

F. A. C. September 16, 1918, Cont.

MINUTES OF MEETING

OF THE

FEDERAL ADVISORY COUNCIL.

September 16, 1918.

A regular statutory meeting of the Federal Advisory Council was held in the Federal Reserve Board room, Metropolitan Bank Building, Washington, D.C., on Monday, September 16th, 1918, at 11 A.M.

Present: All members of the Federal Advisory Council: Messrs. James B. Forgan, President, L. L. Rue, Vice-President, D. G. Wing, J. P. Morgan, W. S. Rowe, J. W. Norwood, Chas. A. Lyster, F. O. Watts, J. R. Mitchell, E. F. Swinney, E. P. Wilmot, Herbert Fleishhacker, and Merritt H. Grim, secretary; and the following members of the Federal Reserve Board: Governor W.P.G. Harding, Messrs. J. S. Williams, C. S. Hamlin, A.C. Miller and J. A. Broderick, acting secretary.

Mr. J. B. Forgan called the meeting to order and asked Governor Harding to address the meeting with reference to the business to come before the Council.

Governor Harding reviewed the topics which the Federal Reserve Board had submitted to the Council in writing and in

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In addition suggested that the Council consider whether there should be any change in the Discount rates at the Federal Reserve Banks. In connection with the subject of removing the embargo on gold Governor Harding asked the Council to consider whether it would be wise to release some gold to Mexico in return for silver bullion which could be used to advantage in place of gold in settling trade balances with certain other countries. He also requested the Council to arrange for a conference with the Capital Issues Committee.

A general discussion followed, after which Governor Harding introduced Mr. J. A. Broderick who had been appointed Acting Secretary of the Federal Reserve Board, in place of H. Parker Willis, resigned. The members of the Federal Reserve Board then withdrew.

The President then stated that the Secretary had sent to each member of the Council the minutes of its meetings and of the Executive Committee meeting on May 20th, 1918, and of the Council meeting on May 21st, 1918.

On motion these were approved.

Mr. Forgan then laid before the Council the topics submitted by the Federal Reserve Board for the Council's

FEDERAL RESERVE BOARD

WASHINGTON

OFFICE OF THE GOVERNOR

August 27, 1918.

Dear Mr. Forgan:-

I acknowledge the receipt of your letter of the 22nd inst. advising that the next statutory meeting of the Federal Advisory Council will be held in the assembly room on Monday and Tuesday, September 16th and 17th, convening at 11 A. M. on Monday the 16th.

At a meeting of the Board this morning consideration was given to the topics which should be discussed at the approaching meeting of the Council, and I am directed to say that the Board would be obliged if you would bring to the attention of the members of the Council the following:

- 1: Development of the acceptance market.
(With reference to the call loan rate of $4\frac{1}{2}\%$ recently established in New York on notes secured by acceptances.)
- 2: The use of bankers' and trade acceptances in financing the movement of crops.
- 3: Progress of the movement to curtail non-essential credits.
Have results thus far been obtained without undue hardships?
Is it practicable to lay down any general rule governing a differentiation between essential and non-essential credits, and if so, what is the best method of its application?
- 4: Investments of banks in public utility securities and loans on such collateral.
What can be done to assist public utilities in the emergency which now confronts them?
- 5: Distribution of Liberty Bonds and discussion of preferential rates at Federal reserve banks on paper secured by Government obligations.

No doubt some other topics will suggest themselves to the Council, and perhaps the Board may have a few additional suggestions to make after it convenes, but the foregoing embraces the subjects which appear to be of greatest consequence at the present time.

Very truly yours,

W. P. G. HARDING,

Mr. James B. Forgan, President,
Federal Advisory Council,
Chicago, Ill.

Governor.

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FEDERAL RESERVE BOARD

WASHINGTON

OFFICE OF THE GOVERNOR

August 29, 1918.

Dear Mr. Forgan:-

I enclose herewith several copies of a letter which the Board has received from a private banking house in Boston, which may be of interest to you and the other members of the Advisory Council.

