

Minutes of actions taken by the Board of Governors of the Federal Reserve System on Monday, May 21, 1951.

PRESENT: Mr. Martin, Chairman
 Mr. Szymczak
 Mr. Evans
 Mr. Vardaman
 Mr. Powell

Mr. Carpenter, Secretary
 Mr. Sherman, Assistant Secretary
 Mr. Kenyon, Assistant Secretary

Minutes of actions taken by the Board of Governors of the Federal Reserve System on May 18, 1951, were approved unanimously.

Minutes of the meeting of the Board of Governors of the Federal Reserve System with the Presidents of the Federal Reserve Banks held on May 18, 1951, were approved unanimously.

Memorandum dated May 18, 1951, from Mr. Sloan, Assistant Director of the Division of Examinations, recommending that the Board approve an advance of funds in the amount of \$1,000 to Glenn M. Goodman, Federal Reserve Examiner in that Division, in connection with his forthcoming approved trip to Europe. The memorandum stated that Mr. Goodman had sufficient accrued annual leave to provide security for the advance.

Approved unanimously.

Letter to the Honorable A. Willis Robertson, United States Senate, Washington, D. C., reading as follows:

"This letter is in response to yours of May 1 in which you ask for any suggestions with respect to amendments that might be made to the Federal Reserve Act which would permit the Federal Reserve System to provide financial aid to small business in normal times.

"The use of the private banking system should be encouraged in the financing of small business enterprises whether the need is for current working capital or for

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"longer term funds. The Reserve Banks are qualified to assist local banks in making credit available to borrowers, who, though otherwise meritorious, may present credit risks of a character which banks will not ordinarily accept; and, by such aid, the Reserve Banks could help to restore and maintain normal credit relationships between such borrowers and the banks. However, the Reserve Banks have been handicapped in carrying out such a function by the restrictive provisions of section 13b of the Federal Reserve Act. Under present law they may make commitments and loans only for working capital purposes, only to 'established' businesses, and only with maturities not exceeding 5 years. These limitations make it difficult to render effective assistance in meeting the requirements of smaller businesses.

"One method of utilizing the services of the Federal Reserve System more effectively in the extension of financial assistance to small business in normal times would be to authorize the Reserve Banks to enter into participations and commitments with financing institutions with respect to loans made to business enterprises, on a basis under which a Reserve Bank might assume not more than 90 per cent of the risk involved and under which loans would not be limited solely to working capital purposes or restricted to 'established' businesses. The maximum maturity on any such loan should be fixed at ten instead of five years. The local bankers, of course, should assume as much of the risk as possible. If your Committee should so desire, the Board will be glad to submit draft amendments to carry into effect changes of this kind.

"Another method of dealing with the problem is incorporated in a bill (S. 1329) introduced in the present session of the Congress which would amend the Federal Reserve Act to provide for the creation of investment companies to aid in meeting the financing needs of small business. Hearings were held on similar legislation in June of last year.

"Some changes in the law such as those mentioned above would be appropriate for consideration in more normal times as means to aid in the financing of business enterprises. As you know, however, because of the great inflationary pressures resulting from the defense emergency, a variety of measures are being taken, especially

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"by the Federal Reserve System, to discourage any extensions of credit that are not essential for defense. In the circumstances, we feel that there is serious question as to the advisability of changes in the law at this time that would provide additional authority for the expansion of the use of credit, even by small businesses, for any purposes that are not closely related to defense needs.

"Recently the Senate Banking and Currency Committee requested the views of the Board on S. 515, a bill to amend the Reconstruction Finance Corporation Act. In response to that request, the Board expressed the view that any credit necessary for the national defense and for other purposes should be made available to the fullest extent possible through private credit channels and that in the exceptional cases in which Government assistance may be required guarantees of loans by private institutions are more desirable than direct Government loans. The reply also stated that if the powers of the Reconstruction Finance Corporation to make direct loans were to be continued they should be in such form as to require that loans be made only in the exceptional cases in which credit is not available from other sources and that the Reconstruction Finance Corporation, which was organized in 1932 as an emergency organization, should continue to be essentially so regarded."

Approved, Mr. Vardaman
not voting.

