Note: The transcript of the Secretary's notes is not to be regarded as complete or entirely accurate and ~~they~~ a should be considered as being strictly for the sole use of the members of the Federal Advisory Council.

W. L.

Secretary's Notes on Meeting of the Federal Advisory Council on November 16, 1941, at 2:00 P.M. in Room 782 of the Mayflower Hotel, Washington, D. C.

All the regular members of the Federal Advisory Council were present except Mr. W. Dale Clark who had informed the Secretary of the Council that he would be at the meeting on Monday, but would be unable to be present on the first day.

The Minutes of the meeting of the Council on September 14-15, 1941, were approved.

Brown discussed certain aspects of Regulation W. He stated the Board did not pay any attention to the recommendations of the Council and especially not in respect to small personal loans. However, small business loans had been exempted from the operation of the Regulation and so much, at least, had been gained. There was some discussion about small personal loans.

Brown continued, saying that he believed the Council should discuss its own attitude toward Regulation W, especially the following three points:

(a) Opinion of Council on non-purpose loans where the suggestion of the Council has been rejected,

(b) Council might, of course, go into details but it was his view that the Council would be well advised not to become involved as there is likely to be growing public sentiment about many of the features of Regulation W,

(c) The Council might do nothing at all. In his opinion, the Council should probably restrict its attitude to matters of general policy.

Wakefield says we might raise the question as to the whole principle upon which Regulation W is based. In his opinion it has not anything to do with inflation or any other pending problem.

Brown stated that, of course, the Council might reiterate the position which the Executive Committee of the Council took or the Council might simply say that the whole Regulation is wrong and that the Executive Order ought never to have been issued, but he himself questions the advisability of criticizing the President.

Harrison points out that before there was any Executive Order ever issued the Council had pointed out that there was really no need for measures of the type that are being considered here for off-setting inflation or helping the defense program. As far as the defense program is concerned, that is being taken care of by priorities, allocations, et cetera.

Wakefield and Brown discussed "selective credit control". The latter stated that Viner and perhaps Morgenthau believed that priorities will take care of reducing bank loans. Eccles, on the other hand, believes that there ought to be direct action and the amount of credit to be given by banks should be controlled. At present the group believing that priorities and allocations will be sufficient seems to be in control. If control is merely through priorities, then there won't be any governmental attempt to dictate to banks the nature of their loans, but if the policy favored by Eccles is followed, the chances are that the banks would have to obtain governmental approval in advance for every loan they desired to make.

Clay stated that his information was that the Treasury is pushing "selective credit control" and wants examiners to have the right to go into banks and even demand that loans already made which are not for purposes of aiding the defense program should be called.

Harrison says the only way in which the Government can carry out its present apparent plan is to issue securities bearing a rate which will enable banks to live. This has been done more or less in Great Britain. The other way would be for the Government to take over banks. There is a real danger that the whole private banking system might be wrecked.

Brown suggests that the Council might present a resolution pointing out that the whole situation can be controlled by priorities and allocations and that the Council is opposed to the whole principle of Regulation W; furthermore, that in the opinion of the Council the whole Regulation will tend to discredit the Federal Reserve System and lead to the control by Government of the extension of all credit. However, the Executive Order having been issued, the Federal Reserve Board is compelled to issue regulations under it. The least the Council might do is to reaffirm the position of its own Executive Committee in regard to small personal loans.

Brown stated that at the last meeting, Leon Fraser, acting as alternate for Mr. Harrison, had objected to the Council taking such action, pointing out that in Great Britain, Canada, and not to mention Germany and other countries, credit is being controlled by the Government and that he, Fraser, believed it to be inevitable.

Harrison says that he agrees with Fraser, but that it will be necessary for the Government to issue special securities for banks as has been done in Great Britain.

Kurtz said that he believed in Regulation W and in Fraser's position. If he were running the Government he would try to control the situation directly.

Wakefield says Great Britain has not issued any regulations. She has taken over practically the property of all her citizens, and has left no place for investments except in Government securities, but this is a very different situation from having the Government in control by means of regulations which will probably persist after the emergency is over.

Hanes agrees with Kurtz and believes some of the measues taken will help to save many a finance company and many a small bank which may get into difficulties if there were not the compulsion by the Regulation of amortization loans.

Harrison says as a practical matter nothing will be accomplished by saying that the whole thing is wrong, but at least the Council as a whole should reaffirm the position of its own Executive Committee.

Kurtz says we should support priorities and allocations for they are certain to disappear as soon as the war is over. The people in charge of priorities and allocations are dollar-a-year men who wish to go home as soon as the emergency is ended, but the same is not true of alphabetical regulations which will remain in existence long after the war is over.

Brown states that "selective credit control" may be exercised through the application of priorities and allocations much better than by means of permanent regulations. The former will disappear with the emergency and it would be well for the Council to suggest that before direct credit control is put into effect at least the attempt should be made to control the situation by means of priorities and allocations. If this is done, we are not shutting ourselves off from later asking for special securities for banks so that the banking system may continue to exist through the emergency. In Great Britain and Canada where there are very few banks all necessary measures can be taken by consultation without legislation or formal regulation. In this country with approximately fifteen thousand more or less independent banking units there can not be consultations and voluntary action and it is necessary to have much more formal action taken than in countries where there are only a few large banking systems.

