

Minutes of actions taken by the Board of Governors of the Federal Reserve System on Tuesday, January 4, 1949. The Board met in the Board Room at 12:15 p.m.

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

Mr. Carpenter, Secretary
Mr. Sherman, Assistant Secretary
Mr. Morrill, Special Adviser
Mr. Thurston, Assistant to the Board
Mr. Riefler, Assistant to the Chairman
Mr. Thomas, Director of the Division of Research and Statistics
Mr. Vest, General Counsel
Mr. Millard, Director of the Division of Examinations
Mr. Baumann, Assistant General Counsel

In accordance with the action taken at the meeting on December 31, 1948, there was presented a draft of letter to Mr. Elmer B. Staats, Assistant Director, Legislative Reference, Bureau of the Budget, reading as follows:

"This is in reply to your letter of November 29, 1948, requesting the views of the Board on a draft of a bill submitted by the Housing and Home Finance Agency, dated November 20, 1948, entitled 'Housing Act of 1949.'

"The proposed bill, after a general declaration of national housing policy, provides in separate titles for financial assistance to local public agencies in connection with the elimination of slum and other blighted areas, amendments to the United States Housing Act of 1947 relating to low-rent public housing, a program of housing research to be undertaken by the Housing and Home Finance Administrator, and financial assistance through the Secretary

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"of Agriculture to provide housing on farms.

"The Board has several suggestions to make about the proposed declaration of national housing policy, and about Titles I and II, dealing respectively with the elimination of blighted areas and the provision of low-rent public housing.

"Declaration of national housing policy

"The proposed declaration of national housing policy states, among other things, that an adequate volume of residential construction is necessary to achieve maximum employment, production, and purchasing power. While this declaration is not objectionable as far as it goes, it fails to recognize that programs for encouraging building can add to inflation in periods of high and virtually maximum employment such as the present by intensifying the bidding for scarce labor and materials and by adding further to the volume or velocity of purchasing power. Accordingly, the Board believes that such a policy declaration should include a statement that all Federal programs for encouraging housing, construction, and redevelopment are to be so conducted as to minimize inflationary pressures during periods of substantially full employment and production.

"For example, if inflationary pressures such as have prevailed in the past year continue, the Board questions whether as many as 100,000 public housing units a year, for which Title II provides, can be built without adding to those pressures unless there is some restriction on other types of construction activity, especially in the higher-priced housing field.

"Financial arrangements of Titles I and II

"Titles I and II of the proposed bill would encourage agencies established by local governments to issue tax-exempt securities to private investors. The Board would like to raise the general question whether such use of tax-exempt securities should not be discouraged rather than stimulated.

"Federal credit, contributions, and grants provide an appreciable part of the security for obligations issued by local agencies operating under the United States Housing Act of 1937, and for obligations which would be issued by agencies operating under Titles I and II of the proposed bill. In the past decade,

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"however, income from Federal obligations generally has been made taxable by the Federal Government, and Federal tax rates have been increased substantially. Under the circumstances, it would seem undesirable to encourage through this bill further additions to the supply of tax-exempt issues.

"A similar question is presented by the proposal in Title II to exempt obligations of local public housing authorities from section 5136 of the Revised Statutes. This exemption would permit national banks and State banks which are members of the Federal Reserve System to hold such obligations in excess of 10 per cent of capital and surplus. Even though such obligations would be secured in part by certain undertakings of the Federal Government, they often would not have the marketability desirable in securities held by banks. Furthermore, during the past decade the Federal Government has steadily reduced the use of guaranteed securities, preferring to have agencies borrow from the Treasury which, in turn, sells securities which are fully taxable. It would hardly seem desirable, therefore, to write a special exemption into section 5136 for these securities which have limited marketability, would not be direct obligations of the United States, and would not be taxable.

"The Board therefore believes that the financial arrangements set out in Titles I and II are not desirable, considering the effects on the Federal tax revenues and the banking system as well as on the local agencies. It may be that an arrangement whereby local agencies participating in these programs would borrow directly from the Federal Government would be more suitable than that provided in the proposed bill, even though the Federal Government were to lend at rates lower than 'the going Federal rate.'

"Title I - Slum clearance and redevelopment

"Title I of the proposed bill, although aimed at a worthy goal, is open to serious objection. Its purpose is to help local communities to eliminate their slum and blighted areas, but there is a serious danger that the bill as it now stands would aggravate one of the most formidable hindrances in such areas to desirable redevelopment in response to ordinary economic forces -- namely, the valuation of land far above its worth.

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"Under this Title the Federal Government would make loans and capital grants to local public agencies for acquiring, clearing, and revaluing slum and blighted areas. The amount of the loans authorized is one billion dollars, and an additional amount of Federal grants totalling 500 million dollars is authorized provided the local governments make matching grants of at least 250 million dollars.

