MINUTES OF SPECIAL MEETING

of the

FEDERAL ADVISORY COUNCIL

held in Washington, D. C., on March 28-29, 1932

MINUTES OF SPECIAL MEETING OF THE FEDERAL ADVISORY COUNCIL

March 28, 1932.

In accordance with a call for a special meeting by President Smith, the Federal Advisory Council assembled in the Federal Reserve Board Room of the Treasury Building, Washington, D. C., on March 28, 1932.

Present:

Mr. Thomas M. Steele	District No. 1
Mr. Robert H. Treman	District No. 2
Mr. Howard A. Loeb	District No. 3
Mr. J. A. House	District No. 4
Mr. Howard Bruce	District No. 5
Mr. John K. Ottley	District No. 6
Mr. Walter Lichtenstein (Alternate for Mr. Melvin A. Traylor)	District No. 7
Mr. Richard S. Hawes (Alternate for Mr. Walter W. Smith)	District No. 8
Mr. L. E. Wakefield (Alternate for Mr. Theodore Wold)	District No. 9
Mr. C. W. Allendoerfer (Alternate for Mr. Walter S. McLucas)	District No. 10
Mr. J. H. Frost	District No. 11
Mr. Walter Lichtenstein	Secretary

Absent:

Mr. H. M. Robinson	District No. 12

As both the President and Vice-President were absent, the meeting was called to order by Mr. Robert H. Treman at 10:45 A.M.

Upon motion, duly made and seconded, Mr. Howard A. Loeb was elected unanimously as Chairman of the meeting.

The Secretary read the call for the special meeting, which was being held to consider the Glass banking bill (S. 4115).

The Secretary then presented proper credentials for the four alternates issued by the respective Federal reserve banks.

Upon request the Secretary also read Section 12 of the Federal Reserve Act defining the duties of the Federal Advisory Council.

A long discussion section by section took place in reference to the provisions of the Glass bill (S. 4115).

Upon motion, duly made and seconded, it was voted that the Chairman appoint a sub-committee of three members to present a draft of a report on the Glass bill to the Council. The Chairman appointed the following committee: Mr. Bruce, Chairman, Mr. Wakefield, and Mr. Frost, the Chairman and Secretary being ex-officio members of the committee.

The meeting adjourned at 2:30 P.M.

WALTER LICHTENSTEIN,

Secretary.

MINUTES OF SPECIAL MEETING OF THE FEDERAL ADVISORY COUNCIL

March 29, 1932.

At 9:30 A.M. the Federal Advisory Council reconvened in the Federal Reserve Board Room, Treasury Building, Washington, D. C., Mr. Howard A. Loeb acting as Chairman.

Present: Mr. H. A. Loeb, Chairman; Messrs. T. M. Steele, R. H. Treman, J. A. House, Howard Bruce, J. K. Ottley, Walter Lichtenstein, Secretary, Richard S. Hawes, C. W. Allendoerfer, and J. H. Frost.

The sub-committee presented its report, corresponding to the one attached hereto with one exception. The report as presented by the committee had under "1. *Control of Affiliates*" a paragraph at the end reading as follows:

> "While in general the Council favors the publication of full reports regarding the condition of affiliates and similar institutions, yet it would seem wise to take into consideration the present situation of the country; it may be better to defer this requirement until such time as the publication of the list of securities held in portfolios by affiliates is less likely to bring about a further unsettlement of the financial situation."

Mr. Bruce moved and Mr. Ottley sconded that the report of the sub-committee be adopted as the report of the Federal Advisory Council. It was unanimously voted to adopt the report and transmit it to the Federal Reserve Board.

The Chairman stated that he would inform the Board that

1. It was the wish of the Council to transmit a copy of the report to each member of the Senate Committee on Banking and Currency by the Council's own Secretary.

2. The Council wished to take steps to provide for suitable publicity of the report.

The meeting adjourned at 10:50 A.M.

WALTER LICHTENSTEIN,

Secretary.

MINUTES OF JOINT CONFERENCE OF THE FEDERAL ADVISORY COUNCIL AND THE FEDERAL RESERVE BOARD

March 29, 1932.

At 11:30 A.M. a joint conference of the Federal Advisory Council and the Federal Reserve Board was held in the Federal Reserve Board Room, Treasury Building, Washington, D. C.