The matter referred to in this letter has already been discussed by members of the Board and Treasury officials, but it is felt that we are unable to estimate the amount of gold that might have to be shipped should the door be opened, and some of us feel that while it might be well to keep this policy in mind with the view of putting it into effect at the proper time, the present is not an opportune time and we should wait until the end of the war is more clearly in sight. It might be interesting however, to discuss this question at the next meeting of the Council.

Very truly yours,

W. P. G. HARDING

Governor.

Mr. James B. Forgan,
President Federal Advisory Council,
Chicago, Ill.

Excerpt from a letter received by
the Federal Reserve Board.

"The enormous demand for raw materials owing to the war and the resulting high price of them has made the Neutrals creditors of the Allies and as the export of gold, the usual medium of settling adverse balances, has been largely prohibited rates of exchange on the United States and on our Allies are ruling at a considerable discount in the neutral countries. This discount has increased to us the cost of the very necessary raw materials at least the amount of the discount. All the Allies including ourselves have endeavored by arranging special credits, that is by borrowing money in those countries, to keep the exchange from being too much against us, just as England before our entry into the war, after having sold us all the securities that she could, borrowed heavily in this country to buy our necessary products.

My suggestion is that we change our recent policy and settle balances in gold. I well understand the fear that if the war lasts a long time we shall find our gold being depleted and our reserves endangered. This fear is, I think, based on the fallacy which I had hoped had passed with the enactment of the Federal Reserve Act that a fixed proportion of gold or legal tender must be held absolutely intact against outstanding bank notes or deposits. The strength of a bank is not in its proportion of cash reserve but in the character of its loans and discounts and in its reputation. It makes no difference if its cash is 60% or 10% of its liabilities provided this proportion is large enough for the public to feel confident that they can obtain the kind of money that they wish when drawing their deposits or when presenting notes for payment. Fortunately in this country our people are not accustomed to the use of gold, so that a removal of what are practically restrictions on gold payments would not result in any withdrawals of gold except for export.

How much would be withdrawn for export to settle our exchanges? Our Allies would not withdraw gold as the exchanges with the Allies are still very much in our favor. With Holland, Switzerland, and the Scandinavian countries our imports have nearly ceased and if necessary we can prevent gold going to these countries as contraband. With Spain now that withdrawals of German deposits to that country are being prevented and the army purchases have been covered by a special loan no large withdrawal of gold need to be expected. The European neutrals want our products not gold which is at a discount with them owing to its superabundance. The South American countries alone will take our gold, and this is especially true of Argentina.

Suppose fifty, or even one hundred million dollars in gold were shipped during the next year to Argentina, this amount would not materially affect our enormous stock of gold or reduce materially the sixty per cent of gold which is held against the Federal notes. Only forty per cent was contemplated by the Federal Reserve Act so that the amount is now one and one-half as much as was planned. A reserve is of no use except as it gives credit and as it is used. Forty per cent gold, or even less will amply protect our credit.

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Besides the obvious savings in the purchasing power, by having our dollar worth its gold equivalent in foreign countries, which would result from free export of gold, the general credit of this country would be wonderfully strengthened in foreign countries both during the wartime and afterwards. There is nothing that hurts the credit of a country and its merchants so much as a depreciated currency and a refusal to pay in the international standard of value, namely gold. We have been endeavoring to build up our commerce with South America, but unsatisfactory delivery of merchandise and the refusal to ship gold has given its people a bad opinion of our country and its merchants.

Moreover, if the neutral countries were certain that they could obtain gold from this country, they would not want it. They all have more gold than ever before and they have no use for more. If our credit was good, they would have large deposits with our banks or instead of rediscounting at once in this country all time bills of exchange on the United States, their bankers would have such bills held for their account so as to earn the interest, just as our bankers before our entry into the war held large amounts of long Sterling bills. England, besides paying for a portion of the necessary supplies from the United States in gold, also thereby reduced rates of interest in this country so that we held her bills and loaned the government money. It seems to me that this would work in exactly the same way in the neutral countries. Not only would we pay for products which we need with gold, which we do not need, but re-establish our credit and by lowering interest rates in the neutral countries, induce their people to place their funds in this country and thereby stop their demand for our gold. In fact, I doubt very much if it would take nearly fifty millions of gold to rectify the exchanges with Argentina or even with the whole world. If this is so, it seems extremely foolish for the United States to pay interest on loans from Spain or Argentina and still have to pay a premium of from 10 to 25% on its purchases, owing to our depreciated exchange, and also to ruin our credit as a nation, not only for now, but for all time.

