

Minutes of actions taken by the Board of Governors of the Federal Reserve System on Friday, November 4, 1955. The Board met in the Board Room at 11:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Balderston, Vice Chairman
Mr. Mills
Mr. Robertson
Mr. Shepardson

Mr. Carpenter, Secretary
Mr. Sherman, Assistant Secretary
Mr. Kenyon, Assistant Secretary
Mr. Thurston, Assistant to the Board
Mr. Young, Director, Division of Research and Statistics
Mr. Solomon, Assistant General Counsel
Mr. Wood, Economist, Division of Research and Statistics

Pursuant to the understanding at yesterday's meeting of the Board, there had been prepared a revised draft of reply to Representative Patman's letter of October 17, 1955, with regard to provisions of the Internal Revenue Code having to do with the treatment of commercial bank profits and losses on Government securities transactions for tax purposes. Copies of the revised draft had been sent to the members of the Board along with copies of the background statement proposed to be enclosed with the reply. The text of the background statement had been modified in accordance with suggestions made at the meeting yesterday. There had also been distributed copies of an alternative draft of reply in which the only change from the other revised draft was the shifting of the second paragraph to the end of the letter.

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Governor Mills said he felt strongly that the original draft of reply, with minor changes suggested at yesterday's meeting, was the most appropriate type of letter to send. With regard to the suggestion that the background memorandum be transmitted, he commented that the memorandum contained unsolicited information and that it could readily become the basis for a subsequent inquiry as to whether the Board did or did not believe that the present law was appropriate. His reason for favoring so strongly the original draft, Governor Mills said, was that the competent party to answer the question of the appropriateness of the present law would be the authority that administers the tax laws and has responsibility for introducing new laws or challenging amendments to the present law. He felt, therefore, that the letter to Mr. Patman should state, as the original draft did, that since the Treasury has the responsibility for administering the tax laws that are enacted by the Congress, it would seem that any question relating to the broad desirability of a provision of the Internal Revenue Code should be addressed to the Treasury rather than to the Board of Governors.

Governors Balderston, Robertson, and Shepardson indicated that they favored the second of the alternative drafts distributed prior to this meeting. It was recalled that Governor Szymczak had expressed himself as agreeable to the original draft and had taken the position that if revisions were agreed upon, he would favor retaining language which pointed

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out that the Treasury has the responsibility for administering the tax laws that are enacted by the Congress.

In a discussion concerning the question whether to transmit the background memorandum as an enclosure with the reply, it was pointed out that the memorandum contained only factual information which presumably could be obtained by Mr. Patman through his own staff or other sources. It was also stated that the inclusion of the memorandum would demonstrate a desire to cooperate by supplying information which might prove useful and would indicate that appropriate investigation into the field of Mr. Patman's inquiry had been made by the Board since the date of receipt of his letter.

At the conclusion of the discussion, approval was given to a letter from Chairman Martin to Representative Patman reading as follows, Governor Mills voting "no" because of his strong preference for the original draft of reply for the reasons which he had stated:

In your letter of October 17, 1955, you refer to provisions of the Internal Revenue Code relating to the manner in which commercial bank profits and losses on Government securities transactions may be treated for tax purposes, and you ask the Board's views on the desirability of retaining the provision under which banks are permitted to deduct from ordinary income net capital losses on the sale or exchange of bonds and other debt instruments.

You specifically ask whether "tax switches" of securities by banks, which are facilitated by the provisions of the Internal Revenue Code referred to in your letter, in any way conflict with Board policy, say, in a period when the Board is seeking to make it costly for member banks to obtain additional reserves in order to restrain excessive expansion of bank credit. A tax switch for any given bank neither adds to nor takes from the reserves available to that

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bank. Therefore the quantity of reserves which banks would have to use in making credit extensions would not be affected by such tax switches.

If, instead of making a tax switch, a bank reduces its holdings of investment securities, that individual bank would then have additional loanable funds available. The present provisions of the Internal Revenue Code no doubt make some banks less reluctant than they otherwise would be to sell securities on which they have capital losses and shift into other assets. However, if the securities sold are acquired by other banks, the total volume of reserves for the banking system as a whole would not be changed because of the transaction. Sales and purchases of securities by banks are, of course influenced by investment, lending, tax, and other considerations. We have no basis for measuring the extent to which banks may be influenced by tax considerations in their willingness to sell securities.

The tax laws are, of course, enacted by the Congress for a variety of reasons. We have confined our comments regarding the provisions which you mention to their impact on the effectuation of monetary policy. However, in the hope that it may be of some assistance to you, we are enclosing a memorandum giving background information regarding the tax treatment of commercial bank capital gains and losses on Government securities.

