

MINUTES OF THE MEETING OF THE EXECUTIVE COMMITTEE OF THE  
FEDERAL ADVISORY COUNCIL

December 7, 1943

At 11:00 A. M., the Executive Committee of the Federal Advisory Council convened in the Conference Room of the Federal Reserve Building, Washington, D. C., on Tuesday, December 7, 1943, 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, Robert V. Fleming, and Walter Lichtenstein, Secretary.

The Secretary reported Mr. Huntington would be unable to attend the sessions of this meeting of the Executive Committee owing to conflicting engagements.

The President of the Council presented the problem of permitting commercial banks having savings accounts to purchase a certain amount of the restricted government issues in so far as this is now permitted to mutual savings banks and to building and loan associations.

The President of the Council again discussed the loans to be made by the Smaller War Plants Corporation which had been the subject of discussion at the last regular meeting of the Federal Advisory Council.

The Secretary of the Council read a letter from the Hon. Robert P. Patterson, Under-Secretary of War, in which he expressed himself in very complimentary fashion about the resolution adopted by the Federal Advisory Council on the final settlement of terminated contracts.

The Secretary of the Council read the draft of the resolution dealing with the question of the loans of the Smaller War Plants Corporation. After some discussion, on motion duly made and seconded, the resolution reading as follows, was unanimously adopted:

"The Smaller War Plants Corporation has within the past few weeks announced that it will enter into repurchase agreements up to 100% with banks on loans of \$25,000 or less, to business concerns engaged in the production of war material or essential civilian requirements where the bank agrees to close and service the loans. The interest rate on such loans to be 4%, with one per cent going to the Smaller War Plants Corporation and 3% to the banks. The announcement says that any of the regional offices of the Smaller War Plants Corporation shall have authority to approve these loans without consulting Washington.

"The Federal Advisory Council feels that the announced plan of the Smaller War Plants Corporation is fraught with the possibility of ultimate danger both to solvent and well run small businesses and is a threat to the continued existence of the small banks of the country.

"The one hundred per cent guarantee of a loan by a government agency is equivalent to direct loaning to businesses by the government. Such 100 per cent loans may well be justified in certain cases to companies engaged in war production as a war necessity where credit is not otherwise available. But the Smaller War Plants Corporation plan requires no showing the credit is otherwise unavailable, and it applies to all borrowers engaged in any line of essential civilian production. In no case is any bank or other financial institution required to share any part of the risk but the

entire risk is to be borne by the government. The rate, 4%, is the same in all cases, irrespective of the financial responsibility, quality of management or earning record of the borrower.

“The Smaller War Plants Corporation is a new organization and it is yet to be seen what loans it will guarantee. If it is strict in its credit standards it will make few if any loans which the borrower could not obtain elsewhere. If it is lax and easy in its credit standards it will not only cause a loss to the National Treasury, but by enabling inefficient, poorly managed, or badly conceived businesses to operate on government money at a very low rate, create unfair competition for well run and sound small competitive businesses, which may well cause the failure of many businesses in this latter class.

“While an interest rate of 3% is generous for a riskless loan, the overall rate of 4% is impossible of competition by the average small bank. The announced policy of the Smaller War Plants Corporation would tend to cause all small borrowers to borrow under the guarantee of the corporation in order to get a rate as low as that of their competitors. This would mean the socialization of such credit and its extension by public officials, with any loss passed on to the general taxpayer. It would transfer the business of appraising risks in loans, from bankers whose stockholders' and depositors' money is at stake, to the government.

“The banks have ample funds to meet most legitimate demands from small business. While, as stated above, the rate of 3% for a riskless demand loan is generous and one on which a large bank could not only exist but make excellent profits it is too low a rate to enable the average small bank to pay expenses and continue in operation. If the announced plan of the Smaller War Plants Corporation is expanded and becomes general it will mean the extinction of many small banks throughout the country, with the consequent dislocation of the business of the communities in which such banks are located.

“If the Smaller War Plants Corporation is to operate under the existing law it should require as a condition of a loan evidence that credit is not otherwise available, and should except in extreme cases require that some percentage of the credit risk be borne by the servicing bank.”

A further discussion took place regarding the investment in restricted government issues of savings departments in commercial banks.

The meeting adjourned at 11:50 A. M.

WALTER LICHTENSTEIN,  
Secretary.

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

December 7, 1943

At 12:05 P. M., a joint conference of the Executive Committee 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., on Tuesday, December 7, 1943.

