

Minutes of actions taken by the Board of Governors of the Federal Reserve System on Tuesday, April 25, 1950. The Board met in the Board Room at 10:35 a.m.

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

Mr. Carpenter, Secretary  
 Mr. Sherman, Assistant Secretary  
 Mr. Kenyon, Assistant Secretary  
 Mr. Morrill, Special Adviser  
 Mr. Thurston, Assistant to the Board  
 Mr. Riefler, Assistant to the Chairman  
 Mr. Thomas, Economic Adviser to the Board  
 Mr. Vest, General Counsel  
 Mr. Millard, Director, Division of  
 Examinations  
 Mr. Townsend, Solicitor to the Board  
 Mr. Young, Director, Division of  
 Research and Statistics  
 Mr. Myrick, Assistant Director, Division  
 of Bank Operations  
 Mr. Youngdahl, Chief, Government Finance  
 Section, Division of Research and Statistics

Mr. Thomas reported on recent developments in the money and Government securities markets.

Mr. Youngdahl withdrew from the meeting at this point.

Mr. Szymczak made a statement substantially as follows:

"Pursuant to the understanding at the meeting on April 16, 1950, I arranged to have Mr. Shepard, Chairman, and Mr. Peyton, President, of the Minneapolis Bank meet me in Chicago on Thursday, April 21, to discuss the Towle matter. During our conversation President Peyton expressed the view that the Board was not aware of the feelings of the directors of the Helena Branch with respect to Mr. Towle and of the importance of the matter to the Federal Reserve System. Mr. Peyton indicated

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"that the Helena Branch directors felt that no action should be taken either by the directors of the Minneapolis Bank or by the Board to censure or punish Mr. Towle for his actions. I reviewed the matter thoroughly with Chairman Shepard and President Peyton and in the course of the discussion mentioned that while it was the strong feeling of the Board that Mr. Towle should be requested to retire at once, if in the judgment of the Minneapolis Bank directors such retirement should be deferred to the end of this year the Board probably would agree to Mr. Towle's serving to the end of his present term. Both Chairman Shepard and Mr. Peyton indicated this would be a good arrangement and suggested that the matter be reviewed again at the end of the year, to which I responded that the arrangement should be definite and without any understanding as to a further review at the end of the year."

Mr. Szymczak also suggested that no formal action by the Board was necessary at this time and that no letter be sent to Chairman Shepard, inasmuch as he and President Peyton had indicated they would present the matter along lines of the foregoing discussion at the joint meeting of the Minneapolis and Helena directors to be held on Friday, April 28, at which action in the matter was to be taken by the directors.

Mr. Szymczak's suggestion  
was approved unanimously.

Mr. Carpenter referred to the discussion at the meeting of the Board on February 27, 1950, at which he reported that Mr. Maloney, a member of the Investigating Staff of the House Committee on Appropriations, had called him to say that the Committee had

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decided to look into the various fiscal agency functions performed by the Federal Reserve Banks for the Treasury and other Government agencies for the purpose of determining whether any of these functions should be performed by the agencies themselves. He said that, following Mr. Maloney's first telephone call, Mr. Bartelt, Fiscal Assistant to the Secretary of the Treasury, had been advised that when the staff met the first time with Mr. Maloney, the suggestion was made that he also confer with Mr. Bartelt about the matter, which he did. Mr. Carpenter also said that subsequently certain information with respect to the nature and cost of fiscal agency functions performed by the Federal Reserve Banks was furnished to Mr. Maloney and that he visited the Federal Reserve Banks of New York, Philadelphia, and Chicago for the purpose of observing the fiscal agency activities carried on at these banks.

On Thursday, April 20, 1950, Mr. Carpenter stated, Mr. Maloney met with members of the Board's staff again at which time he introduced two of his assistants who had been assigned to do the necessary investigating work in connection with the study and it now appeared that the matter had progressed to a point where it seemed desirable to advise the Federal Reserve Banks formally of the matter and to this end the staff proposed, with the approval of the Board, to suggest informally to Mr. Maloney that the Chairman

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of the House Committee on Appropriations send a letter to the Board stating the scope and purpose of the study. Mr. Carpenter went on to say that the staff had kept in touch with Mr. Bartelt in connection with all developments in this matter and would continue to do so.

The procedure proposed by Mr. Carpenter was approved unanimously.