"To make available such substantial amounts of Federal credit and cash grants under provisions that would permit localities to pay more for redevelopment land than it is worth seems to us to encourage overvaluation of land in deteriorating areas, and to raise all land values, in varying degrees, in and around affected areas before redevelopment can begin. The expenditure of the large amount of Federal funds contemplated in this Title cannot achieve its avowed purpose if it merely represents a reward for improper land use or for skill in disposing of land at prices in excess of current economic value. To prevent such a misuse of Federal funds there should be more specific standards and safeguards than Title I now contains. It may well be that further study of the legal, social, and economic problems involved will be required before really adequate standards and safeguards can be formulated. But it would seem that at the very least, the present bill should contain some requirement that the local public agencies shall use condemnation or such other methods in acquiring land as will give reasonable assurance that the prices paid will not be excessive, and will not represent values which could not be sustained if adequate police, housing, and similar regulations were enforced with respect to existing buildings.

"Title II - Low-rent public housing

"There is clearly a social need for the resumption of the low-rent public housing program which Title II of the bill would make possible. Subject to our previous comments on the financial arrangements, the Board would have no objection to enactment of this Title, with two changes.

"The first change which the Board would suggest is the deletion of the provision in Section 201 that 'a gap of at least 20 per centum be left between the upper rental limits for admission to the proposed low-rent housing and the lowest rents at which private enterprise

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"is providing . . . a substantial supply of decent, safe, and sanitary housing . . ." Inclusion of this requirement seems likely to lead to needless controversy and impediments to the program, without increasing appreciably the other statutory safeguards against undue competition with privately-provided housing.

"The second change which the Board would suggest is deletion of the provision for demolition of a number of dwellings substantially equal to the number of new dwellings provided under the program. This requirement now appears in section 10 (a) of the United States Housing Act of 1937, and would be modified slightly by section 206 (b) of the proposed bill.

"We recognize that many dwellings are substandard and should be eliminated from the market, but it would seem to be better to force these dwellings out of the market by the competition of better dwellings at comparable rents than to require their demolition merely because certain new units have been built. Poor as they are, these substandard dwellings perform two functions: first, they provide shelter now for their occupants; and second, even when they are vacant, they serve by their very presence to check rent increases in other low-rent dwellings.

"The Board may have comments to make on Title IV, dealing with farm housing. If so, they will be forwarded in a later letter.

"If changes can be made in the proposed bill to take account of these views, the Board will have no objection to passage of this legislation. The most serious defect of the proposed bill is the lack of safeguards and standards in Title I. Should it be impossible to remedy this defect, the Board would recommend that this Title be eliminated."

Approved unanimously.

Chairman McCabe stated that unless further changes were made in the galley proof, the President's Economic Report would contain the paragraph proposed by the Board relative to additional authority to increase reserve requirements except for the sentence

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relating to the payment of interest on reserve balances, and would also recommend continuation of authority for the regulation of consumer instalment credit.

Mr. Vardaman referred to the discussion of the Board's budget for the year 1949 at the meeting on December 31, 1948, stating that he felt the procedure followed in the preparation of the budget should be considered at a meeting of the Board. He also suggested that consideration be given to establishing a procedure under which the Board's budget would be reviewed at the same time that the Federal Reserve Bank budgets were considered and to setting the time for such consideration in October or November rather than in December as is now provided, and that a special committee be appointed to review the budget and make recommendation to the Board with respect thereto.

Mr. Bethea entered the meeting at this time.

There was a discussion of Mr. Vardaman's suggestions, during which it was pointed out that the Board's budget was among the matters assigned to the Personnel Committee for initial consideration principally because the budget consisted largely of expenditures for personnel.

There was a discussion of various ways in which the budget might be handled, at the conclusion of which Chairman McCabe suggested that the matter be referred back to the Personnel Committee for further consideration and recommendation to the Board.

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Chairman McCabe's suggestion was approved unanimously.

The meeting then recessed and reconvened at 2:30 p.m. with Messrs. McCabe, Szymczak, Draper, Vardaman, and Clayton, and Mr. Carpenter present.

Mr. Vardaman referred to the letter approved by the Board under date of December 15, 1948, to Mr. Peterson, Vice President of the Federal Reserve Bank of St. Louis with respect to possible violations by the United Bank and Trust Company, St. Louis, Missouri, of Federal statutes relating to misapplication of funds of member banks and political contributions by corporations, and to a draft of proposed letter to the Attorney General of the United States transmitting a copy of a letter received from the Federal Reserve Bank under date of December 21, 1948, giving information with respect to the possible violations as disclosed by a recent examination of the member bank.