Kurtz points out that "selective credit control" is deflationary and when the war is over it may be necessary to take an entirely different tack.

Ragland and Huntington believe that there is not any point in attacking the whole principle of Regulation W. They do think the position of the Executive Committee should be confirmed.

Hanes believes there isn't any point in repeating what we said before and it is probably better to cooperate than just oppose.

Brown believes that if there were no possibility of the Board changing its view on the non-purpose loans then there would be no sense in passing a resolution, but a minority of the Board favors excepting non-purpose loans from the Regulation and the position of the Council may help strengthen the hands of the minority if there should be any change in sentiment. If we are to resolve about "selective credit control" this ought to be done in an entirely separate resolution.

Harding agrees with Hanes but thinks the recommendation of the Executive Committee should be approved. He agrees that any resolution on credit control should be entirely separate.

Clay agrees with Harding.

Dick would like a preamble stating the original position of the Council but would not object seriously if this were omitted. Then the position of the Executive Committee should be confirmed, and there should be a separate resolution about credit control.

Wakefield said Montgomery-Ward and Company had borrowed $48,000,000 but intended to pay off its loans and keep down its inventories and simply live from hand to mouth. Montgomery-Ward in carrying out this intention has cancelled many of its commitments.

Brown states that this apparently is not the policy of Sears-Roebuck and Company and that, in fact, Sears had taken over in many instances orders cancelled by Montgomery-Ward.

Harrison moved to reaffirm the action of the Executive Committee with respect to Regulation W and is ready to move a separate resolution recommending that credit control be carried out by means of priorities and allocations.

After some further discussion, Clay moved, and Harding seconded formally, two resolutions, one to reaffirm the position of the Executive Committee vis-a-vis Regulation W and the other dealing with credit control. Both measures were unanimously adopted and the chair appointed Harrison and Kurtz to draw up these two resolutions.

Brown brings up the proposals for amending the S.E.C. Act. The Association of Investment Bankers of America has been agitating for changes in the S.E.C. Act, concealing some of its activity from commercial bankers. Out of the discussions which a committee of the A.I.B. has had with the Securities and Exchange Commission came four classes of proposals.

1. Changes agreed to by both the industry and the S.E.C.

2. Changes suggested by the S.E.C. and opposed by the industry.

3. Changes suggested by the industry and opposed by the S.E.C

4. Changes suggested by the industry about which the S.E.C. is entirely neutral.

After these discussions the A.I.B. got the Committee on Interstate and Foreign Commerce of the House of Representatives to put forward a group of suggestions for amendments to the two S.E.C. acts. This plan was followed in order to evade the Presidential Order which forbade Government agencies to propose legislation without first clearing their proposals through the Budget Committee.

In the proposals as put forward there are three sections which above all others concern the banks:

There is proposed a new subsection (2)14. The present Act does not attempt to regulate non-public sales of securities, though "public sale" is not defined in the Act. The new subsection states that "public sale" is anything by which the public interest is affected, and thus any agency is included which accepts deposits, has premiums on policies, etc. The idea is that S.E.C. should have the right to protect the depositors and policyholders against loss by requiring registration of loans above a certain amount. S.E.C. claims it has not proposed this provision but that it does not oppose it and Congress might well consider the question.

A committee appointed by New York commercial banks asked that banks be excluded from the provision, and a committee of the Investment Bankers agreed to this, for the A.I.B. was not seeking to hamper commercial banks but was trying to prevent insurance companies from buying issues of securities privately. The S.E.C. objected to the exclusion of banks. Then it was suggested that loans should be excluded that did not have any securities with coupons attached and were not based on any indenture or similar instrument. If this were adopted, term loans would be excluded from the operations of the section, but the principle of giving S.E.C. authority over commercial banks would remain. The New York committee unfortunately agreed to the suggestions of the A.I.B. and is therefore in a somewhat awkward position, but finally decided to go along with all other banks in opposing the new subsection. Bankers naturally feel that even with the exception agreed to by the A.I.B., the S.E.C. would be in the position of the camel getting its nose into the tent as far as control of banks is concerned.

<u>Brown</u> and <u>Hanes</u> were in Washington last week and had conferences with the Board of Governors, the Comptroller, and Crowley of the F.D.I.C.

The Board of Governors (Ransom was away) agreed to oppose the section in question, as did the F.D.I.C. and the Comptroller, and an excellent joint letter was issued by these three agencies, together with separate covering letters, the best one being the covering letter of the Board of Governors. The covering letter of the F.D.I.C. mainly spoke of the glories of the F.D.I.C., while the Comptroller's letter was a rather colorless production. The Board's letter was very strong and direct.

The Secretary of the Council, at the request of Mr. Brown, read the joint letter of the Comptroller, Board of Governors, and F.D.I.C. opposing (2)14 in the S.E.C. proposals.