(August 29, 1918)

FEDERAL RESERVE BOARD

WASHINGTON

Office of the Governor.

September 7, 1918.

My dear Mr. Forgan:-

As an additional topic for discussion at the meeting of the Council, I wish to suggest "Supervision of loans made by banks for capital purposes."

The Capital Issues Committee have been advised by their counsel that they have jurisdiction over loans of this kind. The opinion will be reviewed next week by the counsel of the Board. The members of the Capital Issues Committee would like, during the stay of the members of the Council in Washington, to have a conference with them on this subject, and have agreed to take no action until they have had this conference with the Council.

I hope therefore that you will add this topic to your list and that it will be convenient to the Council to confer with the members of the Capital Issues Committee.

Very truly yours,

W. P. G. Harding,
Governor.

Mr. James B. Forgan,
President Federal Advisory Council,
Chicago, Illinois.

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the Committee proposed to assist the banks of the country in discriminating against

It was decided that the Council members should discuss all the topics and leave it to the Executive Committee to formulate tentative recommendations on them embodying the consensus of the views expressed and report to a subsequent meeting.

The topics were then taken up seriatim, the members freely expressing their opinions on them.

At 1:15 P.M. the Council on motion of Mr. Morgan adjourned until 2:30 o'clock.

At 2:30 P.M. the Council resumed consideration of the topics. Mr. Foxgan stated that an arrangement had been made for the Council to meet with the Capital Issues Committee at 3:30 o'clock. Consideration of the topic on "Supervision by the Capital Issues Committee of loans made by banks for capital purposes" was on motion postponed until after this meeting.

Mr. Swinney suggested that the Council make a recommendation to the Federal Reserve Board in regard to the proposed additional tax on undistributed earnings of banks, which was discussed and on motion referred to the Executive Committee.

At 3:30 o'clock Mr. Drumm, a member of the Capital Issues Committee, came in and explained that he had been requested by his Committee to explain the procedure by which

Secretary.

the Committee proposed to make it work effective and to assist the banks of the country in discriminating against non essential industries particularly with regard to loans involving capital issues. He asked the members of the Council to cooperate with his Committee by passing a resolution to be used by it, urging all banks to assist it in obtaining from prospective borrowers ^{for capital purposes} such information as would enable it to decide before any commitments for material, labor or capital are made, whether or not a certificate of necessity should be issued. The Council members then discussed with Mr. Drumm certain features of the Committee's proposed plan, after which he withdrew and the Council resumed its session.

Mr. Fleishhacker moved that the Council recommend thorough cooperation on the part of banks with the Capital Issues Committee and that the Executive Committee be requested to prepare a formal resolution; motion seconded and carried.

The subject of Discount rates was considered and referred to the Executive Committee.

Mr. Forgan stated that Governor Harding had asked that the Council make a recommendation on the subject of affording state banks joining the Federal Reserve system the same privileges with respect to government deposits that national banks enjoy, and suggested an amendment to the law covering the case. On motion the question was also referred to the Executive Committee. At 5 P.M. the Council adjourned until ten o'clock September 17th, when they will receive the report of the Executive Committee.

Secretary.

September 17th, 1918.

The Federal Advisory Council met at 10:30 A.M. Tuesday, September 17th, 1918, in the Federal Reserve Board room.

Present: Messrs. J.E. Forgan, President, L.L. Rus, Vice-President, D.G. Wing, J.P. Morgan, W.S. Rowe, Chas. A. Lerley, Y.O. Watts, J.R. Mitchell, H.M. Skinner, H.P. Wilcox, Herbert Platchhacker, and Merritt H. Grim, Secretary. Absent J.W. Sweeney.

MINUTES OF MEETING

OF THE

EXECUTIVE COMMITTEE.

The President laid before the meeting the report of the Executive Committee making tentative recommendations on all of the

September 16, 1918.

