than they were to any other nonbank holders and that insurance companies had not been given any special consideration in this connection.

Chairman McCabe asked Mr. Williams if he had anything to suggest as to what might be done and the latter replied that he did not have but had wondered whether there had been any effort to confer with the insurance companies and, if so, what the reaction was.

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Mr. Odlin referred to the comment in the Board's statement as set forth above with respect to high corporate profits and stated that, while he would admit that such profits were high in dollar amounts, they were temporary in their duration and, in view of high operating costs, he did not think they were high. He questioned whether it was particularly appropriate for an agency of the Government to refer to such profits with an implied criticism that they were too high.

Chairman McCabe stated that the causes of inflation mentioned in the Council's statement did not include corporate profits and the Board felt that if the list of inflationary causes was to be complete it would be necessary to include profits.

Mr. Eccles stated that corporate profits were substantial inflationary factors for the reason that without them there would not have been as great an expansion in expenditures of corporations for capital goods which aggravated the shortages of lumber, steel, skilled labor, and other things which were in short supply. Furthermore, he said, if there had not been high corporate profits the pressure for increased wages would have been much easier to resist, and that because of high profits corporations agreed to increase wages without much argument because they did not have a strong defense. For that reason, he was of the opinion that the Council could not argue that wages were a factor in the inflation and ignore entirely the inflationary effects of corporate profits.

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Mr. Fleming asked if the Board had made an examination of the adequacy of depreciation reserves of corporations and he questioned whether profits would be as large as reported if adequate depreciation reserves were provided to meet higher replacement costs.

Chairman McCabe stated that this situation had been recognized by many corporations in the creation of special reserves and he expressed the opinion that in many instances depreciation reserves unquestionably were too low.

President Brown stated that high corporate profits could disappear over night but that wage increases would continue for a much longer period.

Mr. Eccles responded that that did not eliminate the fact that high profits were an important factor in the inflationary situation. He also said that, with the increased cost of living, increases in wages were as much justified as higher depreciation reserves because of higher replacement costs, and that if corporations could justify increased profits on the ground of higher replacement costs labor likewise could argue for higher wages because of the higher cost of living. This situation, he said, argued for the retention of wage controls as well as excess profits taxes as one could not be removed without the other but that having been removed they could not now be restored.

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Mr. Odlin said that he just wanted the record to show that the question had been raised and that he did not think there should be the implication that corporate profits were unjustifiably high.

President Brown stated that the Council spent most of the time in its separate meeting on the question of the 2-1/2 per cent rate on long-term Government securities and, since Mr. Burgess was a director of one of the large insurance companies and came from New York where most of the large insurance companies were located, he would like to have Mr. Burgess discuss the question of sales of securities by insurance companies as well as the questions of the psychological effect of supporting the market at par or slightly below par and whether such support would result in further sales in the market or would restrain such sales.

Mr. Burgess made substantially the following statement:

> I would like to tie this into the discussion on corporate profits. I think Mr. Eccles has brought out an important point and I would prefer to see it broken down into two elements. First, I think business pricing policies have been inflationary and that is why profits have been higher. Secondly, the large program for capital expansion, which perhaps is the most active inflationary factor and which has been supplemented by tremendous spending by States, municipalities, and utilities, has been financed partly out of profits and partly out of money borrowed from the market.
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> The banks feel that by increasing reserve requirements the Federal Reserve System is "milking a dry cow" and that the loans that the banks are making are the result of activities that they have to finance. As a result of the

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American Bankers Association program, increases in discount rates, warnings, etc., the banks have been backing away from loans for capital purposes and term loans have not been increasing. It is difficult to see what other loans could be avoided. The banks have done a lot of screening. The vulnerable point has been in the capital goods field for the reason that every analysis of the business cycle shows that the big expansion is in durable goods. I feel that if an attempt were to be made to deal with the inflationary situation it should be in that field. Loans being made by the insurance companies are for the expansion of capital goods. These companies have not only been using new savings currently received but also additional funds obtained by sales of securities to the Federal Reserve Banks. These sales not only make credit available to the borrowers from the insurance companies but also create additional bank reserves which could be used by the banks for further multiple expansion. The banks have shown a willingness to use these reserve funds to purchase short-term Government securities with the result that there has been no net increase in the System's holdings of securities. While the purchase of short-term Governments by the banks prevents the use of additional reserve funds for further credit expansion, they do not offset the additional credit made available to borrowers from insurance companies. This credit involves a movement of goods which in turn involves further use of bank credit through loans to customers to finance such movements.