Chairman McCabe stated that, in accordance with the understanding at the meeting of the Board on March 16, 1950, he had discussed with Mr. Staats, Executive Assistant Director of the Bureau of the Budget, the reasons for the Board's view why the Administrative Services Act and the Reorganization Plan No. 18 submitted to the Congress by the President on March 13, 1950, should not be regarded as being applicable to the Board of Governors. Mr. Staats responded, Chairman McCabe said, that it was his impression that it was not intended that the Board should be covered by either the Act or the Reorganization Plan, but that he would look into the matter immediately and advise whether any other view was held at the Bureau of the Budget.

Chairman McCabe also said that during the conference with Mr. Staats, the latter expressed a very high regard for the quality of the work done by the Board's staff and stated that the Bureau of

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the Budget was undertaking to prepare budget forecasts for a period of five years and that he would appreciate it if the Bureau could have the assistance of the Board's staff in that task. The Chairman added that he had told Mr. Staats that the Board would be glad to cooperate in the matter in any way it could.

A further matter discussed with Mr. Staats, Chairman McCabe stated, concerned recent developments in connection with the bank holding company bill proposed by the Board. He said he outlined to Mr. Staats how the Board had endeavored to get the views of other interested Government agencies and to reach an agreement on the legislation before it was submitted to the Committees, that these agencies had failed to make their views known, but that after the bills had been introduced, the views of the agencies in opposition to the legislation were presented for the first time during hearings on the bill. He added that he emphasized to Mr. Staats the difficulties presented by such a situation in getting adequate consideration of legislation by the Congress and discussed how such situations might be avoided in the future.

Chairman McCabe also referred to the reduction from 4-1/2 to 4-1/4 per cent in the interest rate on Federal Housing Adminis-

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tration insured mortgages which became effective yesterday. In that connection he read a letter which he had written to Mr. Foley, Administrator of the Housing and Home Finance Agency under date of April 20, 1950, in the absence of other members of the Board, expressing the personal view that the reduction should not be made. It was understood that a copy of Chairman McCabe's letter would be sent to each member of the Board.

Mr. Thurston stated that when he was in Nashville, Tennessee, last week he called to see Mr. Silliman Evans, publisher of The Nashville Tennessean, in connection with Mr. Evans' protest regarding the action of Mr. Fort, Vice President in charge of the Nashville Branch of the Federal Reserve Bank of Atlanta, in writing a letter endorsing a candidate in a local political election. Mr. Thurston stated that Mr. Evans was in Washington but that he talked with Mr. Nye, editor of the paper, who indicated that he considered the matter closed. Mr. Thurston went on to say that this morning he received a telephone call from Mr. Evans who was still in Washington, and who raised the question whether the Board would object to his publishing its letter of April 19, 1950, to Senator Maybank on the subject. Mr. Thurston added that while he would prefer that the letter not be published, he would like to see the matter disposed of and that publication of the letter by Mr. Evans might be the best way to accomplish that result.

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Chairman McCabe suggested that Mr. Thurston call Mr. Evans and advise him that the publication of the letter was a matter entirely in his hands and on which he would have to make his own decision.

This suggestion was approved unanimously.

Question was then raised whether a letter should be sent to all Federal Reserve Banks informing them of the substance of the incident so that they might take any steps that were appropriate to prevent a similar occurrence at another Federal Reserve Bank.

It was agreed unanimously that the Secretary should prepare for the consideration of the Board a draft of such a letter to the Federal Reserve Banks.

Chairman McCabe stated that, in a telephone conversation yesterday with Mr. Lyon, Secretary of the National Association of Supervisors of State Banks, he (Chairman McCabe) raised the question whether the executive committee of the Association which was to have luncheon with the Board on Thursday, April 27, 1950, would be interested in listening to a guest speaker following the luncheon. Mr. Lyon responded, Chairman McCabe said, that the members of the committee would prefer to meet informally with the Chairman for the purpose of discussing matters in which they were interested. Chairman McCabe said that he had informed Mr. Lyon that he would be glad to comply with the wishes of the committee. He also said

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that, in the absence of objection, he would meet with the committee following the luncheon.

Chairman McCabe stated that he had been informed that Senator Robertson's Subcommittee of the Senate Banking and Currency Committee met in executive session earlier today and, on a three to two vote, sent to the printer the substitute bank holding company bill which had been prepared in the Office of the Comptroller of the Currency, with the understanding, however, that the substitute bill would be discussed at a meeting of the subcommittee next week at which time some of the amendments proposed by the Board would be considered.