The possible violations referred to consisted of the establishment by the Trust Company of a ledger account in the name of the treasurer and assistant secretary of the bank to which was credited commissions from insurance placed on collateral security on loans made by the bank and from which contributions for political purposes had been made. The question involved was whether the funds in the account belonged to the Treasurer and

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Assistant Secretary, as claimed by the President of the bank, or whether the funds were the property of the bank and the political contributions were in fact made from bank funds.

Mr. Vardaman stated that he had asked that the proposed letter to the Attorney General be placed on the docket so that he could express his views with respect to the manner in which the entire matter has been handled. He said that the incident involved the question of what the attitude of the examining divisions of the Federal Reserve Banks and the Board should be with respect to possible violations; that is, whether all violations should be reported immediately to the United States Attorney or whether the examiners should try to find a satisfactory solution in those cases where there was no actual defalcation or other similar offense but an ill-advised or unintentional violation of some statute. It was his view that the latter course should be followed, and that, if necessary, the examiner should first report such matters to the United States Attorney orally with a view to working out a satisfactory solution.

In this connection Mr. Vardaman referred to incidents that had come to his attention which might indicate that there was some animosity toward the member bank on the part of Mr. Carstarphen, General Counsel of the Federal Reserve Bank of St. Louis, and that possibly he had influenced the attitude of Mr. Peterson toward the

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member bank. He stated that in the circumstances the question was raised whether the Board should ask Mr. Millard to go to St. Louis to ascertain what the actual situation was in this respect and to attempt to ascertain whether there had been a deliberate violation of the law which would justify the Board in taking action to remove the officers of the member bank.

During the discussion of Mr. Vardaman's suggestion, Messrs. Vest, General Counsel, and Millard, Director of the Division of Examinations, were called into the meeting and Mr. Vest reviewed the instructions of the Board to the Federal Reserve Banks with respect to reporting possible violations of law.

The letters from Mr. Peterson dated November 30 (to which the Board's letter of December 15, 1948, was a reply) and December 21 submitting copies of a letter and attachments thereto sent to the United States Attorney at St. Louis were read, together with an excerpt from the report of examination of the United Bank and Trust Company as of October 5, 1948, relating to the possible violations.

The members of the Board other than Mr. Vardaman expressed the view that, rather than censuring the examiners at St. Louis for reporting the matter, they should be commended, and that Mr. Peterson could not have done otherwise than to bring the matter to the attention of the Board.

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Mr. Vardaman said he did not agree for the reason that he felt that before reporting the matter Mr. Peterson should have talked personally with the president of the bank and, if necessary, taken him to see the United States Attorney.

There was some question on the part of the other members of the Board whether the last step referred to by Mr. Vardaman would have been appropriate under the circumstances.

At the conclusion of the discussion it was agreed that Mr. Millard should call Mr. Davis, President of the Federal Reserve Bank of St. Louis, on the telephone and arrange to go to St. Louis at a time when Messrs. Davis and Peterson would be at the Bank for the purpose of making a full investigation of the manner in which the matter had been handled by the Federal Reserve Bank, the reasons for the actions that had been taken by the Bank including whether there was anything in the personal attitude of the officers involved toward the member bank that would be subject to criticism, and any developments in connection with the matter since it was first reported by the examiners. It was understood that as soon as Mr. Millard's investigation was completed he would make a report to the Board.

Mr. Millard inquired whether it was to be understood that he would confine his investigation to the Federal Reserve Bank of St. Louis and it was agreed that he should first look into the matter at the Federal Reserve Bank and then, if in his judgment such a step would be desirable, he might visit the member bank with Mr. Peterson or ask Mr. Davis to invite the president and possibly other senior officers of the member bank to the Federal Reserve Bank for luncheon and for such discussion of the matter as appeared to be advisable.

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Mr. Vardaman then presented and there was read the following statement which he asked be made a part of the minutes of this meeting:

"With reference to the minutes of December 15, I want to be recorded as opposing the action in transmitting the letter to the St. Louis Federal Reserve Bank, with reference to the United Bank and Trust Company of St. Louis. It is my thought that this matter was improperly handled by the Examining Division of the St. Louis Bank, and by the Examining Division of this Board. I do not think the matter should have been referred to the U. S. Attorney without a more thorough investigation into the matter by the Chief Examiner and the senior officers of the St. Louis Bank, and by the Director of the Examining Division of this Board; and, if necessary, by a Board member from this Board.

"Although there was an apparent technical violation of certain statutes by the bank, there was absolutely no indication or evidence of criminal intent, since the account in question had been openly on the books for several years -- all deposits and withdrawals being properly listed and accounted for; and the examiners have had constructive knowledge of this account for this period of time.