(In response to an inquiry from Chairman McCabe whether there was any move on the part of insurance companies to adopt a program similar to the program of the American Bankers Association to avoid as much as possible the extension of inflationary credit.) I think the insurance companies have discussed that problem informally but I don't know of any such an arrangement. I think it would be helpful if the Board or the Treasury would get representatives of the insurance companies together. The Treasury talks to representatives of insurance companies from time to time on other problems, and what you want the insurance companies to do is to do the same screening job on loans that the banks have been doing.

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On the question of the effect of insurance company selling on the Government security market, it is my pretty solid impression that if you offer a premium on Government securities there is a greater inducement to sell securities and lend than there would be if the insurance companies had to take a loss on securities sold. If insurance companies were taking a loss on bonds which they sold, there would be a greater screening of their loans. How much screening there would be I do not know. Some people think that if the market was on a 2.55 per cent basis and insurance companies could get a 3 per cent obligation that they would make the loan. My own feeling is that people who hold that view are overlooking the reluctance of insurance companies to take a loss.

When there is a drop in support levels a certain amount of selling comes into the market immediately. We went through that in December. I think in times like this it is a good thing to give people a shock. We can't get through a deflation without someone getting hurt. I think a further reduction in market prices has been anticipated to a considerable extent and a lot of weak owners of Government securities have already been shaken out. I do not think there would be pandemonium in the market if support prices were reduced but if the change were made I would make it large enough so that it would be a deterrent to selling. I would favor a decline in support prices to 99 or 98 so that there would be a real deterrent. That is a vigorous step and if it is taken you would have to think of possible reactions in Europe and elsewhere.

I agree with the System's action on the discount rate but I do not agree with the recent action to increase reserve requirements. The latter action has raised in the public's mind the question whether the policy of supporting the Government security market will be maintained because it has forced the sale to the Federal Reserve Banks of $1 billion or $1.5 billion of securities.

In a discussion of the effect of the recent increase in reserve requirements, Mr. Burgess expressed the view that the increase would not materially affect the expansion of bank credit, because

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the banks have obligations to take care of the needs of their customers to finance current business, mortgage loans, etc., and were under tremendous pressure to extend such credit. He also said that when banks get excess reserves they almost automatically purchase short-term Government securities as shown by the fact that the System's net holdings of securities have not increased as compared with a year ago.

Chairman McCabe stated that the opinions of bankers range all the way from (1) a strong fear on the part of small bankers of any change whatsoever in the support price of Government securities to (2) the feeling on the part of larger banks that such prices could be lowered to advantage. He asked the Council to what level prices should be reduced if a change were made.

Mr. Fleming renewed the suggestion that an attempt be made to get the heads of insurance companies to confer with the Treasury and the Board and some question was raised whether that would have any beneficial result. Mr. Fleming's reason for his suggestion was that the insurance companies were interested in preventing a development of a boom and bust situation and in keeping the economy on a sound basis. While there would be divergent views, he thought the result of such a conference would be worth the effort.

Mr. Fleming then asked what effect a decrease in support prices would have on the foreign situation. He thought that the

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Russians would propagandize the change and stated that it was that factor that caused him to join with the majority of the Council favoring the maintenance of support prices. In taking that position, he said, he recognized that as long as prices were maintained it would be difficult to prevent monetization of the Government debt.

President Brown inquired whether it was necessary for the System to maintain the present level of support prices on all issues of bonds and Mr. Fleming asked why the System felt it was necessary to support some issues at a price of as much as 101.

Mr. Eccles explained why, as long as a 1-1/4 per cent one-year certificate rate and 2-1/2 per cent long-term rate were maintained, it was necessary to maintain a level of prices on intermediate issues which would have a proper relation to the two rates. He stated that if there were no market for the issues between the 1-1/4 per cent certificate and the 2-1/2 per cent long-term bond there might be unduly wide fluctuations in such issues which might result in injury to small holders without any offsetting benefit from the standpoint of the anti-inflationary program. He added that the System would have gotten away from the support of the short-term rate long before this if the Treasury had been agreeable and that until that occurred he did not see how the System could avoid maintaining prices at premiums on the intermediate

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issues. He called attention to the fact that there had been no support of the partially tax exempt issues other than for the purpose of maintaining orderly market conditions in such issues.