Present: Members of the Federal Reserve Board:

Mr. Ogden L. Mills, Secretary of the Treasury; Governor Eugene Meyer; Mr. John W. Pole, Comptroller of the Currency; Messrs. C. S. Hamlin, A. C. Miller, G. R. James, and W. W. Magee; also Messrs. Chester Morrill, Secretary of the Board; Floyd R. Harrison, Assistant to the Governor; Walter Wyatt, General Counsel of the Federal Reserve Board; E. A. Goldenweiser, Director, Division of Research and Statistics, Federal Reserve Board, and E. L. Smead, Chief of Division of Bank Operations.

Present: Members of the Federal Advisory Council:

Mr. H. A. Loeb, Chairman; Messrs. T. M. Steele, R. H. Treman, J. A. House, Howard Bruce, J. K. Ottley, Walter Lichtenstein, Secretary, Richard S. Hawes, C. W. Allendoerfer, and J. H. Frost.

The Secretary of the Council read the report on the Glass bill (S. 4115) adopted by the Federal Advisory Council.

It was pointed out that there was a certain danger in publishing the paragraph referred to above and reading as follows:

> "While in general the Council favors the publication of full reports regarding the condition of affiliates and similar institutions, yet it would seem wise to take into consideration the present situation of the country; it may be better to defer this requirement until such time as the publication of the list of securities held in portfolios by affiliates is less likely to bring about a further unsettlement of the financial situation."

It was unanimously voted to omit said paragraph from the report.

The Chairman of the Council stated that

1. It was the wish of the Council to transmit a copy of the report to each member of the Senate Committee on Banking and Currency by the Council's own Secretary.

2. The Council wished to take steps to provide for suitable publicity of the report.

No objection to this procedure was raised by the Federal Reserve Board.

The meeting adjourned at 12:45 P.M.

WALTER LICHTENSTEIN,

Secretary.

Note 1: The report was officially transmitted to the Federal Reserve Board with the following covering letter:

"Washington, D. C.,

March 29, 1932.

Mr. Eugene Meyer, Governor,
Federal Reserve Board,
Washington, D. C.

Dear Governor Meyer:

Enclosed please find the unanimous recommendations of the Federal Advisory Council in reference to bill S.4115, as introduced by Mr. Glass in the Senate of the United States on March 14 (calendar day, March 17), 1932. It is requested that you submit these recommendations to the Senate Committee on Banking and Currency for its consideration.

Very truly yours,

(Signed) WALTER LICHTENSTEIN,
Secretary.

Enclosures."

Note 2: The Secretary of the Federal Advisory Council arranged for the release of the report with the following covering statement:

"FEDERAL ADVISORY COUNCIL
STATEMENT FOR THE PRESS

For immediate release. March 29, 1932.

There are attached recommendations respecting the Glass banking bill made to the Federal Reserve Board today by the Federal Advisory Council of the Federal Reserve System. The recommendations have been transmitted by Governor Eugene Meyer to the Senate Committee on Banking and Currency for consideration in connection with the Glass bill.

The Council is an official body, advisory to the Federal Reserve Board on matters pertaining to the Federal Reserve System. Its membership is composed of one banker from each of the twelve Federal Reserve Districts.

The members of the Council are:

Walter W. Smith, President, St. Louis.
Melvin A. Traylor, Vice President, Chicago.
Thomas M. Steele, New Haven.
Robert H. Treman, Ithaca.
Howard A. Loeb, Philadelphia.
J. A. House, Cleveland.
Howard Bruce, Baltimore.
John K. Ottley, Atlanta.
Theodore Wold, Minneapolis.
Walter S. McLucas, Kansas City.
J. H. Frost, San Antonio.
Henry M. Robinson, Los Angeles.
Walter Lichtenstein, Secretary, Chicago."

Note 3: On Wednesday morning, March 30, the Secretary of the Federal Advisory Council delivered in person a full copy of the report at the office of each member of the Senate Committee on Banking and Currency in the Senate Office Building. In each instance the report was accompanied by a covering letter, of which the following is an example:

"Washington, D. C.,

March 30, 1932.

Honorable Peter Norbeck,
303 Senate Office Building,
Washington, D. C.