Letter to the Honorable Lyndon B. Johnson, Chairman, Preparedness Subcommittee, Committee on Armed Services, United States Senate, Washington, D. C., reading as follows:

"In your letter of April 4 you stated that in connection with the performance of its duties, which include a continuous study of all policies, programs, activities, operations, facilities, requirements and practices of the Department of Defense, the Armed Services and other agencies exercising functions relating to them, and the administration thereof in all respects, the Preparedness Subcommittee is engaging upon a study of the particular tasks assigned to each entity in the mobilization structure and

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"the methods and procedures employed in carrying out the assigned tasks. In this connection, you requested certain information regarding functions of a defense character being performed by the Board of Governors.

"In answer to your request there is set forth in the attached statements and enclosures information with respect to the guaranteed loan program (Regulation V), the regulation of consumer credit (Regulation W), the regulation of real estate credit (Regulation X), and the voluntary credit restraint program. In addition, the Subcommittee has been placed on our mailing list to receive all publications and releases distributed by the Board relative to these functions.

"We trust that the information given herewith will serve the purposes of your Subcommittee and we will be glad to furnish additional information as requested."

Approved unanimously.

Letter for the signature of the Chairman to Mr. A. E. Barit, President and General Manager, Hudson Motor Car Company, Detroit, Michigan, reading as follows:

"Thank you for your informative letter of May 8 on the subject of Regulation W and particularly the effect of the present instalment credit restrictions on your sales.

"The Board has felt that relatively strict terms are appropriate for instalment credit under the regulation at this time in view of the strong inflationary pressures now present in the economy. While we are very much concerned that the regulation not be excessively restrictive in the case of individual businesses or industries, the Board feels, nevertheless, that the regulation must provide a definite curb on instalment credit if it is to be effective in this period of national emergency. Although supply and demand conditions in markets for the specific regulated articles such as automobiles are one factor to be considered in setting the terms of Regulation W, the Board must also consider the economic and credit conditions in the economy as a whole.

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"We are glad to have your observations on the effect of Regulation W on current new and used car sales. As you point out, published statistics on the industry generally appear weeks after the developments they reflect. However, the Board's staff watches developments in the automobile markets closely and, as you know, certain sales, production, and inventory data are available to us somewhat earlier than are the usual published figures. It appears to us, and I believe you will agree, that a number of factors other than the credit regulations have also been influencing the current volume of automobile sales.

"You refer to the claim made by some dealers that the sale of used cars does not involve the use of critical materials or manpower. This is of course true. The expansion of instalment credit for the purchase of used cars, if this credit were not regulated, would, however, contribute to an inflationary increase in demand for articles that do use critical materials. Any increase in demand for used cars would tend to spread to the demand for new cars either directly or via the trade-in. Moreover, any expansion of credit buying encouraged by easier credit terms would tend to circulate throughout the economy in the form of larger demand for all consumer goods.

"I appreciate your interest in writing to us. You may be assured that your views will be considered in our continuing study of the effect of the regulation. Regulation W is a flexible instrument and the Board will be prepared to modify its terms promptly when such action appears to be in the interests of the national defense program."

Approved unanimously.

Letter to the Honorable Olin D. Johnston, United States Senate, Washington, D. C., reading as follows:

"Mr. Raymond M. Foley, Administrator, Housing and Home Finance Agency, has referred to us a letter addressed to you by the Honorable R. Aubrey Harley, Attorney-at-Law, Newberry, South Carolina, concerning Regulation W. Mr. Harley's letter has reference to the difficulties of some home owners in Newberry in meeting the terms of Regulation W applicable to home improvement credit.

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"In drafting the present regulation, a considerable amount of research and study preceded the setting of terms in the home improvement area. The required terms in other regulated areas provide for minimum down payments of 33 1/3 per cent in the case of automobiles, 25 per cent for major household appliances, and 15 per cent for furniture, with maximum maturities of 15 months in all three classes of goods. The down payment requirement of 10 per cent and the 30 months maturity permitted in the case of home improvements, of course, reflect a wide differential.

"These relatively lenient requirements were adopted in recognition of the possibility that such terms might be needed for necessitous home repairs. The fact that a large majority of home repairs and improvements do not exceed \$500 to \$800 (monthly payments of approximately \$15 to \$25) led the Board to believe that the more lenient terms would not render compliance unduly burdensome in the light of the purpose of the regulation to restrain the use of consumer credit. In this regard it may be noted that when the regulation became effective, the terms of entitlement to FHA insurance of credit for home repairs included a 10 per cent down payment and a maximum maturity of 36 months.

