MINUTES OF THE MEETING OF THE FEDERAL ADVISORY COUNCIL

September 18, 1949

The third statutory meeting of the Federal Advisory Council for 1949 was convened in Room 932 of the Mayflower Hotel, Washington, D. C., on Sunday, September 18, 1949, at 2:15 P.M., the President, Mr. Brown, in the Chair.

Present:

Charles E. Spencer, Jr.	District No. 1
W. Randolph Burgess	District No. 2
Frederic A. Potts	District No. 3
Sidney B. Congdon	District No. 4
Robert V. Fleming	District No. 5
J. T. Brown	District No. 6
Edward E. Brown	District No. 7
Henry E. Atwood	District No. 9
James M. Kemper	District No. 10
J. E. Woods	District No. 11
Reno Odlin	District No. 12
Herbert V. Prochnow	Secretary

Absent:

Mr. W. L. Hemingway	District No. 8

A complete list of the items on the agenda for the meeting and the conclusions of the Council are to be found in the *Confidential Memorandum to the Board of Governors from the Federal Advisory Council,* which follows on pages 28, 29, 30 and 31, of these minutes.

The meeting adjourned at 6:37 P.M.

HERBERT V. PROCHNOW
Secretary.

September 19, 1949

At 10:00 A.M., the Federal Advisory Council reconvened in Room 932 of the Mayflower Hotel, Washington, D. C.

Present: Mr. Edward E. Brown, President; Messrs. Charles E. Spencer Jr., W. Randolph Burgess, Frederic A. Potts, Sidney B. Congdon, Robert V. Fleming, J. T. Brown, Henry E. Atwood, James M. Kemper, J. E. Woods, Reno Odlin, and Herbert V. Prochnow, Secretary.

Absent: Mr. W. L. Hemingway.

The Council reviewed its conclusions of the previous day regarding the items on the agenda and sent to the Secretary of the Board of Governors the *Confidential Memorandum to the Board of Governors from the Federal Advisory Council,* which follows on pages 28, 29, 30 and 31, listing the agenda items with the conclusions reached by the Council. The *Memorandum* was delivered to the Secretary of the Board of Governors at 1:00 P.M. on September 19, 1949.

The meeting adjourned at 12:40 P.M.

HERBERT V. PROCHNOW
Secretary.

MEMORANDUM TO THE BOARD OF GOVERNORS FROM THE FEDERAL ADVISORY COUNCIL RELATIVE TO THE AGENDA FOR THE JOINT MEETING ON SEPTEMBER 20, 1949

1. In view of changed economic conditions and the present level of the Government securities market, what should be the policy of the Federal Reserve System with respect to the rediscount rate?

The Council believes that under current conditions it is desirable to retain the present rediscount rate. Any reduction in the rate now would only tend to ease money rates at a time when rates are historically very low. With deficit financing, and with business showing some improvement, it is not desirable to lend encouragement to a possible inflationary trend. Normally the rediscount rate should be a penalty rate. The present rate is low for a period of relative prosperity. A reduction in the rediscount rate now would also tend to increase the prices of Government securities and would therefore make more difficult the Treasury and Open Market Committee responsibilities in connection with the Government security markets.

2. What are the views of the Council as to business trends during the remainder of 1949?

The business trend at present is moderately upward from its low of recent months, and it is probable that it will continue upward for the remainder of 1949. Developments which might threaten a continuance of this trend are strikes in such major industries as steel, coal and the railroads and effects of the British devaluation.

3. Does the Council have any comments to make on the credit policy actions taken by the Federal Reserve System since the last meeting of the Council?

The Council is in agreement with the June statement indicating a departure from the policy of maintaining a fixed pattern of rates. The Council also approves the reductions in reserve requirements that have been made. These actions have been an encouraging influence on business sentiment. Looking backward, the Council believes it would have been helpful if the Federal Reserve System had released securities to the market more promptly in late June and early July and if interest rates had not been permitted to fall so low. The Council also believes the whole bond market would be in sounder condition if the System had released and were currently releasing bonds more freely from its portfolio.

4. Does the Council wish to express any opinion at this time with respect to the future refunding program of the Treasury?

The Council believes that the Treasury's announcement that it proposes to issue notes to refund the bonds coming due in December is a step in the right direction. As the program develops, it should include refunding into both intermediate and longer-term issues. Too large a proportion of the Federal debt is now in short-term securities, especially when considered in connection with the amount of savings bonds outstanding and with the steadily shortening maturities of the present long-term issues.

5. What are the views of the Council with respect to the following legislative proposals:

   a. A basic revision in the law relating to reserve requirements which would base requirements on types of deposits rather than location of the bank, and would be applicable to nonmember as well as member banks.

(a) The Council is unanimously of the opinion that neither the Board of Governors nor any Federal agency should have authority to fix the reserve requirements of non-member banks.