Dear Senator Norbeck:

In accordance with my instructions, I beg to hand you herewith a copy of the report of the Federal Advisory Council on Senate Bill 4115, together with the recommendations of the Federal Advisory Council to the Federal Reserve Board, dated September 15, 1931, referred to on page 8 of the present report of the Federal Advisory Council.

My understanding is that these documents were officially transmitted to the Senate Committee on Banking and Currency yesterday by Governor Meyer.

Very truly yours,

(Signed) WALTER LICHTENSTEIN,

Secretary."

March 29, 1932.

The Federal Advisory Council has given careful consideration to Senate Bill 4115. It is of the opinion that the present is an inopportune time to raise many of the issues presented in this proposed legislative measure. Reforms in our banking system may be desirable, but such should be made at a time when the country has passed through the present crisis and when there is no danger that legislative enactments will retard recovery and add to the existing difficulties with which banks are confronted.

The Council feels that the effect of this proposed measure is likely to destroy the benefits of the Glass-Steagall Act, the Reconstruction Finance Corporation Act, and similar measures. If the bill should be enacted into law it would necessitate a wholesale liquidation of securities which would most certainly cause a further decline in the prices of all securities. Such deflation would work extreme hardship not merely upon banks but upon all holders of securities in this country and especially upon those who have borrowed from banks and who are finding difficulties even at present in meeting their obligations.

It must also be pointed out that in the opinion of the Council, the thesis apparently underlying this measure that loans upon securities are in general undesirable and should be drastically limited would undermine the customary system of capital financing which has been an inherent part of the present industrial and financial system almost from its beginning. Without the flotation of securities which have been financed directly or indirectly by banks, it would have been impossible to build up the large enterprises which have contributed so much to the progress of industrial development in this country.

In addition to the above general expression of opinion, the Federal Advisory Council desires to point out, in some detail, its specific objections to certain features of the bill.

1. CONTROL OF AFFILIATES. The Federal Advisory Council is in accord with the purpose sought to be achieved in Section 20 and believes that a control of affiliates is desirable.

The definition of affiliates in Section 2, however, is much too broad and comprehensive. It brings within the provisions of the Act any corporation regardless of its business which may happen to have a majority of its Executive Committee, directors or managing officers, directors of a member bank.

Section 9 limits the sum which a parent member bank may lend to an affiliate to 10% of the capital and surplus of the parent bank and such loans must be secured by 120% of listed exchange securities or 100% of either eligible paper or savings banks' securities, neither of which would be for the most part in the possession of an affiliate, unless it happened to be a bank. Furthermore, this provision would seem to bar the acceptance of real estate mortgages as collateral from an affiliate upon the part of those banks located in states where there are no laws regulating the investments of savings banks. Likewise, commodity or livestock paper, unless its maturity is such as to make it eligible, could not be used as collateral for a loan made to an affiliate.

The Federal Advisory Council also believes that the provision in Section 25, Page 49, Paragraph 2, which refers to the sale for cash of the stock of an affiliate within a three year period is not at all clear. If this means that the stock of the affiliate held by the parent institution must be sold for cash away from the bank, in other words divorcing the affiliate from control by the bank, it will create a distinct hardship, as there are large

numbers of such affiliates in existence today whose compulsory liquidation would cause serious financial losses. Apparently this section is in conflict with some of the provisions of Section 20.

2. CENTRALIZATION OF POWER. It was the original intention of the Federal Reserve Act to decentralize the banking power in this country by establishing twelve autonomous regional Federal reserve banks. The Federal Reserve Board itself was planned originally to be largely a supervising and coordinating body. The proposed Act, however, tends to increase radically the power of the Federal Reserve Board at the expense of the individual Federal reserve banks and to make of the Federal Reserve System in effect a centralized banking institution. In support of this statement attention is called to the following sections:

Section 3 delegates the power of direct action to the Federal Reserve Board which even if practical would result in so embarrassing the operations of member banks as to lead to the elimination of important and necessary activities or to the virtual surrender of individual bank management to the Federal Reserve Board.

Section 8 gives power to the Federal Reserve Board to fix the percentage of the capital and surplus which any member bank may lend in the form of collateral loans, and it is within the power of the Federal Reserve Board to change this percentage at any time upon ten days' notice and to direct any member bank to refrain from an increase of its security loans for any period up to one year. This would be a tremendous increase in the powers of the Federal Reserve Board and would introduce an element of uncertainty in the minds of those directing any given member bank as to when the bank in question might be subjected to the direct action authorized in this section.