Executive Committee making tentative recommendations on all of the

The Executive Committee met at 5:15 P.M. and continued in session until 7:45 o'clock. Present: Messrs. James B. Forgan, Chairman, L. L. Rus, D. G. Wing, J. P. Morgan, W. S. Rowe, and Merritt H. Grim, Secretary.

Tentative recommendations and answers were prepared on the topics referred to it by the Council and the Chairman was requested to present the report at the meeting of the Council in the morning.

In connection with the subject of member state banks receiving government deposits, the same as national banks are permitted by law to do, the Committee prepared a formal recommendation thereon but decided to ask the Council to consider the matter more fully before adopting it.

On motion the resolution presented by Mr. Watts was unanimously adopted. The printed copy hereto attached marked

Secretary.

The President was authorized to present these recommendations to the Federal Reserve Board at the joint session arranged for.

The Council then adjourned.

Secretary.

Federal Advisory Council

September 17th, 1918.

The Federal Advisory Council met at 10:30 A.M. Tuesday, September 17th, 1918, in the Federal Reserve Board room.

Present: Messrs. J.B. Forgan, President, L.L. Rue, Vice-President, D.C. Wing, J.P. Morgan, W.S. Rowe, Chas. A. Lyerly, F.O. Watts, J.R. Mitchell, E.F. Swinney, E.P. Wilmot, Herbert Fleishhacker, and Merritt H. Grim, Secretary. Absent J.W. Norwood.

The President laid before the meeting the report of the Executive Committee making tentative recommendations on all of the topics including that on the subject of member state banks receiving government deposits in connection with which the committee suggested further consideration by the Council.

The Council after carefully considering and amending the Committee's report adopted recommendations and answers to the Federal Reserve Board's topics. See printed recommendations hereto attached on Topics 1, 2, 3, 4, 5, 6, 7, 8, 9 and 10. In connection with No. 10 Mr. Rowe asked to be recorded as declining to vote.

Mr. Watts suggested that the Council make a recommendation to the Federal Reserve Board to the effect that Congress should take into account the present high prices in connection with tax levies as proposed in the pending revenue bill.

On motion the resolution presented by Mr. Watts was unanimously adopted. See printed copy hereto attached marked Topic No. 11. The President was authorized to present these recommendations to the Federal Reserve Board at the joint session arranged for.

The Council then adjourned.

Secretary.

RECOMMENDATIONS OF THE FEDERAL ADVISORY
COUNCIL TO THE FEDERAL
RESERVE BOARD

September 17, 1918

TOPIC NO. 1—Development of the acceptance market. (With reference to the call loan rate of $4\frac{1}{2}\%$ recently established in New York on notes secured by acceptances.)

Recommendation:

The making of a preferential rate by banks in the financial centers on demand loans secured by acceptances will aid in the development of the market for acceptances by facilitating and encouraging their use. It seems to us that the acceptance market is developing wonderfully well under existing circumstances which while favorable for the making of such forms of credit are not so favorable for the marketing of them.



TOPIC NO. 2—The use of bankers' and trade acceptances in financing the movement of crops.

Recommendation:

The Council is of the opinion that the bankers and commercial interests are both alive to the use of trade and bankers' acceptances and that the use of these forms of credit is being developed as rapidly as can be expected under present conditions. While conservative bankers are disposed to encourage the legitimate use of bankers' acceptances they are equally disposed to discourage their misuse where the transaction does not naturally arise in the usual course of their customers' business. They are inclined to hold their acceptance privilege in reserve for the benefit of their customers engaged in essential lines of business, whose credit requirements are enhanced by war orders.



TOPIC NO. 3—Progress of the movement to curtail non-essential credits.

(a) Have results thus far been obtained without undue hardships?

Answer:

The efforts of the Federal Reserve Board, followed up by various Clearing House associations and other bodies, have, we believe, resulted in bankers generally discriminating between essential and non-essential credits and in a reduction of the latter. They cannot, however, enforce payment of

current loans nor can they indiscriminately decline new credits to the point of causing hardships and embarrassments to their customers without such action retaliating against themselves. We are of the opinion that no undue hardships have resulted and we believe that as a rule borrowers are cooperating with the banks by curtailing their demands for credit for non-essential purposes.

(b) Is it practicable to lay down any general rule governing a differentiation between essential and non-essential credits, and, if so, what is the best method of its application?