The following draft of letter to Mr. Mills, Chief Examiner, Federal Reserve Bank of Kansas City, had been circulated to the members of the Board and was presented for consideration:

In accordance with the request contained in your letter of October 27, 1955, the Board approves the designations of Willard Cable and Walter W. Scott as special assistant examiners for the Federal Reserve Bank of Kansas City for the specific purpose of rendering assistance in the examinations of the Commerce Trust Company, Kansas City, Missouri, and The International Trust Company, Denver, Colorado.

Approved unanimously.

Reference was made to a request from Mr. Sprecher, Assistant Director, Division of Personnel Administration, for authority to travel to

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Minneapolis, Minnesota, and Chicago, Illinois, during the period from November 24 through December 1, 1955, to visit the Personnel Departments of the Federal Reserve Banks of Minneapolis and Chicago. The request contemplated that Mr. Sprecher would spend four days during this period on official business.

Approved unanimously.

There were presented telegrams to the Federal Reserve Banks listed below approving the establishment without change on the dates indicated of the rates of discount and purchase in their existing schedules:

St. Louis	October 31
San Francisco	November 2
New York	November 3
Philadelphia	November 3
Chicago	November 3
Kansas City	November 3

Approved unanimously.

There had been sent to the members of the Board copies of a letter dated October 12, 1955, from Senator Sparkman, Chairman of the Subcommittee on Housing of the Senate Committee on Banking and Currency, in which he referred to a round-table discussion of the residential construction and mortgage financing field which would be held by the Subcommittee on November 28 and 29, 1955, requested that Chairman Martin participate, and that the Subcommittee be supplied with copies of an advance statement on the subject. Copies of a draft of such a statement also had been distributed to the members of the Board.

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Chairman Martin suggested that consideration of the statement be deferred until the meeting on Wednesday, November 9, so that all of the members of the Board would have an opportunity to review the draft carefully. After agreement with this suggestion was expressed, Governor Mills discussed possible changes in two parts of the statement. It was understood that the staff would make revisions in line with Governor Mills' and other suggestions and that copies of a revised draft would be distributed prior to the meeting on November 9.

In this connection it was reported that inquiries had been received from the Treasury Department and the Housing and Home Finance Agency regarding the statement which the Board intended to present, the thought being that some coordination among the agencies would be mutually advantageous. It was agreed that there would be no objection to furnishing appropriate persons in those agencies copies of the current draft of Chairman Martin's statement with the understanding that the draft was not in final form.

Governor Robertson reported receipt of a telephone call from an official of the Farm Credit Administration who stated that a proposal was being considered which would consolidate the Federal Intermediate Credit Banks and the Production Credit Corporations and which, among other things, would involve a change in the name of the Federal Intermediate Credit Banks. The question raised was whether there would be any complication because of the change in name in view of the fact that the Federal Intermediate Credit

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Banks are designated by that title in the provisions of the Federal Reserve Act having to do with discounting of paper at the Federal Reserve Banks. Governor Robertson said he responded that a mere change in name probably would not raise any questions but that the change might bring up the whole question of borrowing by the Federal Intermediate Credit Banks from the Reserve Banks, that he was not in a position to say what the reaction of the Board would be, and that he was not sufficiently acquainted with the reasons underlying the inclusion in the Federal Reserve Act of the provisions to which he referred to give any opinion as to what problems might be involved.

Mr. Young discussed proposed arrangements in connection with the seminar for commercial bank and insurance company economists to be held on November 7 and 8. The members of the Board expressed agreement with the program which he outlined, including a luncheon with members of the Board and its staff in the Board's dining rooms on November 7 and informal luncheon arrangements on November 8 for the economists participating in the seminar who might wish to remain for luncheon on that date.

The members of the staff then withdrew from the meeting and the Board went into executive session.

The Secretary subsequently was advised by Governor Balderston that during the executive session the Board approved the recommendation contained in the memorandum dated September 9, 1955, from Mr. Young, Director, Division of Research and Statistics, that

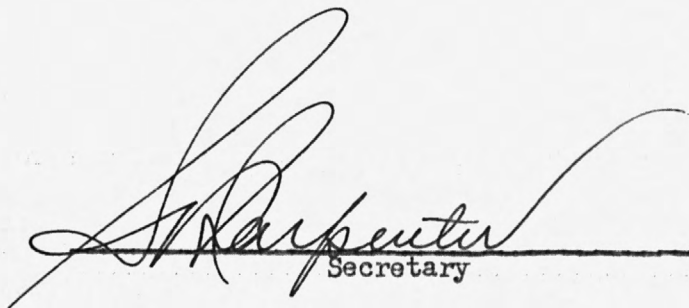
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Gloria J. Hile be appointed as Economist in that Division, with basic salary at the rate of \$5,710 per annum, effective as of the date of assuming her duties and subject to the completion of a satisfactory employment investigation.

Minutes of actions taken by the Board of Governors of the Federal Reserve System on November 3, 1955, were approved unanimously.

The meeting then adjourned.



Secretary