There followed a discussion of the question whether the Board should communicate with any of the members of the subcommittee and Mr. Vardaman stated that he felt no further action by the Board was necessary or desirable inasmuch as it had clearly stated its position with respect to the legislation at the time S. 2318 was introduced and during the subsequent hearings. Other members of the Board agreed with Chairman McCabe's suggestion that he discuss the matter with Senator Flanders and it was understood that he would do so.

Mr. Vest stated that the Senate had passed a bill, S. 3105, to provide additional funds for construction of branch buildings of Federal Reserve Banks, the amount of the authorization having been



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reduced from \$15 million as recommended by the Board to \$10 million, with a restrictive provision that such buildings be of simple design, and that their construction be undertaken only when urgently needed for the efficient and economical operation of the branch, with due regard for the local unemployment situation. Mr. Vest also raised the question whether Chairman Spence of the House Banking and Currency Committee who had introduced a bill in the form originally proposed by the Board should be requested to change the bill to the form passed by the Senate, or whether he should be advised that the Board would prefer the bill in its original form.

This question was discussed and it was agreed that Chairman McCabe should call Chairman Spence on the telephone and say to him that the Board preferred the bill as first introduced, if he thought it could be enacted in that form; but that the Board was prepared to defer to his judgment on the question whether the legislative situation was such that it would be desirable to try to get the unamended form or whether it would be preferable merely to take the bill in the form passed by the Senate.

At this point all of the members of the staff with the exception of Messrs. Carpenter, Sherman, and Kenyon withdrew, and the action stated with respect to each of the matters hereinafter referred to was taken by the Board:

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Minutes of actions taken by the Board of Governors of the Federal Reserve System on April 24, 1950, were approved unanimously.

Mr. Carpenter reported that the Comptroller of the Currency would issue a call on April 27, 1950, on all national banks for reports of condition as of the close of business on April 24, 1950, and that, in accordance with the usual practice and the Board's letter of March 21, 1950, a call would be made on April 27 on behalf of the Board of Governors of the Federal Reserve System on all State member banks for reports of condition as of April 24, 1950.

The call to be made on behalf of the Board on April 27, 1950, was approved unanimously.

Letter to Mr. Williams, President of the Federal Reserve Bank of Philadelphia, reading as follows:

"The Board approves the payment of salary to you as President at the rate of \$25,000 per annum and to Mr. W. J. Davis as First Vice President at the rate of \$18,000 per annum for the period May 1, 1950, through February 28, 1951, the date the statutory terms of office for these positions will expire. According to your letter of April 20, 1950, these are the rates which were fixed by the Board of Directors.

"The Board of Governors also approves the payment of salary to the following officers at the rates indicated, which, according to your letter of April 20, 1950, are the rates fixed by the Board of Directors, for the period May 1, 1950, through April 30, 1951.

<u>Name</u>	<u>Title</u>	<u>Annual Salary</u>
Philip M. Poorman	Vice President & Cashier	\$15,000
Ernest C. Hill	Vice President	15,000

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"Wm. G. McCreedy	Vice President & Secretary	\$14,000
Karl R. Bopp	Vice President	14,000
Robert N. Hilkert	Vice President	13,000
Leonard E. Donaldson	Vice President	13,000
James V. Vergari	Counsel & Asst. Secretary	12,000
Wallace M. Catanach	Asst. Vice President	9,500
Richard G. Wilgus	Asst. Vice President & Asst. Secretary	9,000
Norman G. Dash	General Auditor	9,000
Roy Hetherington	Asst. Cashier	7,000
Henry J. Nelson	Asst. Cashier	6,200
Edward A. Aff	Asst. Cashier	5,500
Ralph E. Haas	Asst. Cashier	5,500"

Approved unanimously.

Letter to Mr. Gidney, President of the Federal Reserve Bank of Cleveland, reading as follows:

"This refers to your letter of March 10, 1950, and its enclosure, regarding a proposal made by the Legislative Committee of the Cleveland Clearing House Association with respect to the classification as time deposits for reserve purposes of a certain portion of commingled deposits of trust funds made by the trust department of a member bank in its own banking department.