The power of control by the Federal Reserve Board over the actions of the Federal Open Market Committee, as authorized in Section 10, might possibly tend to slow up open market operations at times when quickness of action might be absolutely essential in order to bring about desired results.

In Section 11 the Federal Reserve Board is empowered to cancel the right of any member bank to borrow on so-called fifteen day paper and to declare existing loans due if such a member bank has failed to heed a notice instructing it not to increase loans on collateral security. It would appear to the Federal Advisory Council that this endows the Federal Reserve Board with an arbitrary power which is highly undesirable entirely aside from other features in this section to which reference will be made hereafter.

The Federal Advisory Council believes that subdivisions F and G of Section 13 give power to the Federal Reserve Board to regulate what is a purely routine loan operation of a member bank. The ability of member banks to trade in Federal reserve funds tends to maintain a greater degree of liquidity in the general banking situation than would otherwise be the case. In this connection attention is called to the ever increasing restrictions upon, and to the diminishing scope of, loaning operations of banks. This results in increasing unnecessary balances on the part of member banks and makes it more difficult for them to employ funds profitably.

3. LIQUIDATING CORPORATION. In general the Council endorses the idea of a liquidating corporation. It is, however, not in harmony with the provisions as set forth under Section 10 (Section 12B) of the proposed Act. The Council is of the opinion that such a corporation as is proposed should be financed entirely by Government money as is intended to be done in the case of nonmember banks. Furthermore, the Council believes that it might be well to consider the possibility of creating twelve agencies, one in each of the Federal reserve districts, rather than seeking to create a single body for the whole country.

Such twelve agencies might then be placed under the control and guidance of the Federal Reserve Board or some other coordinating group. In no event does the Council believe it proper to require member banks to furnish the funds needed for such a corporation without at the same time giving the member banks control of such a corporation for which they are to furnish the capital from out of their own resources. The Council, furthermore, suggests the possibility of having the activities of a Federal Liquidating Corporation taken over by the Reconstruction Finance Corporation.

4. Increase of Reserves. The Federal Advisory Council presumes that the requirement of larger reserves as set forth in Section 13 of the proposed Act is intended to provide for greater liquidity on the part of banks. The Council believes, however, that the experience of the past ten years has clearly indicated that there is little or no relation between reserves and liquidity. In the opinion of the Council liquidity is the result of careful and prudent bank management and is measured by the character of the assets held by the bank. Furthermore, the imposition of additional reserves will reduce available resources in the member banks at a time when these are largely needed, while at the same time they will bring no advantage to the System, the resources of which have been and are ample to take care of changing financial situations. The effect of this requirement would also be to tie up an additional volume of gold as a reserve against increased member bank deposits in the Federal reserve banks without any apparent justification.

5. Segregation of Time Deposits. The Federal Advisory Council regards the provisions in Section 14 of the proposed Act, intended to segregate the assets behind time deposits from those against other deposits, as likely to lead to undesirable results. In the opinion of the Council this provision will lead either to the withdrawal of demand deposits or the diversion of demand deposits into time deposits. It believes that the increase of investment in real estate foreseen in this section will tend to reduce the liquidity of banks. There is also imposed upon the Comptroller of the Currency a duty which burdens him with tremendous responsibility insofar as he is required to specify the type of property and the securities in which one-half of the time deposits of the member bank may be invested in the absence of state laws governing the investment of such funds. It has been the experience of a number of members of the Council that the absence of restriction in respect to the investment of time deposits has produced a greater degree of liquidity in banks than can be possibly accomplished under the permissions granted in this section.

The Council feels that the views here set forth in regard to Section 14 might be much amplified. In its opinion the most important effect of this section would be to bring about a disruption of the present credit structure of the country. Many banks in this country having a large percentage of time deposits use these funds for the purpose of aiding commerce, industry, and agriculture in their respective communities. These would be compelled under the provisions of Section 14 to liquidate a large proportion of these loans and invest the funds so obtained in real estate or specified securities.

6. Fifteen Day Paper. Section 11 penalizes borrowers on so-called fifteen day paper. In the opinion of the Federal Advisory Council such a provision would make Government bonds a much less desirable form of investment for member banks. It would handicap the United States Treasury in its necessary financing, increasing the rate on Government securities and thereby the interest rate on all other classes of securities and thus depreciate the market price of securities generally. It should also be pointed out that the ability of member banks to borrow on their promissory notes for a period of not exceeding fifteen days is essential in periods of depression when sufficient eligible paper is not available for rediscount.