Brown says there are two other sections in the proposal affecting banks. Section 17 says any report made to stockholders by directors and officers of any corporation which is inaccurate, misleading, or contains false statements would subject such officers and directors to the same penalties imposed for filing a false registration statement. At present banks are not subject to any registration requirements for the sale or purchase of stock. The proposal, of course, sounds innocent and quite proper, but banks are simply not in a position to issue statements which might not be subject to attack. If, for example, banks carry their bonds below market value and do not state this fact in their reports to stockholders, they might be accused of suppressing pertinent information. In many cases banks simply are not in a position to know what the present or ultimate value of their "charge-offs" may be. Likewise, if reserves are set up for possible losses, and earnings are reported net, the S.E.C. might claim suppression of information. Banks now are supervised by the Comptroller or the F.D.I.C. or the Board of Governors, and each bank must make a sworn statement of its exact position to its supervisory authority, and these supervisory authorities examine banks very carefully, so that under present conditions, without any further regulation or law, banks are very closely supervised. The new proposal would merely give S.E.C. inquisitorial jurisdiction over banks and thus subject banks to still another governmental agency.

Under present conditions, banks are protected from politically inspired suits, for there is an understanding that the Department of Justice will not direct a United States District Attorney to bring suit against a bank except at the request of one of the regular supervisory authorities. This would change if Section 17 of the proposed amendments to the S.E.C. Act were to be adopted.

Hanes suggests that a resolution be adopted that the Board of Governors be asked to oppose Section 17.

Ragland so moved, and Harding seconded, and the proposal was unanimously adopted.

Brown. There is still a third section in the proposed amendments which was not originally suggested by the investment bankers but is not opposed by them, namely, that the S.E.C. should be given authority over all pension funds to which employees contribute, unless such fund is insured one hundred per cent with some insurance company.

Brown gives the history of this: namely, that some time ago one of the research staff of the S.E.C. made a study of pension funds and pointed out that neither Federal nor State authorities at present regulate or supervise any pension funds and members who have contributed to pension funds may find that they have lost their protection as a result of mismanagement of the fund in which they are interested. This was just a study and was not intended to support immediate action.

A short time ago the Johns-Manville Company offered a voluntary pension fund to its employees and the S.E.C. claimed that even under the present Act voluntary funds were subject to the control of the S.E.C. and Johns-Manville Company submitted to this ruling without taking legal action, as did Sears-Roebuck and Company in a similar situation. Of course, every one knows there have been many abuses in connection with pension funds. The concern of the banks in the proposal is two-fold: in the first place, many large banks have pension funds of their own, and secondly, many large industrial companies, such as the International Harvester Company, have trusteed their pension funds, generally with New York banks. In New York State, trustsof which beneficiaries live outside of the State are exempt from the State tax laws, and as a result it is more favorable for a large concern to turn its pension fund over to a trust company in New York than, for example, to one in Illinois. The proposal of the S.E.C. would be a first step toward giving the Commission control over insurance companies.

As far as banks are concerned, their pension funds, where existing, are subject to the examination of the usual bank examiners as regards the securities and the like, though there is no attempt made by examiners to assess bank pension funds from an actuarial standpoint. Of course, the New York banks are concerned because they would lose much valuable business. There are, of course, people in the Government who think that all old age pensions should be under Government auspices; labor unions have always objected to private pension funds because, by these pension funds, employees are tied too closely to their employers. In the case of all national banks, trusts are subject to examination, and in this way examiners already have control. In the case of State banks, many States have similar provisions.

Harrison says opposition can be based on the fact that banks are now examined by banking authorities and where these do not examine pension funds, legislation should be urged to have it done by bank examiners, and not set up another authority over banks in Washington.

Brown stated that he understood it was the sense of the meeting that there was to be a resolution to cover this subject.

The desirability of regulating exchange charges, which had been suggested as a topic by Mr. Ragland, was taken up.

Ragland pointed out that he tried to have some action taken about a year ago, but nothing was done.

Harding says that the trouble is the Board is afraid to approach Congress because Henry Steagall would then insist that banks be again allowed to pay interest on demand deposits.

Hanes suggests that the absorption of exchange charges is bad banking practice, and the Board therefore should enforce Regulation Q.

Brown and Huntington both feel that the Board should not be asked to make regulations on subjects which banks should regulate themselves. Brown thinks it is a mistake to bring this matter to the Board because, after all, there are relatively few banks affected.

Harding suggests that there not be any resolution, but that the President of the Council simply ask the Board about the situation. The matter was left there.

It was decided to discuss Mr. Wakefield's question of the desirability of the Treasury withdrawing its balances from special depositaries and placing them in Federal Reserve Banks to reduce excess reserves. Likewise, suggesting to the Board of Governors to work out a reclassification of reserve cities, which would also lead to a substantial reduction in excess reserves. If these two and possibly similar measures were carried out, there probably would not be any need to take action intended to increase the power of the Board of Governors over reserves by raising the present maximum limit of required reserves.

Harding stated that the present amount of war loan deposit is about $784,000,000, and putting this in the Treasury would really have very little effect on excess reserves.

It was decided to drop this question.

Harrison withdrew both of his questions which appeared on the agenda, "Bank Capital and Bank Earnings" and "Treasury Financing with particular reference to the type of issues that might go into the hands of permanent investors and types that are much more appropriate and suitable for bank investors".

Harrison stated that under present conditions he did not see that the 10% ratio of capital to deposits has any sense. He believes that deposits will increase and earnings decrease.

Wakefield believes dividends may go up.

Harrison thinks there will be pressure to increase the wages of bank employees substantially.