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

Chairman Marriner Eccles; Vice-Chairman Ronald Ransom; Governors M. S. Szymczak, John K. McKee, and Ernest G. Draper; also, Messrs. Lawrence Clayton, Assistant to the Chairman; Chester Morrill, Secretary of the Board of Governors and Liston P. Bethea and S. R. Carpenter, Assistant Secretaries of the Board of Governors; Walter Wyatt, General Counsel and George B. Vest, Assistant General Attorney; E. A. Goldenweiser, Director, Division of Research and Statistics; Leo H. Paulger, Chief, Division of Examination; L. M. Piser, Chief of the Government Securities Section of the Division of Research and Statistics; Edward L. Smead, Chief, Division of Bank Operations; Carl E. Parry, Chief, Division of Security Loans, and Robert F. Leonard, Director, Division of Personnel Administration.

Present: Members of Executive Committee of the Federal Advisory Council:

Mr. Edward E. Brown, President; Mr. George L. Harrison, Vice President; Messrs. Charles E. Spencer, Jr., William Fulton Kurtz, Robert V. Fleming, and Walter Lichtenstein, Secretary.

The President of the Council in discussing the possibility of permitting commercial banks having savings accounts to buy restricted securities issues expressed the opinion on behalf of the members of the Executive Committee of the Council that there ought to be a definite restriction as to the percentage a commercial bank might be allowed to invest in such securities at any one time and also a restriction as to the total percentage of its savings which it might so have invested at any one time. He pointed out that there are three classes of banks involved and that the problem is a somewhat different one in each case:

1. Small country banks where it might be dangerous to permit one hundred per cent of savings to be invested in restricted issues.
2. Banks in medium sized towns and banks in the outlying districts of large cities where savings deposits often amount to 50% and more of the total deposits.
3. Larger commercial banks whose savings deposits are not likely to be more than about ten per cent of the total deposits of such banks.

After a long and detailed discussion it was agreed that those members of the Executive Committee of the Council who are at the same time members of the Committee of the American Bankers Association advising the Treasury would arrange to consult with the Under-Secretary of the Treasury regarding the problem.

The Secretary of the Council read the resolution given above, dealing with the proposed loans of the Smaller War Plants Corporation.

After further discussion it was decided to send copies of the resolution, with a covering letter addressed to the Secretary of the Board of Governors by the President of the

Council, to the Chairman of the War Production Board and to the members of the Board of Directors of the Smaller War Plants Corporation. It was decided to take up at the Executive Committee Meeting of the Council, to be held on January 5, 1944, the question whether this resolution should be released for publication.

The letter addressed to the Secretary of the Board of Governors by the President of the Council read as follows:

“At the meeting of the Executive Committee of the Federal Advisory Council held today a resolution was unanimously adopted in respect to the loans of \$25,000 or less which the Smaller War Plants Corporation is making to business concerns engaged in the production of war material or essential civilian requirements. The Executive Committee of the Council will appreciate it if the Board of Governors of the Federal Reserve System will transmit as soon as possible copies of the enclosed resolution to the Chairman of the War Production Board and the members of the board of directors of the Smaller War Plants Corporation.”

The meeting adjourned at 1:30 P. M.

WALTER LICHTENSTEIN,  
Secretary.

NOTE: This transcript of the Secretary's notes is not to be regarded as complete or necessarily accurate. The transcript 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 Executive Committee of the Federal Advisory Council on December 7, 1943, at 11:00 A. M., in the Conference Room of the Federal Reserve Building.

Mr. Huntington was not able to be present. All other members of the Executive Committee were on hand throughout the meeting.

BROWN presented the question of permitting commercial banks having savings accounts to purchase a certain amount of the restricted government issues. The suggestion had been made to permit subscription of such issues up to 10% of the amount of the savings accounts in the commercial banks. He feels there ought to be some definite formula. It was brought out that the matter had been discussed at a meeting of the A. B. A. Committee at the Treasury at the time of the last meeting of the Council.

BROWN also brings up the problem of the loans being made by the Smaller War Plants Corporation which, as brought out at the last meeting of the Council, is entering into repurchase agreements up to 100% with banks on loans of \$25,000 or less, to business concerns engaged in the production of war material or essential civilian requirements where the bank agrees to close and service the loans. As an indication of some of the men in charge of local offices of the Smaller War Plants Corporation, it was pointed out that one of the men in charge of a regional office of this Corporation actually had made the suggestion that any discharged soldier should be allowed to borrow up to \$5,000, depositing his honorable discharge papers as a kind of security for the loan.