As to the reserves of member banks, while the Council recognizes that there is some lack of logic in the present basis for determining reserves, the banking system has over the years grown up with this arrangement and has operated effectively under it. Before the Council expresses its opinion on a change to some other basis, the Council desires more opportunity to study specific proposals and their effects on individual banks and on the banking system.

b. The authority of the Federal Reserve Banks with respect to industrial loans.

(b) On March 11, 1947, the majority (with a minority dissenting) of the Council supported S. 408 with certain amendments but with the following qualification:

"The Council's support, with these amendments, of Bill 408 is given in the belief that some safety valve is desirable for emergency credit situations, and with the recommendation that the lending and guarantee powers of certain other government agencies, including the R. F. C., should be greatly curtailed, and in many instances should be terminated."

At the time of the above statement by the Council, Congress was considering a restriction of the lending and guarantee powers of the RFC to emergency situations. Subsequent legislation has continued the RFC with broad powers, and there is no present prospect of reducing these powers. The Council is opposed to two government agencies having lending or guarantee powers in the same field and therefore would not favor giving additional guaranteeing powers to the Federal Reserve Banks in the industrial field.

c. H.R. 5749, introduced in the House of Representatives by Chairman Spence on July 25, 1949, "To amend Section 9 of the Federal Reserve Act, as amended, and for other purposes." This bill, proposed by the Board, relates to capital requirements for membership and the establishment of branches by member banks.

(c) The Council favors H.R. 5749.

6. The Board would like to have the views of the members of the Council on the proposal contained in the enclosed letter dated August 10, 1949, addressed to Mr. Leonard, Director of the Board's Division of Bank Operations, by Mr. Joseph J. Lawler, Third Assistant Postmaster General, outlining a plan which the Post Office Department has under consideration with respect to issuance and collection of Postal money orders. There is also enclosed a copy of a memorandum prepared by Mr. Leonard under date of August 11, 1949, regarding a meeting of representatives of the Post Office Department with members of the Board's staff at which the proposal was discussed.

The Council favors the proposal relating to the issuance and collection of Postal money orders provided the Federal Reserve Banks are fully reimbursed for their total expense in handling these items including a reasonable amount for overhead.

7. Should the holding company bill not include an exemption for wholly-owned trust companies?

The Council believes that the holding company bill should be amended to exempt wholly-owned trust companies not doing a commercial banking business. Such an exemption would not interfere with the primary purpose of the bill.

8. The question of the attitude of the Federal Reserve Board toward H.R. 5512 which would give the Federal Land Banks the power to borrow from the Federal Reserve Banks for one year at the Federal Reserve discount rate.

In the judgment of the Council the provisions of H.R. 5512 would provide for an improper use of central banking facilities and are unsound. The adoption of such legislation would inevitably lead to pressure for similar privileges by other Government lending agencies. The Council would appreciate knowing the position of the Board on this bill.

9. The Board has sent to the members of the Council a confidential staff study relative to deposit insurance coverage and the rate and base of deposit insurance assessments. The Board would appreciate the current views of the Council concerning any changes that should be made in deposit insurance coverage and the rate and base of deposit insurance assessments.

On May 17, 1949, the Council made the following statement to the Board of Governors regarding the subject of deposit insurance:

"The Council is familiar with the discussions on this matter which the Federal Deposit Insurance Corporation has had with a committee of the American Bankers Association. Without being committed to any particular formula, the Council favors in general an approach to this subject on the basis of these discussions.

"Specifically, the Council believes any legislation should include the following points:

A. No increase should be made in the present insurance coverage of $5,000;

B. The maximum assessment in any one year should not exceed one-twelfth of one per cent;

C. Provision should be made for maintaining the integrity of the fund by establishing a statutory formula for an automatic scale of assessments, based on the previous years' losses and expenses, to range from no assessment, or an assessment of a nominal amount, under present conditions, to a maximum of one-twelfth of one per cent per annum.

"In any study for the purpose of determining the adequacy of Federal Deposit Insurance Corporation funds and the rate of assessments, the Council suggests the importance of considering not only the possible losses of the Federal Deposit Insurance Corporation but also the effect on bank earnings, capital and dividends of the steady drain of assessments. These assessments reduce the power of the individual bank to make its own provision for losses."

The Council appreciates the opportunity it has been given to examine the confidential staff study, which the Council regards as an important contribution to the consideration of this subject. The Council also appreciates the interest the Board is taking in these phases of Federal deposit insurance which are of such vital importance to all banks. In the light of discussions now taking place among various interested groups, the Council does not at this stage of these discussions wish to commit itself to specific proposals. In the meantime the Council will give the matter further study.

10. Discussion of H.R. 1689.

In connection with H.R. 1689, the Council has unanimously approved the resolution which follows for transmission to Senator Maybank as Chairman of the Senate Committee on Banking and Currency:

RESOLUTION

"The Federal Reserve System is this country's Central Bank. Its decisions are of grave importance for the Nation's well-being. They influence the trend of business and employment.