Mr. Burgess said that this problem was one that was in the hands of the monetary authorities because they could do something about it, that looking backward he thought it could be said that the Treasury and the Federal Reserve were doing "too little too late" in the field of monetary control, and that the whole ideology of market control that had been built up during the War and continued into the peacetime period was one of the things that stood in the way of effective monetary control.

Chairman McCabe stated that there was more responsibility in the matter than that resting on the Treasury and the Federal Reserve and Mr. Burgess responded that the bankers were "particeps criminis" in the matter.

In response to an inquiry from Mr. Szymczak whether the Council would suggest that the market be permitted to seek its own level, Mr. Burgess referred to the Council statement on that point.

During a discussion of the possible effects of a drop in support prices of government securities, Mr. Burgess stated that there was a substantial opinion that the System would not be able to maintain the present prices and also that it should not do so.

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He also said that he was a member of a committee that in the course of the next few weeks would publish a recommendation for greater flexibility in the government security market.

In a discussion of what was meant by greater flexibility it was brought out that it did not mean no support but support at a lower level. In response to an inquiry by Mr. Szymczak whether it would mean dropping support prices by steps, Mr. Fleming expressed the view that such a policy would be an invitation to the public to sell securities before they declined further.

President Brown stated that a majority of the Council felt that psychologically the long-term bonds could not be permitted to go below par, that all members of the Council felt that there should be some support, that the member of the Council holding the most extreme view thought that they could be permitted to go down to 95, that Mr. Burgess was thinking of 99 or thereabouts, and that one or two members of the Council felt that 99-7/8 would be sufficient decline to discourage further selling. He added that he was one of the majority of the Council who felt that "you can't cut off a dog's tail by inches".

Referring to Mr. Burgess' statement that the Federal Reserve and the Treasury were doing too little too late, Mr. Eccles stated that the Board had been fully aware as far back as 1942 of the prob-

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lem now being faced by the System and the Treasury, that at that time the System advised the Treasury that no long-term market securities should be issued if there was to be support of a short-term rate, and that special nonmarketable securities should be offered to insurance companies and other nonbank investors, but that the banks argued strongly against anything other than marketable issues, and that the System got nowhere with its suggestion.

In response to an inquiry from Mr. Spencer whether the Treasury would have sold the necessary amounts of securities under that procedure, Mr. Eccles replied that it would have sold what was needed and would have avoided the existing problem of a pattern of rates. He also said that there were two ways of dealing with the problem (1) the traditional method of selling securities in the market and raising the discount rate, and (2) the special reserve plan proposed by the Board. On the first method, he said, the System would have to be prepared to raise the discount rate high enough so that Federal Reserve Bank credit would not be used to expand credit. He also said that during the period 1945 to 1947 the monetary and credit policies to be followed were discussed with the bankers and the decisions reached were largely agreed to by them. He made the further statement that the record would show that the Board had not been derelict in recognizing the problem and that it was not responsible for doing too little too late.

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Gold Policy.

5. The gold policy of the Federal Reserve System and the Treasury, including the procedure with respect to gold exports and imports.

The Council desires to defer the discussion of this subject to a later date when it can be fully considered. In general, it believes that the movements of gold, including the transfer of gold by foreign central banks, should as far as practicable be removed from discretionary authority. The Council would be interested in knowing whether there have been occasions when licenses have been denied to foreign central banks for the transfer of gold. The Council also feels it would be desirable to examine our whole gold policy and the present legislation regarding gold, and it would welcome any data and information from the Board of Governors which would be helpful in such a study.

Chairman McCabe read the Board's response to this topic as follows:

There have been discussions between representatives of the System and of the Treasury regarding the United States gold policy, with particular reference to the possibility of relaxing or removing controls on the transfer of gold by or for foreign central banks. After extended discussions, however, it did not appear feasible for the Treasury to relinquish entirely its control over gold transactions, especially in view of the current unsettled international situation. The Board plans to review this problem from time to time and to hold further discussions with the Treasury when conditions warrant. To the extent possible, in the light of its confidential character, the Board will be glad to supply the Council with further information on the subject as a basis for future study and discussion.

President Brown stated that the large discretionary power remaining in the Treasury under existing legislation should be

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reviewed and that, except in cases where movements of gold were important for political or other reasons, gold should be permitted to move in and out of the country freely in the settlement of international balances.

In response to an inquiry by President Brown whether there had been any instances in the last two or three years in which gold licenses had been denied, Mr. Szymczak stated that there had been three instances in which the foreign nations involved had been dissuaded from requesting licenses to move gold. He also said that the Board felt that the present was not a good time to take the matter up with the Treasury again and that such action might be harmful instead of helpful in the present situation.