The SECRETARY reads a letter received by Mr. Morrill under date of

November 18, 1943, from the Hon. Robert P. Patterson, Under Secretary of War, acknowledging receipt of the resolution of the Federal Advisory Council on the subject of the final settlement of terminated contracts. Judge Patterson ends his letter: "I think that this resolution is the finest brief statement of this subject I have seen."

KURTZ states he thinks if loans of the Smaller War Plants Corporation were made after the war as a kind of subsidy to small business to get it going, there might be something to be said in favor of such loans. Undoubtedly, after the war many small businesses unless they can obtain assistance will go under and many of them will not be able to obtain credit through the ordinary channels. However, he believes that even after the war banks should be required to take 10% of the risk of any loan made.

The SECRETARY reads the draft of a resolution on this subject, proposed by Mr. Brown, and also two paragraphs suggested by Mr. Huntington as an addition to the resolution as proposed by Mr. Brown.

KURTZ suggests omitting the paragraphs proposed by Mr. Huntington. There was a general feeling that in the form proposed, it might not be advisable to include these paragraphs in the resolution though some of the suggestions made are pertinent and ultimately were embodied in the final form of the resolution, a copy of which is attached to these minutes.

BROWN reverts to the question of allowing commercial banks with savings accounts to invest such savings in restricted issues. He feels there must be a formula which would regulate not merely the amount of each issue the bank might purchase, but, also, the total amount of such securities a bank should be allowed to hold. He points out that there are really three classes of banks: (a) the small country banks, (b) banks in outlying districts of large cities such as Chicago, some of which have \$30 - \$50 million of savings, (c) the large commercial banks having savings accounts. There should be a total ceiling, say 10% which

would mean about \$2 billion.

HARRISON does not see much merit in permitting the investment of such savings in restricted issues as he feels these savings deposits in the case of commercial banks are really the same as demand deposits. At the depth of the depression, the Comptroller of the Currency did not permit banks to demand notice of withdrawal of such deposits.

KURTZ points out that in many cases the state authorities actually compelled savings banks to require notices of withdrawal.

HARRISON would fix a definite dollar limit beside the percentages.

SPENCER points out that the tendency would be, if a ceiling were put on, for many banks to buy at once all that they would be allowed to buy.

BROWN in answer says that what he means is to limit the permissible purchase of restricted securities to 5% of total savings in any one drive and a limit of 25% of savings as the total amount of restricted issues that could be held at any one time.

SPENCER points out that it is his understanding the whole proposal at present is to be merely for the next drive.

BROWN says that the proposal which evidently originated with Mr. A. L. M. Wiggins, President of the A. B. A., was motivated by a desire to help out small banks who are having difficulty meeting their expenses.

The meeting adjourned at 11:50 A. M.

NOTE: On December 7, 1943 at 12:05 P. M. a joint meeting of the Executive Committee 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.

Beside the members of the Executive Committee and its Secretary, previously listed, the following were present from the Board: Chairman Eccles, Vice Chairman Ransom, Governors Szymczak, McKee, and Draper; also, Messrs. Clayton, Morrill, Bethea, Carpenter, Goldenweiser, L. M. Piser, Chief of the Government Securities Section of the Division of Research and Statistics, Wyatt, Vest, Smead, Leonard, Parry, and Paulger.

BROWN raises the question of permitting commercial banks having savings accounts to buy restricted securities issues. He made the statement that the A. B. A. Committee which met at the Treasury, at the time of the last meeting of the Council, had not been consulted by Mr. A. L. M. Wiggins, President of the A. B. A., though he announced at the meeting in the Treasury that the A. B. A. Committee wanted savings to be used to buy restricted issues. Wiggins also filed a memorandum on the subject but this had not been shown previously to the A. B. A. Committee. Brown thinks there ought to be a definite restriction and that in any one drive a bank should not be allowed to invest more than 5% of its savings in restricted securities and at no time should be allowed to invest in all more than 25% of its savings in restricted securities.

FLEMING says in fairness to Wiggins it had been agreed that he was to discuss the matter with Fleming after the meeting at the Treasury. However, owing to a death in his wife's family, Fleming was not available for consultation and Wiggins felt it would not be fair to bother him at that time.