"As you know, representatives of the Cleveland Clearing House Association met with members of the Board's staff in Washington on March 28, 1950, and explained the reasons which have prompted them to make this proposal. The Board has given careful consideration to the arguments advanced by them at that meeting, as well as those stated in the letter addressed to you on March 9, 1950, by Mr. L. F. Laylin, Chairman of the Association's Legislative Committee. Consideration has also been given to the alternative proposal made by Mr. R. S. Douglas, counsel for the Cleveland Trust Company, in his letter to the Board's General Counsel dated April 5, 1950.

"It is understood that the principal objective

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"of the proposal made by the Cleveland Clearing House Association is the elimination of the requirement prescribed in the Board's ruling of December 19, 1949 that, in order for a commingled deposit of trust funds to be considered a time deposit for reserve purposes, there must be a written agreement between the trust and banking departments of a member bank with respect to notice of withdrawal of funds from such deposit.

"It has been proposed, therefore, that the Board of Governors amend its Regulation D so that a certain portion of trust funds deposited in the banking department, to be determined on a reasonable basis or under a fixed formula, might be given a time deposit status for reserve purposes notwithstanding the absence of an agreement between the banking and trust departments of the bank restricting withdrawals of funds from such deposit. As an alternative means of accomplishing the objective of the proposal, Mr. Douglas has suggested in his letter to the Board's General Counsel that the Board's ruling of December 19, 1949, might be modified in order to make it possible for deposits of trust funds in accordance with that ruling to be considered time deposits without the necessity for any written agreement between the two departments of the bank.

"The Board's ruling of December 19, 1949, required that the deposit of trust funds on a time basis shall be subject to a written agreement between the trust department and the banking department which complies with the requirements of one of the regulatory definitions of time deposits. For example, a deposit of such funds in a time deposit, open account, would be required to be subject to an agreement providing for not less than thirty days' written notice prior to any withdrawal. This requirement, however, was not, and was not intended to be, a new restriction; it was the intent of the Board's ruling merely to make it clear that time deposits of trust funds should comply with requirements applicable to other types of time deposits.

"As you know, a requirement restricting withdrawals has always been an essential element of the definition of a time deposit. The elimination of this requirement as now suggested with respect

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"to time deposits of trust funds would tend to break down one of the most important distinctions between time and demand deposits. Bearing in mind the favored status given time deposits under the law, the Board feels that the proposed action on the part of the Board, even if legally permissible, would be undesirable as a matter of general policy.

"While it may be contended that a deposit of trust funds on the basis here proposed would in effect constitute a time deposit because it is contemplated that funds placed in the deposit will not be withdrawn for at least thirty days, the deposit would appear in legal effect to be payable on demand, since there would be no agreement limiting withdrawals. It is true that the Board is authorized by section 19 of the Federal Reserve Act to define the term 'time deposits' for the purposes of that section; but it seems questionable whether Congress intended that the Board's discretion should be such as to permit it to define as a time deposit one which is legally payable on demand. This question would be accentuated if it should be deemed necessary to make a similar amendment to Regulation Q, in view of the statutory prohibition upon the payment of interest on deposits payable on demand.

"In its ruling of December 19, 1949, the Board recognized that whether the trust department of a member bank might properly deposit commingled trust funds on a time basis in its own banking department is necessarily affected by applicable provisions of State law relating to trust administration; and it was for this reason that the ruling required that a member bank should be satisfied that any such practice is not inconsistent with State law or with the terms of any applicable trust instrument or court order. It was appreciated that there might be States in which the statutory or other law might be such that the practice would not be permissible.

"For the reasons indicated, the Board feels that it cannot properly take the action requested by the Cleveland Clearing House Association; and it will be appreciated if you will transmit to the Association a copy of this letter."

Approved unanimously.

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Letter prepared for the Chairman's signature to Honorable Brent Spence, Chairman, Banking and Currency Committee, House of Representatives, Washington 25, D. C., reading as follows:

"This refers to your letter of March 30, 1950, in which you asked for our reaction to a letter you received from your colleague, the Honorable Robert W. Kean, of New Jersey, with reference to section 32 of the Banking Act of 1933. Mr. Kean's letter was prompted by the fact that it was necessary for him to resign in 1949 as President and Director of Livingston National Bank, Livingston, New Jersey, because he was a partner in Kean, Taylor & Co., New York, New York, an investment firm which the Board regarded as being primarily engaged in the underwriting and distribution of securities within the meaning of section 32.