Regulation of Consumer Credit.

6. Policies of the Board of Governors in enforcing regulation of consumer credit.

> Without discussing the necessity or desirability of the legislation on consumer credit, the regulations issued by the Board of Governors appear to the Council generally reasonable and fair and well received. Since the terms are similar to those already being followed by banks the effect on loans directly by banks to installment borrowers will be slight. Principal criticisms of the regulations now appear to come from dealers in furniture and used cars.

Chairman McCabe stated that the Board appreciated the views of the Council on this matter and wished to assure the members that if at any time they had suggestions as to policies that might be

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followed in connection with the regulation of consumer credit or questions with respect to the policies adopted by the Board in this field the Board would be very glad to have the Council submit them.

Mr. J. T. Brown inquired what the Board intended to do to enforce compliance with the regulation, and Mr. Evans stated that the regulation now rested on the basis of a statute enacted by the Congress and gave the Board additional powers to enforce compliance. He discussed very briefly how these powers might be used and stated (in response to further inquiry by Mr. Brown) that the Board proposed to inspect registrants in the field to see that the regulation was being observed and he outlined the policy that the Board proposed to follow in that connection.

Mr. J. T. Brown then referred to the proposed amendment which would render unenforceable consumer instalment contracts which did not comply with the terms of the Board's regulation and expressed strongly the opinion that the amendment should not be adopted for the reason that banks purchase such paper as holders in due course or acquire it as collateral for advances, that in most cases failure to comply with the regulation was unintentional and when discovered was corrected immediately, and that if the contracts were made unenforceable it would work a great deal of hardship on the banks because of attempts of unscrupulous borrowers (at the suggestion of "ambulance

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chasing" lawyers or otherwise) to avoid payment of their obligation. Other members of the Council indicated full agreement with Mr. Brown's views, the opinion being expressed that the amendment might be particularly undesirable from the standpoint of possible injury to small banks which handle paper for small automobile dealers or other small concerns which created instalment credit obligations.

Mr. Evans explained the reasons for the Board's action in publishing notice that it was considering such an amendment and there was a discussion of how and to what extent such an amendment would affect nonconforming contracts. He also said that if the Board should find that it could not enforce the regulation without such a provision it could put it into effect.

Mr. McCoy suggested that if the amendment were adopted banks would refuse to take paper from a dealer or finance company and stated that in such a situation his bank would not extend credit on any contract that was not made directly by the bank.

In the ensuing discussion members of the Council indicated that they favored effective enforcement of the regulation, that the regulation had been well received, and that there was a more friendly feeling toward it than in the past.

President Brown stated that he thought almost all small loan and finance companies were opposed to the regulation, that so far as

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large sellers such as mail order houses were concerned their sales of durable goods had increased to a point where they were having difficulty financing them and that they were glad to have some restraint imposed. Therefore, he said, on the whole they were rather favorable to the regulation. He thought that if any group had any grounds for opposition it was the furniture people but that that was not too important.

Mr. Odlin stated that the record should show that the discussion of consumer credit at this meeting was not to be interpreted as an approval on the part of the Council of the permanent lodgment in the Board of authority to regulate consumer instalment credit and that he did not favor such authority.

Bank Holding Company Legislation.

7. The Board of Governors would appreciate any further views and comments the Council may have regarding proposed Bank Holding Company legislation.

In connection with proposed bank holding company legislation, the Council adopted the following resolution on May 20, 1947:

RESOLUTION

The Council for the past few years has at almost every meeting discussed the holding company situation, the inadequacies of existing legialation, and proposals for additional legislation in connection with it.

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(1) The Council believes that holding company legislation should be enacted at this time. Experience has shown that the present legislation is inadequate and that additional legislation is urgently necessary.

(2) It approves the general approach to the holding company problem embodied in Senate Bill 829.

(3) It believes Senate Bill 829 should be amended--

(a) By adding to the declaration of policy and the standards for Federal Reserve Board, Comptroller of the Currency, and Federal Deposit Insurance Corporation action a more definite statement of objectives and standards. (A memorandum is attached which was the subject of discussion between the Board of Governors and the Federal Advisory Council which indicates the type of amendments in this regard which the Council believes necessary.) [The memorandum follows on the next page.]

(b) By granting tax exemption to such holding companies as are required to divest themselves of nonbanking assets. Simple justice requires that such tax exemption should be granted, and a precedent exists for it in the utility holding company legislation.