Answer:

As applications for bank credit are of such unlimited variety that each must be dealt with on its individual merits, we doubt the feasibility of laying down any general rule governing a differentiation between essential and non-essential credits. We believe bankers generally appreciate the necessity for such differentiation and fully understand the difference between essential, less essential and non-essential credits. Moreover, the demand for essential credits is so strong as to make it as unnecessary as it would be unwise and unpatriotic to fail to discriminate in their favor. We believe the persistent prosecution of the Federal Reserve Board's efforts, already well developed, will be all that is necessary.



TOPIC NO. 4—(a) Investments of banks in public utility corporations and loans on such collateral.

Recommendation:

It is most essential that the assets of the banks of the country be kept in as liquid form as possible and with this in view they should not invest to any large extent in public utility securities nor to any large extent make loans on such collateral.

(b) What can be done to assist public utilities in the emergency which now confronts them?

Answer:

In our opinion a mistake was made in the law under which the War Finance Corporation was organized by involving the banks in the financing of public utilities. The law should be so amended or such legislation enacted as would give the War Finance Corporation general instead of emergency power to deal directly with the borrowers without the intervention of the banks or through some other corporation or agency organized for the purpose. It is highly desirable that loans should be made to public utilities only where rates are granted which are adequate to meet the present cost of operation. In the interest of the Government's war program power should be given a

board appointed by the President to regulate public service rates or if that power cannot constitutionally be granted them, then to negotiate with and urge local state authorities to grant such increases in rates for all classes of public service as may be found necessary during the period of the war and for a reasonable time thereafter.



TOPIC NO. 5—Distribution of Liberty bonds and discussion of preferential rates at Federal Reserve Banks on paper secured by Government obligations.

Recommendation:

We would recommend that the member banks should make loans on the Fourth Liberty Loan bonds on the same terms as those very generally made on the Third Liberty Loan bonds, viz., the coupon rate for ninety days' loans, with a moderate advance over that rate for renewals, and that the Federal Reserve banks, to encourage subscriptions to the new loan, should make a preferential rate on ninety days' loans of from $\frac{1}{4}$ to $\frac{1}{2}$ of one per cent below the coupon rate.



TOPIC NO. 6—Gold Embargo.

Recommendation:

The Council is of the opinion that it would be unwise to permit the free export of gold at this time in view of the fact that it is impossible to accurately estimate the amount that would be required not only to adjust our own trade balances but those of our Allies to neutral countries, particularly South America.

In regard to the release of gold to Mexico in return for silver bullion, we believe that if a substantial increase in silver imported from that country can be obtained by increasing somewhat the percentage of gold exported against silver bullion shipped us, such an arrangement would under present conditions be to our advantage.



TOPIC NO. 7—Supervision by the Capital Issues Committee of loans made by banks for capital purposes.

Recommendation:

We would recommend that the member banks be urged to cooperate with the Capital Issues Committee in its effort to obtain full information of projected capital issues, so that the consent of the Committee may be obtained before any financial commitments are made by prospective borrowers.

TOPIC NO. 8—Discount rates.

Recommendation:

It is the opinion of the Council that the discount rates of the Federal Reserve banks have been properly and carefully regulated by the directors of the respective banks with the approval of the Federal Reserve Board and we see no occasion at present for any change either in the existing rates or in the policy heretofore pursued, other than as we have previously recommended for the encouragement of subscriptions to the Fourth Liberty Loan.



ADDITIONAL RECOMMENDATIONS

TOPIC NO. 9—Tax on undistributed earnings of banks, proposed in pending legislation.

Recommendation:

In view of the fact that the undistributed earnings of banks immediately become additional banking capital, which should be conserved during this war period, the Council recommends that an exception be made of the banks so that as was provided in the previous tax law the normal rate only shall apply to their undistributed profits and that the Federal Reserve Board take steps to bring this matter before the proper committees of congress.



TOPIC NO. 10—Member state banks to receive government deposits.

Recommendation:

For the purpose of affording state banks coming into the Federal Reserve system all the privileges afforded to national banks with respect to government deposits, this Council would recommend that the words, "All national banking associations" occurring in Section 5153 of the Revised Statutes of the United States should be changed to read "All banks members of the Federal Reserve system."