BROWN reads the memorandum prepared by Wiggins which provided that any bank might invest funds of its savings accounts in restricted securities up to a total of \$100,000, or 10% of these savings accounts, whichever is greater.

MCKEE says he is in favor of small banks with savings accounts being given the same privileges as that now enjoyed by mutual savings banks. He thought, however, this privilege should be restricted to banks having not more than one million dollars of savings and the big banks should only be allowed to share only up to the same amount of their savings deposits.

ECCLES joined the meeting at 12:20 P. M. and said he had talked to Mr. Daniel Bell, Under-secretary of the Treasury, and Bell had stated to him that the Treasury regretted having made an announcement indicating that commercial banks having savings accounts might be permitted to buy restricted issues at the next drive. The Secretary of the Treasury thought it might be just as well if it were admitted that the announcement was a mistake and that commercial banks be not allowed to subscribe to restricted issues. There had been some conversation with Messrs. Sproul and Rouse, and others, and there seemed to be a feeling that perhaps banks might be permitted to subscribe up to \$100,000 and that the subscriptions be limited to the F and G bonds. Then there is some talk of permitting banks to buy directly from the Treasury the 2 1/4% issues and lately there has been some idea of permitting the purchase up to \$100,000 of the 2 1/4's or of any market issues like the 2 1/2's. In no event, however, should a bank be allowed to take more of such issues than 100% of its savings accounts and they should be allowed to come in and subscribe at the same time as mutual savings banks are permitted to do so. They should not be allowed to subscribe to the F and G's. The understanding is that this would apply merely to the next drive after which the whole situation should be reviewed.

ECCLES suggested dropping the whole business. The fact is most commercial banks are discouraging savings deposits and are quite ready to lose this business to mortgage banks and to building and loan associations. These latter are very strong in communities of 10,000 and up. He thinks banks have made a mistake in

allowing this competition to be developed and at some later time they may be glad to have savings deposits. The Treasury should not do anything or it should recognize the fact that savings in commercial banks are the same as those in the mutual banks and in building and loan associations and should place no greater limitations on the investment of such savings in commercial banks than in the case of mutual savings banks and building and loan associations. However, there should be an orderly transition and for this reason there ought to be some definite limitation. He personally thinks in the next drive the maximum should be \$100,000, and in no case more than 100% of the savings, and subscriptions should be limited to the two issues, namely, the 2 1/4's and 2 1/2's. He is convinced this will not satisfy anyone.

HARRISON thinks that this proposal of Eccles might be less liberal than that made by Wiggins as Wiggins had suggested \$100,000 or 10%, whichever is greater.

BROWN says there are really three classes of banks and the problem is a somewhat different one in each case. (1) Small Country banks where it might be dangerous to permit 100% of the savings to be invested in the restricted issues. (2) Banks in medium size towns and banks in the outlying districts of large cities where savings accounts are apt to amount to 50% or even more of the total deposits. (3) Real commercial banks whose savings deposits are not more than about 10% of the total deposits of the banks. The trouble with the limitation of \$100,000 is that it does not meet the problem of the banks of intermediate size which have deposits of \$2-\$50 million. These banks are being driven out of the savings bank business and will not pay any interest on savings at present. Large banks can take care of themselves.

ECCLES repeats that \$100,000 does not do any good. Ultimately, banks should be allowed to invest up to 25% of the total savings in restricted issues.

Banks with deposits of \$2 - \$50 million are apt to have anywhere from 30% to 60% of the total deposits in the form of savings accounts and a total of \$100,000 does not help them in the least. He suggests that the members of the A. B. A. Committee present, namely, Messrs. Brown, Spencer, and Fleming try to have an interview with the Under-Secretary of the Treasury, and it was arranged that these gentlemen see Mr. Bell at 3:30 in the afternoon.

BROWN asked for limitations of 5% of the savings in any one drive.

ECCLES asked for 10% and a limitation of \$500,000.

BROWN points out that in the case of outlying banks in Chicago, some of which have savings accounts amounting to \$25 million, a limitation of \$500,000 would simply be meaningless.

ECCLES then argues for 10% in each drive.

BROWN again repeats that he would like to see 5% in each drive and an ultimate limit of 25%.

ECCLES points out that the large banks really do not need the privilege and the Treasury would be afraid of too much shifting of investments, while a 10% and \$500,000 limitation would mean that if the scheme works it could be repeated.