Brown stated that he believes New York banks were paying a much larger proportion of their earnings in dividends than formerly. In Chicago, the large banks are paying only about half of their earnings out in the form of dividends. New York banks in the 20's made large amounts of money on call loans, bond transactions, and the like. He thinks that the agitation for having a ratio has been decreasing.

Harrison says the padding of subscriptions for bond issues should be discouraged.

Brown suggested that this might be accomplished if purchasers were required to file a statement giving an undertaking that bonds subscribed for and bought would not be resold before the expiration of six months after purchase.

Harrison agreed and suggested that a temporary registered certificate might be issued for six months and only after that period would the bonds actually be handed over to the purchaser.

The meeting adjourned at 5:45 p.m.

Secretary's Notes on Meeting of the Federal Advisory Council of November 17, 1941, at 10:00 A.M., Board Room, Federal Reserve Building, Washington, D.C.

All members of the Council were present, including Mr. W. Dale Clark.

It was decided not to present a resolution about "selective credit control", but have the President of the Council state the views of the Council orally. The draft of the resolution on Regulation W was presented and put into final form. Copies of the resoltuion were given to each member of the Council and later to all those representing the Board of Governors at the meeting.

The meeting adjourned at 10:30 a.m.

Secretary's Notes on Meeting of the Federal Advisory Council of November 17, 1941, at 10:35 A.M., Board Room, Federal Reserve Building, Washington, D.C.

The Council met with the Board. Of the Board, the following were present: Eccles, Ransom, Szymczak, Draper, McKee, Morrill, Clayton, Carpenter, Wyatt, and Thurston.

Brown stated on behalf of the Council the satisfaction the members of the Council had in the joint letter on Section (2)14 of the S.E.C. proposals, and also the covering letter. Brown stated that all members of the Council were in accord. He also told the Board that the members of the Council felt that the covering letter of the Board was better than the covering letters of the other two agencies. Brown went on to state that Section 17 seemed innocuous but it has given the Council much concern, and the Council hopes that the Board will object to it. By implication it may mean that banks would be affected in that it would cover their annual statements and make officers and directors liable if there was any lack of full information about reserves. It must be pointed out that the value of reserves is, after all, a matter, to a certain extent, of individual opinion. S.E.C. would have the duty to go into the banks to discover whether earnings and assets are correctly stated. At present, U. S. District Attorneys will start suit against officers and directors of banks only as requested to do so by the present supervisory examining bodies. As it is, banks now make sworn statements to the supervising authorities and this new regulation might prove very vexatious. It might lead to a supervision on the part of S.E.C. of banks generally.

McKee stated that he thought this section might be negotiated out and deleted as far as banks are concerned.

Brown undertook to show the danger that would be involved if bonds were written down and the whole question of reserves would create great difficulty.

McKee agreed with Brown and said he believed, as far as the supervising agencies are concerned, Section 17 is really more important than (2)14.

Eccles stated that if the proposals had been in the form of a bill it would have been necessary to submit the bill to all interested governmental bureaus. He doubts, however, whether legislation will develop out of such proposals. If the bill were to pass as a result of such proposals, it would be the first time in the history of legislation that it had happened. If a bill actually should pass the House, it would have to go to the Senate, where it would be referred to the Banking and Currency Committee, and Eccles feels certain that the provisions about which there has been discussion would not get through that Senate Committee. Hearings would be held and supervisory agencies, bankers, and insurance companies would be heard.

McKee says that the reason that the proposals were in the form that they were was in order to avoid the Budget Bureau.

Brown was glad to know that the Board is opposed to Section 17. Another section is one dealing with pension funds. This is intended to support the view of the S.E.C. that it has jurisdiction over pension funds on the ground that it is equivalent to a security being offered to members. This clause arose from a study made under S.E.C. auspices. He told the history of the development as he did at the meeting of the day before. The banks had two interests in this section: (a) banks have pension funds, (b) banks have many pension funds trusteed with them by large industrial corporations. This is especially true of the New York banks. The danger is that the big corporations will drop their pension funds rather than undergo supervision. This would cut across all kinds of business and, therefore, the Council would be glad to have the Board oppose this clause if it can see its way clear to do so.

Ransom states that his belief is that the intention, at least originally, was simply to see to it that pension funds were administered by an independent trustee. He doesn't know if this is still the plan, but he admits that the section in question may defeat its own purpose; however, it isn't clearly a banking question.

Brown suggests it might be possible to have the Board object to the inclusion of bank pension funds and trust funds because these are all subject, at least as far as the assets are concerned, to present bank examining authorities, though it must be admitted that the actuarial situation is not taken into account in these examinations.

The Board staff did not analyze this section, but Wyatt pointed out that this was without significance, as the analysis was made by a law clerk who was not familiar with the discussions that had taken place. As a matter of fact, department officials who had sat in on the discussions were very cognizant of this section.

Eccles says it might weaken the effect of the opposition of Government agencies to certain other sections if they were to oppose the pension fund provision, in view of the bad record made by so many pension funds. A very constructive suggestion would really be necessary if criticisms were to be offered.

McKee says a careful study must be made before the Board assumes a definite position and he suggests that it would be better to wait and see what is really going to be done. The chances are that this particular section, which is very far down on the list, will not be up for consideration until next year.

Brown agrees with what Eccles has said and realizes that the Board may not be able to oppose the section, but all that the Council is asking is that the Board should give the matter careful consideration and study the section somewhat.