(Mr. Rowe not voting.)



TOPIC NO. 11.

Recommendation:

The constant rise in prices has resulted in a condition increasing in danger to the merchant and manufacturer directly and thence to the member

banks and the Federal Reserve system, which should be given serious consideration by those in charge of the taxing program of the Government. We therefore recommend the approval of the amendment to the present draft of the law offered by the National Dry Goods Association, as follows:

“Section 202 of the proposed bill provides:

INVENTORIES

“Sec. 202. That whenever in the opinion of the Commissioner the use of inventories is necessary in order clearly to determine the income of any taxpayer, inventories shall be taken by such taxpayer upon such basis as the Commissioner, with the approval of the Secretary, may approve or prescribe as most clearly reflecting the income of the taxpayer.

We suggest that that section be amended by adding thereto the following:

“‘A reasonable allowance being made for the increased cost of merchandise so inventoried over the average cost of like merchandise during the prewar period.’”



RESOLUTION

RESOLVED, That it is the sense of the Federal Advisory Council that the suggestion made by Governor Harding regarding the absorption by the Federal Reserve banks of the expenses incident to transfers of currency and securities to and from member banks should be given favorable consideration by the Federal Reserve Board.

The following members of the Federal Advisory Council were present at this meeting: President, James B. Forgan, in the chair; Vice-President, L. L. Rue; D. G. Wing, J. P. Morgan, W. S. Rowe, J. W. Norwood, C. A. Lyerly, F. O. Watts, J. R. Mitchell, E. F. Swinney, E. P. Wilmot, Herbert Fleishhacker, and Merritt H. Grim, Secretary.

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MINUTES OF JOINT MEETING OF THE

FEDERAL RESERVE BOARD

AND

FEDERAL ADVISORY COUNCIL

September 17, 1918.

As arranged a joint meeting of the Federal Reserve Board and the Federal Advisory Council was held in the Federal Reserve Board room, Washington, September 17, 1918, at 11:30 A.M.

Present: Messrs. W.P.G. Harding, Governor, A.C. Miller, C.S. Hamlin, J.S. Williams, members of the Federal Reserve Board, and F.A. Broderick, Acting Secretary; and Messrs. J.B. Forgan, President, L.L. Rue, Vice-President, D.G. Wing, J.P. Morgan, W.S. Rowe, J.W. Norwood, Chas. A. Lyerly, F.O. Watts, J.R. Mitchell, E.F. Swinney, E.P. Wilmot, Herbert Fleishhacker, members of the Federal Advisory Council, and Merritt H. Grim, Secretary.

Mr. Forgan called the meeting to order and asked Governor Harding to take the chair. Governor Harding then asked for the report of the Federal Advisory Council. Mr. Forgan read the recommendations of the Federal Advisory Council (See printed copy hereto attached.)

Mr. Forgan requested Governor Harding to send the Capital Issues Committee a copy of the Council's recommendation on "Supervision by the Capital Issues Committee of loans made by banks for capital purposes," Marked Topic No. 7.

Members of both Boards then informally discussed the topics and the Council's recommendations thereon.

At the request of Governor Harding the members of the Council reviewed commercial and financial conditions in their

Minutes of Joint Session Sept. 17, 1918. Cont.

FEDERAL RESERVE BOARD
FEDERAL ADVISORY COUNCIL

various districts.

Governor Harding stated that the Board was constantly having requests for the establishment of branches of Federal Reserve banks in cities of moderate size and that it occurred to him if the Federal Reserve banks should absorb the expense of transfers of currency and securities to and from Federal Reserve banks it might lessen the necessity for such branches. The matter was discussed after which Mr. Mitchell moved that the Council adopt the following resolution on this subject:

"Resolved that it is the sense of the Federal Advisory Council that the suggestion made by Governor Harding regarding the absorption by the Federal Reserve banks of the expenses incident to the transfers of currency and securities to and from member banks should be given favorable consideration by the Federal Reserve Board." Motion was seconded by Mr. Fleishhacker and the President put the motion which was unanimously carried.

On motion the joint session adjourned.

Secretary.