(c) By requiring a larger percentage than 10 per cent of the ownership of stock in two or more banks in order to create an automatic holding company relationship.

(d) By providing that incidental ownership of bank stocks in fiduciary capacities such as executor, trustee under a will, etc., should not create an automatic holding company relationship.

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The Council urges the Board to submit amendments in accordance with these suggestions and to press for the enactment of the bill as so amended.

* * * * *

MEMORANDUM

SUBMITTED IN CONNECTION WITH THE FOREGOING RESOLUTION

1. To reach and regulate any banking operation which, functioning in an area or with a structure larger than that permitted to independent banks, can or does, through the medium of concentrated control, jeopardize independent competitive banking at local or regional levels or place independent banks under the particular circumstances at a competitive disadvantage;

2. To confine the size and expanse of any such banking operation, regardless of its competitive or other aspects, within limits consistent with adequate and sound banking; and

3. To control the magnitude and expanse of any such banking operation, regardless of all other considerations, to the end that, in the event of adverse general economic conditions, such an operation will not be subjected to an inordinate pressure arising from unwieldiness due solely to mere size and expanse which, in turn, may put an inordinate pressure on the nation's banking structure.

* * * * *

On February 17, 1948, the Council adopted the following resolution regarding bank holding company legislation:

RESOLUTION

"The Federal Advisory Council has approved by resolution Bank Holding Company legislation. It believes that Senate Bill No. 829 with the

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"amendments suggested by the Council in its resolution of May 20, 1947 should be passed by this session of the Congress and that action by the Congress should not be delayed.

The Federal Advisory Council urges the Board of Governors of the Federal Reserve System to use its best efforts to secure the passage of the bill, with the amendments suggested by the Council and asks that this resolution be transmitted to the members of the Senate and House Banking and Currency Committees."

* * * * *

The Council reaffirms the position it took on bank holding company legislation as expressed in the above resolutions, and favors the enactment of such legislation at the next session of the Congress.

Chairman McCabe stated that the Board was holding a series of conferences on this subject, and that two conferences had already been held, one with representatives of the holding companies, and one with representatives of the American Bankers Association. He added that it was hoped to have conferences with representatives of the independent bankers associations, reserve city bankers, and State bank supervisors, that at the two meetings that had already been held suggestions were made as to changes in the legislation, and that the Board would be glad to submit to the Council at its next meeting the results of the discussions during the series of conferences.

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President Brown inquired whether the Clayton Act proceeding against Transamerica Corporation would affect the legislation in any way. The reason for his question was, he said, that it might be argued that if the Board was successful in the proceeding against Transamerica there would be no need for legislation.

Chairman McCabe replied that he did not think the Board would relax its support of the proposed legislation regardless of the outcome of the Transamerica matter.

Mr. Eccles reviewed the legislative situation with respect to the bill and proposed amendments thereto which were before the Congress at the last regular session. He also expressed the view that there was no relationship between the legislation and the proceeding against Transamerica and that the legislation was needed to prevent another situation like the Transamerica case from arising.

In response to a comment by Mr. Fleming that the Board should push the legislation at the next session, Mr. Eccles stated that the Board had not had the support of the Comptroller of the Currency or the Federal Deposit Insurance Corporation in the matter. In that connection Chairman McCabe stated that representatives of the Comptroller of the Currency and the Federal Deposit Insurance Corporation had attended the conferences with representatives of the American Bankers Association and would be invited to attend subsequent

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conferences with the independent bankers associations, the reserve city bankers, and the State bank supervisors.

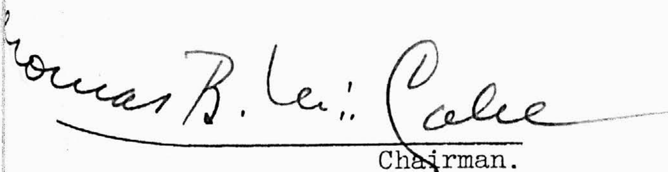
Mr. Fleming asked what the position of the American Bankers Association would be on the legislation and Chairman McCabe stated that the indications had been that there would be a strong resolution at the forthcoming convention of the Association endorsing the principle of bank holding company legislation but reserving the right to suggest changes.

President Brown stated that, if agreeable to the Board, the next meeting of the Federal Advisory Council would be held in Washington on November 14-16, 1948. The members of the Board indicated that these two dates were agreeable to them.

Thereupon the meeting adjourned.

Secretary.

Approved:



Chairman.

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