MCKEE points out that small banks are more than before obtaining demand deposits and are not now anxious to have savings deposits. The result is the percentage of savings deposits in small banks is, in relation to total deposits, dropping very markedly. There is real danger that when after the war a change takes place, the small banks will lose their demand deposits and will not really have anything left. He, therefore, believes these banks should be encouraged to hold on to their savings.

ECCLES says 10% with a \$500,000 limitation will mean a total of about one billion dollars for each drive. He believes small banks can put money safely into long-term bonds because due to the Federal Reserve System there is much

liquidity in the small banks - much more than in the case of the building and loan associations and mutual savings banks.

BROWN says in 1907 and 1914 banks could with safety require notices of withdrawal and a similar situation might occur again; simply because the requirement of a notice of withdrawal closed banks at the time of the depression was no proof that this would always be the case. He again argues that a limitation of \$500,000 will not help many of the banks in outlying districts of Chicago and in medium size towns. He feels, however, that on the whole the Council and Board are in agreement, (1) that there should be a percentage limitation each time and (2) that there should be an overall limitation such as perhaps 25%. Eccles is asking for a dollar limitation so that the Treasury will be more ready to consent to the scheme. He repeats that 5% is too little for the smaller banks.

MCKEE says the Treasury is not willing to have more than one billion dollars of restricted issues taken in any one drive by the banks. It might even prefer \$500 million.

HARRISON says that as an experiment, in the next drive, it might be well to permit 10% to help out the smaller banks. If this turned out to be too much in the next drive the amount might be reduced to 5%.

FLEMING says he would like to have F and G's included as he believes that if small banks were to buy too much of the 2 1/2's they might suffer.

ECCLES doubts whether they would suffer.

BROWN says the Board and Council are in substantial agreement.

ECCLES agrees and is glad the members of the A. B. A. Committee and Mr. Harrison will see Mr. Bell at 3:30 in the afternoon.

#### SMALLER WAR PLANTS CORPORATION

BROWN calls attention to the circular and forms put out by the Smaller War Plants Corporation and gives illustrations of how little apparently the heads of

some of the regional offices of the Smaller War Plants Corporation are acquainted with credit requirements. He says that while it had been stated that Mr. A. L. M. Wiggins, President of the American Bankers Association, had supported the Smaller War Plants Corporation, Mr. Wiggins, himself, denied this. All that Wiggins wanted were loans from the Corporation in those cases where other sources were not available and he did not want a 100% guarantee.

THE SECRETARY OF THE COUNCIL reads the resolution adopted by the Committee and attached to these minutes.

In answer to a question by Eccles as to what the Executive Committee wishes to have done with this resolution, Brown answers he would like to see the resolution published.

HARRISON points out a discrepancy in that the resolution states that small banks can not live if the rate on loans is 3% while at the same time the Executive Committee is arguing that these small banks should be allowed to buy bonds bearing an interest rate of 2 1/2%.

ECCLES in answer points out that no one is claiming small banks can exist if their assets were all invested in 2 1/2% bonds. These small banks need a considerably higher rate than 3% on loans in order that the average rate of return on their earning assets be considerably higher than the rate on government bonds.

MCKEE also points out that to service loans costs the bank much more than the expense connected with the purchase of government bonds.

DRAPER is afraid of what the political reaction might be if the resolution proposed by the Executive Committee of the Council should be published.

ECCLES wants to know who the proper people are to whom this resolution could be given. He thinks Donald Nelson is really responsible, and the resolution might well be sent to him. There was some argument as to whether it would be

would be published after a certain lapse of time unless changes were introduced in the practices of the Smaller War Plants Corporation. It was finally decided to send copies of this resolution, with a covering letter addressed to Mr. Morrill and signed by Mr. Brown, to Mr. Donald Nelson and to the members of the Board of Directors of the Smaller War Plants Corporation. The question of releasing the resolution for publication might be taken up by the Executive meeting of the Council at its meeting on January 5.

Mr. Brown's letter addressed to Mr. Morrill reads as follows: "At the meeting of the Executive Committee of the Federal Advisory Council held today a resolution was unanimously adopted in respect to the loans of \$25,000 or less which the Smaller War Plants Corporation is making to business concerns engaged in the production of war material or essential civilian requirements. The Executive Committee of the Council will appreciate it if the Board of Governors of the Federal Reserve System will transmit as soon as possible copies of the enclosed resolution to the Chairman of the War Production Board and the members of the board of directors of the Smaller War Plants Corporation."

The meeting adjourned at 1:30 P. M.