"As you will recall, section 32 is one of several provisions of the Banking Act of 1933 designed to prevent a recurrence of abuses which had resulted from close relationships between banks and securities firms and which were a matter of major concern to the Congressional committees studying needed reforms in banking legislation in the early 1930's. Section 32 provides, in part, that no partner in a partnership 'primarily engaged' in the underwriting and distribution of stocks, bonds, and other similar securities shall serve at the same time as an officer or director of a member bank, except in limited classes of cases in which the Board may allow such service by general regulations when in the judgment of the Board it would not unduly influence the investment policies of the member bank or the advice it gives its customers regarding investments. As originally enacted, section 32 authorized the Board to issue permits in individual cases; but in a revision of that section in 1935, this impractical permit procedure was eliminated by Congress and the provision for exceptions by general regulations was substituted.

"In its administration of section 32, the Board

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"consistently held that a firm might be 'primarily engaged' in the underwriting and distribution of securities even though such activities constituted less than 50 per cent of the firm's business. In Board of Governors vs. Agnew, 329 U. S. 441, decided in 1947, the United States Supreme Court agreed with this view and went on to construe the term 'primarily engaged' as though it read 'substantially engaged'. The Court's opinion read in part as follows:

\* \* \* It is true that "primary"

when applied to a single subject often means first, chief, or principal. But that is not always the case. For other accepted and common means of "primarily" are "essentially" (Oxford English Dictionary) or "fundamentally" (Webster's New International). An activity or function may be "primary" in that sense if it is substantial. If the underwriting business of a firm is substantial, the firm is engaged in the underwriting business in a primary way, though by any quantitative test underwriting may not be its chief or principal activity. \* \* \*

\* \* \* Firms which do underwriting also engage in numerous other activities. The Board indeed observed that, if one was not "primarily engaged" in underwriting unless by some quantitative test it was his principal activity, then section 32 would apply to no one. Moreover, the evil at which the section was aimed is not one likely to emerge only when the firm with which a bank director is connected has an underwriting business which exceeds 50 per cent of its total business. Section 32 is directed to the probability or likelihood, based on the experience of the 1920's, that a bank director interested in the underwriting business may use his influence in the bank to involve it or its customers in securities which his underwriting house has in its portfolio or has committed itself to take. That likelihood or probability does not depend on whether the firm's underwriting business exceeds

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"50 per cent of its total business. It might, of course, exist whatever the proportion of the underwriting business. But Congress did not go the whole way; it drew the line where the need was thought to be the greatest. And the line between substantial and unsubstantial seems to us to be the one indicated by the words "primarily engaged."

"As a result of the Supreme Court's decision, the Board instituted a review of all cases in which there was a possibility that section 32 might be applicable; and one of these cases was that involving Mr. Kean. On the basis of the facts supplied to us, and after a discussion of the matter with Mr. Kean, the Board concluded that Kean, Taylor & Co. was primarily engaged in the underwriting and distribution of securities within the meaning of section 32 as construed by the Supreme Court. In this connection, we also made a thorough review of the administration of section 32 and considered various amendments to our regulation on this subject which would make an exception covering Mr. Kean's case. We were unable, however, to devise any such exception which, when applied generally, would be both practical to administer and consistent with the purposes of the law and the Board's responsibilities under it.

"It is our feeling that the Supreme Court's interpretation of section 32 is reasonable in the light of the language used and the purposes intended to be accomplished; and, in any event, we must endeavor to apply the law in accordance with that interpretation. Mr. Kean, however, believes that section 32 has been construed to have a broader application than Congress intended and he suggests, therefore, that the law be amended to define the term 'primarily engaged' so as to give it a more restricted meaning. It would be much easier for us to administer section 32 if it contained a precise definition but, from our experience, we think that it would be difficult to devise a definition which would give proper weight to all pertinent considerations and prove satisfactory



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"when applied to varied factual situations.

"Mr. Kean apparently has in mind a definition under which a firm would not be 'primarily engaged' in the underwriting and distribution business unless its business of that nature exceeded a stated percentage of its aggregate business (presumably from the standpoint of either volume or earnings). It seems clear to us that a definition based solely upon this relationship would not be satisfactory. Under such a definition, it would be possible for leading firms in the underwriting and distribution business to avoid being classified as 'primarily engaged' in that business because of the large amount of other business handled by them. Hence, it would seem essential for any definition to take into consideration the amount of the underwriting and distribution business of a firm regardless of its relationship to the firm's other business; and there are other factors which might be considered significant.