"The practicability of some change in the regulation in this connection has been and continues to be the subject of study by the Board's staff, and we appreciate receiving the information contained in Mr. Harley's letter. The letter is returned herewith for your files."

Approved unanimously.

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

"For the confidential information of yourself and your staff in connection with the administration of Regulation W there is enclosed a copy of correspondence between the firm of Canfield, Schell, Hannan & Castiello, Washington, D. C., and the Board.

"This is being forwarded to you because of its close similarity to certain problems which have arisen in the San Francisco Federal Reserve District and which may arise in other districts.

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"In 1948 and 1949, Kelley Kar Company, Los Angeles, California, attempted to use a number of different devices that conflicted with the spirit and often the letter of Regulation W. One device was to purport to include in the sale of an automobile a contract for greasing and servicing the car, with the alleged charge for such greasing and servicing to be paid in the months following the maturity permissible under Regulation W. Another device was to include a purported contract for the sale of gasoline, with the cost to be collected in instalments after the permissible maturity. Another device was to attempt to treat insurance on the automobile in this manner rather than including it in the time balance.

"The Registrant attempted to justify such practices under the mixed-credit provisions of the regulation. The devices were coupled with advertising that, at least on first reading, appeared to offer maturities for the actual cost of the car beyond those permissible under the regulation. The practices caused great confusion among the industry and for a time threatened to disrupt the operation of the regulation in the area.

"The Board through the Federal Reserve Bank of San Francisco advised the Kelley Kar Company that the practices were forbidden by the regulation. The company has presented the same or similar questions to the Federal Reserve Bank of San Francisco under the present regulation and has requested references to Federal Register citations of any interpretations forbidding these practices. They have been reminded of the previous rulings on the specific points, have been advised that published interpretations, particularly the summary interpretations numbered 9 and 10 at pages 1615 and 1616 of the December 1950 Federal Reserve Bulletin (15 Fed. Reg. 7827) cover these matters generally, and have been reminded that in any event the Kelley Kar Company is on notice of the specific interpretations.

"The questions and even phrasing of the inquiry from Canfield, Schell, Hannan & Castiello are closely similar to those from Kelley Kar Company.

"It is believed that this situation is a relatively unusual one which is not likely to be duplicated in other districts, or with respect to other listed articles, but it seems advisable that you have this background material for your confidential information."

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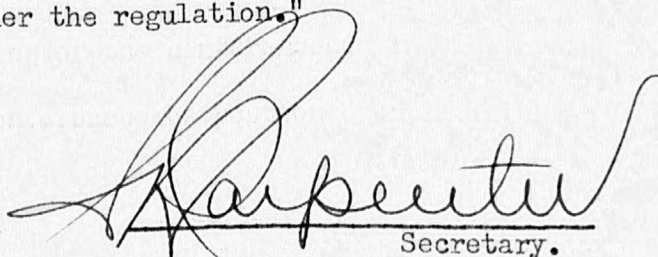
Approved unanimously, together with a letter to Mr. S. D. Schell, Canfield, Schell, Hannan & Castiello, Suite 637, Woodward Building, Washington, D. C., reading as follows:

"This refers to your letter of May 10, 1951, and its enclosures, concerning Regulation W.

"The questions submitted by you are set out in some detail, but it is not clear whether they arise from particular situations or merely as a matter of general interest. Definite answers to questions such as those you asked necessarily depend upon all of the relevant circumstances of a given case.

"Interpretative materials concerning the application of the regulation have been published, both in the Federal Reserve Bulletin and in the Federal Register. Since the present regulation became effective September 18, 1950, the interpretative material will be found in those two sources since that date. The questions as outlined in the enclosures with your letter appear to be answered, not only by the language of the regulation itself, but also by the general principles set forth in the summary-interpretations at section 222.102 (9) and (10), 15 Federal Register 7827, November 17, 1950, and also at pages 1615 and 1616 of the Federal Reserve Bulletin of 1950. The situations outlined by you strongly resemble the specific cases with respect to which the principles cited were stated. In those cases the Board said that the practices involved were not permissible under the regulation.

"The administration of the regulation has been decentralized among the 12 Federal Reserve Banks and their branches. This decentralization normally expedites the handling of specific cases as they arise among those persons who are subject to the regulation. It is suggested, therefore, that you may wish to take up with the Federal Reserve Bank of Richmond, or the Federal Reserve Bank of the district in which the client is located, any specific questions or additional problems that may come to you from your clients under the regulation."



Secretary.