The Secretary of the Council read the resolution adopted bearing on Regulation W.

Brown stated that the Council was glad to see that small business loans had been exempted from the provisions of the regulation.

Szymczak defends the present provision.

Hanes asks whether this provision makes allowance for people who are dependent for income upon quarterly dividends and therefore could not make instalment payments on a monthly basis.

Ransom believes the matter may be taken care of by interpretation, but Wyatt states this would strain the language of the present regulation to a considerable extent.

Eccles states there is an important group in the Treasury that believes there is great danger of a serious inflation resulting from an excess purchasing power of six to nine billion dollars. It is estimated that there is that much spending power in the population in excess of goods available. Much greater taxes are required. Eccles himself doubts whether the danger is quite as imminent as some of these Treasury officials believe, but if taxes and credit control will not check inflation, then we shall have a rationing system covering all civilian goods and price control.

McKee says that loans made for the purpose of encouraging thrift will not hurt the economy.

Harrison says that it is all ridiculous as long as wages and farm commodities are exempt from all controls.

Eccles says it is clear that the Executive Order would govern term loans and open book account.

Brown says while the Council did not pass a resolution, it was the belief of all members of the Council that a full trial should be given to priorities and allocations before an attempt is made to impose "selective credit control". He believes that present increases in bank loans are to a very large proportion for defense purposes or for carrying commodities of which the Government desires to have accumulations. Credit control in banks or capital issues control should not be tried until all other means are exhausted. The Council believes that priorities and allocations will end with the emergency, but the abolition of credit control would be much more difficult, especially in view of the fact that there is a group in the Government which wants socialization of credit and banking.

Eccles points out that if allocations cover more and more items, then you will finally have a complete rationing system. Allocation and price control go together, while credit control is something supplementary. We haven't reached this point as yet, but it is impossible to tell what the future will bring. It is the duty of the Government to use such powers as are given to prevent prices rising. Thus Regulation W is a part of credit control and if the Board had not taken over this function, then the Price Control Board or some other agency would have been given the job. All building except defense construction has practically stopped, so further credit restriction is not needed in that field. Perhaps, however, the price of existing houses and of farms may rise. So long as there is not a complete price control, credit must be controlled.

Brown, in answer to a question, states that rates on commercial loans have gone up somewhat. He reiterates the sentiment of the Council in respect to allocation versus "selective credit control".

Ransom feels that there may be need of general credit control by the Federal Reserve System.

McKee wants to know why there has been a sharp drop in sales of automobiles.

Eccles says there is an over-bought condition, and dealers are holding back deliberately, partly because they wish to keep some stock for next year, as the number of autos produced will be very much reduced, and they also do not wish to sell at present, for most of them have had an excellent year, and consequently feel that their income taxes will be very high, while next year may be a much poorer year, so that they will be in a lower bracket than they are now.

Brown asks the opinion of the Board about Regulation Q, and emphasizes that he is doing this without desiring in any way to make the question controversial. He points out that the Council itself has always been divided in its views. Formerly, the Board wanted the F.D.I.C. to join it in the supervision of the absorption of exchange charges. Danger, however, has been that if the regulation were enforced, all the small banks would immediately bring pressure to abolish the provision forbidding the payment of interest on demand deposits.

Eccles says the question has been on ice so long that it is dead, and he feels that you cannot deal with this problem without considering the related problem of membership in the Federal Reserve System, so he would prefer to leave the whole question on ice.

Ransom says there is no use going into the matter of interest payments. There is a very strong minority who objects to the enforcement of Regulation Q and Congress would be swamped by people who would want a repeal of the provision covering interest payment on demand deposits. He doesn't see any use in enforcing the rule until it can be brought about that all banks will be under the same rule. In the meantime, the Board is getting a flood of letters asking that the regulation be enforced.

Eccles claims that if the regulation were really being enforced, the very banks demanding enforcement now would beg to let sleeping dogs lie if it would mean, as it undoubtedly would, that interest would again have to be paid on demand deposits.

Brown asks whether the Board has any questions; he asks what effect, if any, has increase of reserve requirements had on country banking balances. Has the movement ceased? He feels that the total decrease of excess reserves has been impressive.

Eccles suggests that the Council discuss the matter with Mr. Smead in the afternoon.

McKee says the shift began in January of this year because of industrial activity, and not merely since there has been a rise in reserve requirements.

Brown says that the shift of reserves has been mostly true of New York and not of Chicago.

Eccles points out that the huge increase in currency in circulation has had much to do with the decrease of excess reserves. It is unfortunate that long term rights and middle term rights have been based on a very low rate of interest on securities issued. The result has been that the speculator has gotten the benefit and the real investor has had to pay a premium. On the other hand, the Treasury cannot do its financing on a rising rate structure. If there were a rising rate structure the investor would certainly object and would hold back because he would feel that the next issue might bring him a better rate. Eccles feels that issues of from twelve to fifteen years ought to be on about a 2-1/2 per cent basis, but the market has been going up and the rate is actually lower. It is too late to do anything now. Short rates are going up slightly; New York banks have been largely responsible in the past for the low short term rates but the situation is changing and while banks outside of New York are likely to begin to buy heavily, he doubts if the bill rate will change very much.

The meeting adjourned at 1:15 p.m.