"As an alternative to defining the term 'primarily engaged', Mr. Kean suggests that section 32 might be amended to provide an exception with respect to the underwriting and distribution of so-called 'exempt securities' (mainly Government, State, and municipal securities) in which member banks are permitted to deal pursuant to section 5136 of the Revised Statutes. The Board has by regulation exempted interlocking relationships between banks and securities firms which are not dealing in any securities except Government securities. In connection with Mr. Kean's case, and on other occasions, the Board has considered whether it should broaden this exemption to cover interlocking relationships with firms dealing only in municipal securities; but, in view of the difficulties which have been experienced in the past with low-grade municipal securities and the danger that interlocking relationships might be used to enable securities firms to unload such securities on member banks and their customers, the Board has not felt that it could justify such action under the authority vested in it by section 32.

"We recognize, however, that an argument can be made in support of an amendment to section 32, as suggested by Mr. Kean, which would make an exception

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"for interlocking relationships between banks and securities firms which are dealing in the types of securities which member banks are permitted to underwrite and distribute. The amendment might take either of two forms: (1) It might exempt interlocking relationships with securities firms which do not underwrite or distribute any securities other than such 'exempt securities'; or (2) it might exempt interlocking relationships with securities firms which are not primarily engaged in underwriting or distributing securities other than such 'exempt securities'. As stated above, the Board on several occasions in the past has concluded that such an exemption by regulation would not be justified, and an amendment to the law for this purpose would seem to be open to similar objections. Accordingly, the Board is not prepared to recommend such an amendment, but it would, of course, be glad to be of any possible assistance in preparing a draft of an amendment if you should so desire.

"In considering any amendment to section 32, it should be borne in mind that that section is directed at relationships which present the opportunity for abuses regardless of whether such abuses are actually present in particular cases. The Supreme Court commented upon this fact in Board of Governors v. Agnew, as follows:

'Section 32 is not concerned, of course, with any showing that the director in question has in fact been derelict in his duties or has in any way breached his fiduciary obligation to the bank. It is a preventive or prophylactic measure. The fact that respondents have been scrupulous in their relationships to the bank is therefore immaterial.'

"Legislation of this nature inevitably produces some instances of apparent hardship where, because of the character of the persons involved or other circumstances of the particular cases, there is no reason to believe that any harm will result from the prohibited relationships. A number of cases of this kind have come to our attention but this fact alone does not justify an amendment to the law; and

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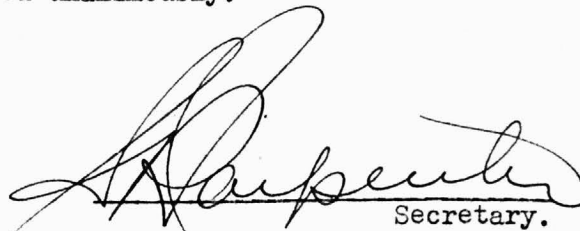
"if section 32 is to be retained and is to be effective, there will be some hardship cases regardless of the manner in which it may be amended.

"Since the receipt of your letter, we have had some further discussion of this matter with Mr. Kean and we are sending him a copy of this letter."

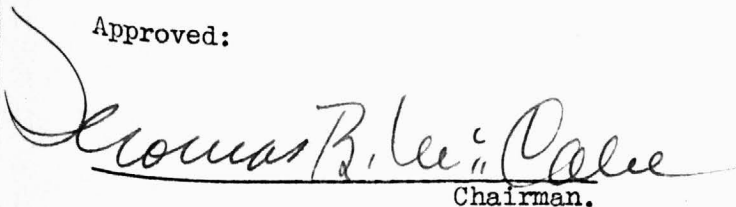
Approved unanimously.

Memorandum dated April 21, 1950, from Mr. Townsend, Solicitor to the Board, recommending that Dr. E. A. Goldenweiser be reimbursed the sum of \$530.50 for his travel expenses from Princeton, New Jersey to San Francisco, California, in connection with the Clayton Act proceeding against the Transamerica Corporation.

Approved unanimously.

  
Secretary.

Approved:

  
Chairman.