7. Limitation of Interest on Deposits. The limitation of interest which member banks may pay upon deposit balances provided for in Section 24 of the proposed Act,

places such banks in unfair competition with nonmember banks not so restricted. It should be remembered that money is a commodity like any other and that member banks should be free to pay the rates necessary to hold their deposits.

8. BRANCH AND GROUP BANKING. In reference to Section 21 and other sections of the proposed Act referring to branch or group banking, the Council begs leave to refer to the recommendations which it made on September 15, 1931, reading as follows:

"The Federal Advisory Council has received the recommendations of the Comptroller of the Currency made in his Annual Report for 1930, suggesting certain changes in the Federal laws relating to banking. The Federal Advisory Council is in sympathy with the Comptroller's recommendations, but suggests certain changes. In the following the original where changed is placed in brackets and the changes suggested by the Federal Advisory Council are italicized:

"I. Group and Chain Banking.

"No national bank should be permitted to become a part of a group banking system, except on the condition that all other banks in the group are [national banks; and when a State member bank of the Federal Reserve system is a part of a group, the Federal Government should be given visitorial powers over the entire group], *members of the Federal Reserve System to the end that the Federal Government have visitorial powers over the entire group*. More specifically:

"(a) No corporation should be permitted to own [a majority] *in excess of 20%* of the stock of a national bank if it owns at the same time [a majority] *in excess of 20%* of the stock of a State bank *unless said State bank is a member of the Federal Reserve System.*

"(b) The Comptroller of the Currency should be given visitorial power over any corporation owning [a majority] *in excess of 20%* of the stock of a national bank.

"(c) No national bank should be permitted to make a loan on the security of the stock of a corporation owning [a majority] *in excess of 20%* of the stock of the lending bank.

"II. Branch Banking.

"A. The McFadden Act should be amended to permit national banks in important commercial and financial centers to establish branches in the area that is economically and financially tributary to such centers without regard to State boundaries or to State banking laws. The privilege should be limited to banks in cities serving a territory sufficient to provide economic diversification. The [trade] area within which banks located in such cities may extend their branches should be defined by a committee consisting of the Comptroller of the Currency, the Secretary of the Treasury, and the Governor of the Federal Reserve Board. Banks permitted to have branches in [a trade] *an* area should have [a minimum capital of] *capital adequate to their deposit liabilities, the minimum not to be less than* $1,000,000. The extension of branches should be subject to the approval of the Comptroller of the Currency.

"B. The National Bank Consolidation Act should be amended to permit any bank within the [trade] *branch-bank* area to consolidate under national charter with the approval of the Comptroller of the Currency."

9. Collateral Loans and Securities. In the general statement the Federal Advisory Council has already expressed its views regarding the desire to limit collateral loans. It wishes here, however, to discuss somewhat more in detail the provisions in Sections 8, 11, 13, 15, etc., all of which deal in whole or in part with the control of the volume of collateral loans and the volume of securities held by member banks. These sections deal with control of volume of collateral loans and volume of securities held by member banks and place arbitrary powers of control and penalties in the Federal Reserve Board. The enforcement of the mandatory provisions of these sections will result in the enforced liquidation and to the detriment of general business. The Council believes that such liquidation will retard if it does not entirely defeat the beneficent effects that may be expected to be realized as a result of the Glass-Steagall bill and the Reconstruction Finance Corporation Act. The Council does not share the view of the proponents of the bill that the underlying cause of either bank disasters or depression is directly related to the volume of collateral loans or the volume of securities held by banks. These did not, and do not now, impair the ability of member banks properly to care for those types of loans the proceeds of which go more directly into commerce, industry, and agriculture.

In conclusion the Council calls attention to the fact that the bill, if enacted into law, would in effect place an underserved stigma upon the flotation and selling of securities and make it almost impossible for banks to do business with dealers in securities. There would seem to be no justification whatsoever for such drastic action.

Finally, the Council believes that it is not possible to promote activity in commerce, industry, and agriculture under an easy money and credit policy and at the same time prevent people by admonition or restriction from buying securities which are being made attractive by this very activity.