Secretary's Notes on Meeting of the Federal Advisory Council of November 17, 1941, at 2:40 P.M., Board Room, Federal Reserve Building, Washington, D. C.

Council met alone, all members being present. Messrs. Goldenweiser, Thomas, and Smead met with the Council to discuss the reserve situation and general business conditions.

Goldenweiser states that J. H. Riddle of the Bankers Trust Company of New York has written an excellent article on the subject of the present reserve situation. An article has also been prepared by a member of the Board's staff, and Goldenweiser will see that each member of the Council receives a copy of this article. This article bears the date of November 13, 1941, and was written by Victor M. Longstreet. The decrease in the excess reserves is almost entirely in New York. New York is the city which always loses reserves by changes of increase in reserve requirements and by the withdrawal of Treasury funds. On the other hand, New York has the advantage that arises from the imports of gold. It used to attract funds by offering high interest payments on deposits when deposits were needed, but this is now a closed avenue. If short term rates were to rise, then people might send money to New York to buy short term bills, etc. Goldenweiser does not regard the situation as one which need cause any alarm. It is very doubtful whether even under existing circumstances New York banks generally will dump any securities upon the market. At present excess reserves in New York are down to about eight hundred million dollars, and probably will go down to about five hundred million by the end of the year.

At this point Goldenweiser left and Woodlief Thomas took over.

Thomas. If currency in circulation increases, the drain will continue, although ordinarily the current is reversed after January 1. It is interesting to know that the circulation of large denominations has been decreasing. National income at present is about ninety-two billion dollars, and some further rise may be expected, but it is likely to become slower as we approach full capacity of production. The process is likely to result in a rise of short term money rates. Lend-lease has tended to restrict the imports of gold. Furthermore, perhaps five hundred million dollars has been taken out of New York in the form of loans made to customers of New York banks $400,000,000 outside of the city of New York. There has been about ~~$4,000,000,000~~ additional currency and about one billion additional Government borrowing in New York, and these have also been the forces tending to reduce excess reserves. Certain factors brought funds into New York during the first half of the year, and practically all the additional money that came into New York during the first half of the year has gone out again since July 1. It used to be felt that when the New York banks were in debt to the Federal Reserve Bank by about fifty million dollars, the situation was just about right; if the banks were in debt to the extent of thirty million dollars or less the market was sloppy, while if the indebtedness of New York banks was more than about seventy-five million, money was tight.

Harrison and Thomas both doubt whether it is true that New York banks, in order to operate smoothly, need excess reserves of five hundred million dollars, as is being stated.

Business situation. Not much change since October, but there has been some slackening in speculative buying by business and consumers. Industries cannot get the goods. Retailers accumulated stocks, but their sales have been smaller in October than they were in August and September when there was a great spurt due to the fear of new taxes on commodities and fear of the provisions of Regulation W. Automobile trade is down, for which many explanations are made. Consumers bought cars earlier as they felt the later cars might not be as good owing to the use of substitute materials. Undoubtedly, also, Regulation W has had some effect. At the moment, dealers are not selling as many cars as are being produced, even though production for civilian consumption has been reduced by about 50 per cent. There seems to be a general hesitation. Production index in October was 160 and, allowing for seasonal influences, the adjusted index is about 164 in October and may be 170 in December. At the beginning of the year the index was 140. In July the index was 160, so obviously, the rate of increase has been slowing down, but the rise for the year has been about 30 per cent. In non-defense industries the rise as a whole has probably stopped. In defense industry, capacity has been increasing but there is a limitation of production imposed by the amount of raw materials available. Price trend is upward, for demand is growing and shortages exist. Unquestionably, the spread between the amount of purchasing power available and the supply of goods is increasing. Taxes and other methods cannot absorb all additional buying power being created. If the tax system did absorb all additional buying power created, it would ruin certain whole classes of the population, for no tax system has ever been devised that bears equally upon all classes of the population in relation to their income capacity.

The meeting adjourned at 3:45 p.m.

MINUTES OF MEETING

of the

FEDERAL ADVISORY COUNCIL

November 16-17, 1941

MINUTES OF MEETING OF THE FEDERAL ADVISORY COUNCIL

November 16, 1941

The fourth statutory meeting of the Federal Advisory Council for 1941 was convened in Room 782 of the Mayflower Hotel, Washington, D. C., on Sunday, November 16, 1941, at 2:00 P. M., the President, Mr. Brown, in the chair.

Present:

Mr. Charles E. Spencer, Jr.	District No. 1
Mr. George L. Harrison	District No. 2
Mr. William Fulton Kurtz	District No. 3
Mr. B. G. Huntington	District No. 4
Mr. Robert M. Hanes	District No. 5
Mr. Ryburn G. Clay	District No. 6
Mr. Edward E. Brown	District No. 7
Mr. S. E. Ragland	District No. 8
Mr. Lyman E. Wakefield	District No. 9
Mr. R. Ellison Harding	District No. 11
Mr. Paul S. Dick	District No. 12
Mr. Walter Lichtenstein	Secretary

Absent:

Mr. W. Dale Clark	District No. 10

The Secretary of the Federal Advisory Council reported that Mr. W. Dale Clark had informed him that he would be unable to be present at this first session but would be present at the sessions on Monday.

On motion, duly made and seconded, the minutes of the meeting of the Council on September 14-15, 1941, copies of which had been previously sent to the members, were approved.