"I submit that the matter probably could have been satisfactorily settled by conferences between Federal Reserve officials, the subject bank officials, and the U. S. Attorney."

In connection with the above matter it was agreed that the information attached to Mr. Peterson's letter of December 21 with respect to the possible violations should be transmitted to the Attorney General of the United States immediately without reference to the information to be developed by Mr. Millard in his investigation at the Federal Reserve Bank of St. Louis.

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Thereupon, unanimous approval was given to the following letter to the Attorney General of the United States:

"There are enclosed for such action as you consider advisable, two copies of a letter dated December 21, 1948, and enclosures, which Mr. William E. Peterson, Vice President, Federal Reserve Bank of St. Louis, addressed to the United States Attorney, St. Louis, Missouri, reporting possible violations of criminal provisions of the laws of the United States disclosed during a recent examination of the United Bank and Trust Company, St. Louis, Missouri, a member of the Federal Reserve System."

The action stated with respect to each of the matters hereinafter referred to was taken by the Board:

Minutes of actions taken by the Board of Governors of the Federal Reserve System on January 3, 1949, were approved unanimously.

Memoranda from Mr. Bethea, Director of the Division of Administrative Services, recommending the following appointments in that Division, on a temporary basis for a period of two months, effective as of the dates upon which the appointees enter upon the performance of their duties after having passed the usual physical examination:

Date of Memo.	Name	Title	Salary
1/3/49	Mrs. Ida C. Sutphin	Cafeteria Helper	\$2,020.00
1/4/49	Jane Frances Hammil	Cafeteria Helper	2,020.00

Approved unanimously.

Memorandum dated January 3, 1949, from Mr. Bethea, Director of the Division of Administrative Services, recommending increases

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in the basic annual salaries of the following employees in that Division, effective January 9, 1949:

<u>Name</u>	<u>Title</u>	<u>Salary Increase</u>	
		<u>From</u>	<u>To</u>
Evelyn M. Buckles	Clerk	\$2,086.00	\$2,152.00
Fannie L. Mock	Elevator Operator	2,086.00	2,152.00

Approved unanimously.

Memorandum dated January 3, 1949, from Mr. Bethea, Director of the Division of Administrative Services, recommending that the resignation of Mrs. Mary Ethel Canter, a cafeteria helper in that Division, be accepted to be effective, in accordance with her request, at the close of business December 31, 1948, with the understanding that a lump sum payment would be made for annual leave remaining to her credit as of that date.

Approved unanimously.

Letter to Mr. Douglas, Vice President of the Federal Reserve Bank of New York, reading as follows:

"In view of the circumstances described in your letter of December 31, 1948, the Board of Governors approves for a further period of six months beginning January 16, 1949, the payment of salary to Mr. Joseph C. Auchter as Supervisor, New Jersey and Connecticut Section, Transit Division, Check Department, at the rate of \$5,585, per annum, which is \$185 in excess of the maximum for the grade in which the position is classified."

Approved unanimously.

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

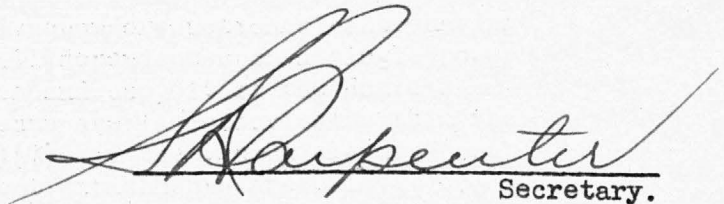
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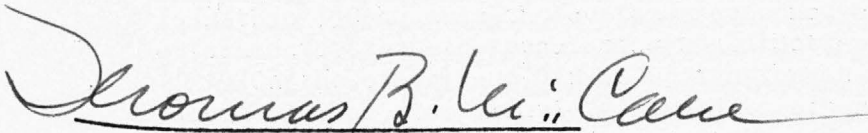
"Reference is made to your letter of December 20, 1948, submitting the request of the Worcester County Trust Company, Worcester, Massachusetts, for approval of the establishment of a branch in Southbridge, Massachusetts, in connection with the proposed absorption of the Southbridge National Bank, Southbridge, Massachusetts.

"In view of your recommendation, the Board of Governors approves the establishment and operation of a branch in Southbridge, Massachusetts, by the Worcester County Trust Company, Worcester, Massachusetts, provided the proposed absorption of the Southbridge National Bank is effected substantially in accordance with the terms and conditions of the purchase agreement submitted and the prior approval of the appropriate State authorities is obtained; and with the understanding that Counsel for the Reserve Bank will review and satisfy himself as to the legality of the steps taken to effect the absorption and establish the branch."

Approved unanimously.


Secretary.

Approved:


Chairman.