The President of the Council discussed certain aspects of Regulation W. He pointed out that while little attention had been paid to the recommendations of the Council, at least small business loans had been exempted from the operations of the Regulation.

On motion made by Mr. Clay and seconded by Mr. Harding, it was unanimously voted to confirm the position of the Executive Committee of the Council in respect to Regulation W, and it was also voted to have a resolution prepared to deal with credit control. The Chairman appointed Messrs. Harrison and Kurtz to prepare both resolutions.

The President of the Council then brought up the proposals that had been submitted to the Committee on Interstate and Foreign Commerce of the House of Representatives, which were an outgrowth of discussions that had taken place between representatives of the Association of Investment Bankers of America and the Securities and Exchange Commission.

The President pointed out that there were three provisions specifically of interest to banks:

(1) A new subsection designated as (2)14. The present Act does not attempt to regulate non-public sales of securities, though "public sale" is not defined in the Act. The new subsection states that "public sale" is anything by which the public interest is affected,

and thus any agency is included which accepts deposits, receives premiums on policies, etc. The idea is that the S.E.C. should have the right to protect depositors and policy holders against loss by requiring registration of loans above a certain amount. The S.E.C. has not proposed this provision but it does not oppose it and Congress might well consider the question.

A committee appointed by New York commercial banks asked that banks be excluded from the provision, and a committee of the Investment Bankers agreed to this, for the A.I.B. was not seeking to hamper commercial banks but was trying to prevent insurance companies from buying issues of securities privately. The S.E.C. objected to the exclusion of banks. Then it was suggested that loans should be excluded that did not have any securities with coupons attached and were not based on any indenture or similar instrument. If this were adopted, term loans would be excluded from the operations of the section, but the principle of giving the S.E.C. authority over commercial banks would remain.

(2) The whole of Section 17 also is of great interest to banks. If the proposal embodying Section 17 were to become law, any report made to stockholders by directors and officers of any corporation which is inaccurate, misleading, or contains false statements would subject such officers and directors to the same penalties as are now imposed for filing a false registration statement. At present banks are not subject to any registration requirements for the sale or purchase of stock. The proposal, of course, sounds innocent and quite proper, but banks are not in a position to issue statements which might not be subject to attack. If, for example, banks carry their bonds below market value and do not state this fact in their reports to stockholders, they might be accused of suppressing pertinent information. In many cases banks do not know what the present or ultimate value of their "charge-offs" are. Likewise, if reserves are set up for possible losses, and earnings are reported net, the S.E.C. might claim suppression of information. Banks now are supervised by the Comptroller or the F.D.I.C. or the Board of Governors, and each bank must make a sworn statement of its exact position to its supervisory authority, and these supervisory authorities examine banks very carefully, so that under present conditions, without any further regulation or law, banks are very closely supervised. The new proposal would give the S.E.C. inquisitorial jurisdiction over banks and thus subject banks to still another governmental agency.

(3) A proposal that the S.E.C. be given authority over all pension funds to which employees contribute unless such fund is covered completely by insurance in some recognized insurance company. The President of the Council gave the background of this proposal, which is an outgrowth of a pure piece of research made by members of the staff of the S.E.C., which showed that neither Federal nor State authorities at present regulate or supervise any pension funds. The interest of banks in the proposal is twofold:

(a) Many of the larger banks have pension funds of their own which are now, at least in the case of National banks, subject to examination by the regular examining authorities, and the same is true in the case of many State banks, so that the control of the S.E.C. would merely mean additional examination.

(b) Many large industrial concerns have appointed banks, especially banks in New York, as trustees of their pension funds.

Fundamentally, undoubtedly the S.E.C. is in favor of this proposal as it would be a first step toward giving the Commission control over insurance companies.

A lengthy discussion took place and it was decided to discuss this whole matter further with the Board of Governors of the Federal Reserve System at the joint meeting and possibly present a resolution.

It was pointed out that the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, and the Federal Deposit Insurance Corporation had presented a joint statement to the Committee on Interstate and Foreign Commerce of the House of Representatives opposing the new Section (2)14 to be added to the Securities Act of 1933. It was understood also that the Board was probably opposed to the other two sections of the proposals to which the President of the Council had made reference.

The desirability of regulating exchange charges in a manner similar to that provided in Regulation Q was then discussed. It was decided that the President of the Council address an inquiry to the Board regarding the situation.

After a short discussion it was decided to drop the question about the desirability of the Treasury withdrawing its balances from special depositaries and placing them in Federal Reserve banks in order to reduce excess reserves.

Two other questions on the agenda were withdrawn. These were:

(a) Bank Capital and Bank Earnings;

(b) The types of government issues that might go into the hands of permanent investors and the types that might be more appropriate and suitable for bank investors.

The meeting adjourned at 5:45 P. M.

WALTER LICHTENSTEIN,
Secretary.

MINUTES OF MEETING OF THE FEDERAL ADVISORY COUNCIL

November 17, 1941

At 10:00 A. M., the Federal Advisory Council reconvened in the Board Room of the Federal Reserve Building, Washington, D. C., the President, Mr. Brown, in the chair.

Present: Mr. Edward E. Brown, President; Mr. George L. Harrison, Vice President; Messrs. Charles E. Spencer, Jr., William Fulton Kurtz, B. G. Huntington, Robert M. Hanes, Ryburn G. Clay, S. E. Ragland, Lyman E. Wakefield, W. Dale Clark, R. Ellison Harding, Paul S. Dick, and Walter Lichtenstein, Secretary.

It was decided not to present a resolution about "selective credit control", but have the President of the Council state the views of the Council orally. A draft of a resolution on Regulation W was presented which, in its final form, reads as follows:

> "The Federal Advisory Council endorses and reaffirms the views expressed by its Executive Committee in a letter, dated August 16, 1941, and addressed to Governor Ronald Ransom, making suggestions as to desirable amendments to Regulation W.
>
> The Council also wishes to endorse specifically the position taken by its Executive Committee at a meeting held in the Board Room of the Federal Reserve Building on September 26, 1941. The belief was expressed by the Committee at that time that Section 5(b) should be eliminated once a purpose test is adopted, i.e., if the statement of the borrower indicates that the loan is not being made to purchase a 'listed article' or to refund any indebtedness previously incurred in the purchase of a 'listed article'. While the public understands the restriction of instalment credit granted for the purpose of purchasing 'listed articles' the Council is fearful that restrictions by Regulation W of instalment credit granted for other purposes is subject to serious misunderstanding and injurious public reaction."

The meeting adjourned at 10:30 A. M.

WALTER LICHTENSTEIN,
Secretary.

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

November 17, 1941

At 10:35 A. M., a joint conference of the Federal Advisory Council and the Board of Governors of the Federal Reserve System was held in the Board Room of the Federal Reserve Building, Washington, D. C.

Present: Members of the Board of Governors of the Federal Reserve System:

Chairman Marriner S. Eccles; Vice Chairman Ronald Ransom; Governors M. S. Szymczak, John K. McKee, and Ernest G. Draper; also Messrs. Lawrence Clayton, Assistant to the Chairman; Elliott Thurston, Special Assistant to the Chairman; Chester Morrill, Secretary of the Board of Governors; S. R. Carpenter, Assistant Secretary of the Board of Governors, and Walter Wyatt, General Counsel.

Present: Members of the Federal Advisory Council:

Mr. Edward E. Brown, President; Mr. George L. Harrison, Vice President; Messrs. Charles E. Spencer, Jr., William Fulton Kurtz, B. G. Huntington, Robert M. Hanes, Ryburn G. Clay, S. E. Ragland, Lyman E. Wakefield, W. Dale Clark, R. Ellison Harding, Paul S. Dick, and Walter Lichtenstein, Secretary.

The President of the Council stated on behalf of the Council the satisfaction the members felt in the joint letter of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, and the Federal Deposit Insurance Corporation, dealing with Section (2)14 of the S.E.C. proposals; also the members of the Council felt that the covering letter of the Board of Governors was an excellent one.

The President of the Council then went on to state that the Federal Advisory Council also felt some concern about two other sections in the proposals, namely, Section 17 and the proposal dealing with the supervision of pension funds.

The Chairman of the Board of Governors expressed some doubt as to whether these proposals would ever be enacted into law, as he felt reasonably certain that in any event the Senate Committee on Banking and Currency would be opposed to the proposals.

The Secretary of the Council read the resolution bearing on Regulation W which appears earlier in these minutes.

The President of the Council then stated that while the Council had decided not to present a resolution on the subject of "selective credit control", he was authorized to state verbally that the members of the Council felt a fair trial should be given to the imposing of restrictions by means of priorities and allocations before any attempt be made to impose "selective credit control". He pointed out that priorities and allocations would undoubtedly end with the present state of emergency, while it would be much more questionable whether "selective credit control" would disappear after the emergency were over.

The President of the Council asked the opinion of the Board of Governors about Regulation Q, and emphasized that he was doing this without desiring in any way to raise controversial questions.

The Chairman of the Board of Governors stated that on the whole it seemed to him desirable to leave this whole question quiescent at present, and there was general agreement with this position.

There was some general discussion about interest rates and Government issues.

The meeting adjourned at 1:15 P. M.

WALTER LICHTENSTEIN,
Secretary.

MINUTES OF MEETING OF THE FEDERAL ADVISORY COUNCIL

November 17, 1941

At 2:40 P.M., the Federal Advisory Council reconvened in the Board Room of the Federal Reserve Building, Washington, D. C., the President, Mr. Brown, in the chair.

Present: Mr. Edward E. Brown, President; Mr. George L. Harrison, Vice President; Messrs. Charles E. Spencer, Jr., William Fulton Kurtz, B. G. Huntington, Robert M. Hanes, Ryburn G. Clay, S. E. Ragland, Lyman E. Wakefield, W. Dale Clark, R. Ellison Harding, Paul S. Dick, and Walter Lichtenstein, Secretary.

Messrs. Goldenweiser, Thomas, and Smead met with the Council to discuss the reserve situation and general business conditions.

Dr. Goldenweiser started the discussion in respect to the reserve situation but as he had to leave to keep another appointment, the discussion was continued by Mr. Woodlief Thomas, who discussed not merely the reserve situation but also general business conditions.

Mr. Woodlief Thomas finished the discussion at 3:45 P.M. and the meeting adjourned.

WALTER LICHTENSTEIN,
Secretary.