"The Board of Governors of the Reserve System is the top command of the System. It should be manned by the ablest and best qualified people in the country. When the System was set up, the salaries of the Board were placed at the same level as members of the Cabinet and that relationship has been continued until the present.

"H.R. 1689 would break this sound tradition by treating the Board simply as a minor regulatory agency. This would lower the prestige of the Board and make it much more difficult to persuade able men to be its members. It would impair its influence upon banks and the public and cripple it for its essential service to the Nation.

"We recommend that members of the Board be placed on a higher salary level, preferably $20,000."

* * * * * * *

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

September 20, 1949

At 10:45 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 Thomas B. McCabe; Governors Marriner S. Eccles, M. S. Szymczak, Ernest G. Draper, James K. Vardaman, Jr., and Lawrence Clayton; also, Mr. S. R. Carpenter, Secretary of the Board of Governors.

Present: Members of the Federal Advisory Council:

Mr. Edward E. Brown, President; Messrs. Charles E. Spencer Jr., W. Randolph Burgess, Frederic A. Potts, Sidney B. Congdon, Robert V. Fleming, J. T. Brown, Henry E. Atwood, James M. Kemper, J. E. Woods, Reno Odlin, and Herbert V. Prochnow, Secretary.

Absent: Mr. W. L. Hemingway.

President Brown requested and received permission of the Board to consider the last item on the agenda first, because the Council felt the item was the most important. President Brown then read the item and the conclusions of the Council as given in the *Confidential Memorandum to the Board of Governors from the Federal Advisory Council,* as printed on pages 28, 29, 30 and 31, of these minutes.

An off-the-record discussion followed.

The President of the Council then read the first and second items on the agenda, which were closely related, and the conclusions reached by the Council, as expressed in the *Confidential Memorandum* previously mentioned. At the request of Chairman McCabe, the ensuing discussion was off the record.

President Brown read the third item on the agenda and the conclusions of the Council included in the *Confidential Memorandum,* which is a part of these minutes. A brief discussion of recent open market activities followed.

President Brown than read agenda item 4 covering the refunding program of the Treasury and the conclusions of the Council as stated in the *Confidential Memorandum,* included in these minutes on pages 28, 29, 30 and 31. Chairman McCabe stated that the Board is in general agreement with the Council on this item.

President Brown than read item 5a of the agenda and the conclusions of the Council as given in the *Confidential Memorandum* cited above.

Chairman McCabe raised the question as to the leadership of the correspondent banks in correcting the present inadequacies and inconsistencies in reserve requirements in various states.

Dr. Burgess replied that the A. B. A. has part of its staff working on a uniform banking code and some progress in that direction has been made. He believes a very large percentage of the deposits are now represented by Federal Reserve membership or are in states having good reserve laws.

President Brown read item 5b on the agenda and the conclusions of the Council as given in the *Memorandum to the Board of Governors* previously mentioned. Chairman McCabe stated that he thought it was unnecessary to discuss this item.

President Brown read item 5c on the agenda and the conclusions of the Council as stated in the *Confidential Memorandum* previously cited. There was no further comment by either members of the Board or the Council.

President Brown read item 6 on the agenda and the conclusions of the Council as expressed in the *Confidential Memorandum* mentioned above.

President Brown read item 7 on the agenda and the conclusions of the Council as given in the aforementioned *Memorandum.* Chairman McCabe stated it is difficult to work out this matter, but he hopes something may be done about it.

President Brown then read item 8 on the agenda and the conclusions of the Council as expressed in the *Memorandum* cited above. Mr. Clayton stated that the Board and the Council are in agreement on this matter.

President Brown read the agenda item relative to changes in F.D.I.C. coverage, the rate and base of insurance assessments and the conclusions of the Council as given in the *Confidential Memorandum.* Mr. Eccles suggested that the Council might appoint a committee to work with the Chairman of the Board on the report the Chairman will make to the Joint Committee on the Economic Report on this subject by October 15, 1949.

The members of the Council and the Board agreed that the next meeting would be held on November 13, 14 and 15, 1949.

The meeting adjourned at 1:35 P.M.

HERBERT V. PROCHNOW
Secretary.

MINUTES OF THE MEETING OF THE FEDERAL ADVISORY COUNCIL

September 20, 1949

At 2:30 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; Messrs. Charles E. Spencer Jr., W. Randolph Burgess, Frederic A. Potts, Sidney B. Congdon, Robert V. Fleming, J. T. Brown, Henry E. Atwood, James M. Kemper, J. E. Woods, Reno Odlin, and Herbert V. Prochnow, Secretary.

Absent: W. L. Hemingway.

The Council unanimously approved the appointment of a committee consisting of Mr. Robert V. Fleming, Chairman, Dr. W. Randolph Burgess, and Mr. Frederic A. Potts, to work with the Chairman of the Board of Governors during the preparation of the report the Chairman has been asked to submit to the Joint Committee on the Economic Report relative to the subject of Federal Deposit Insurance.

The meeting adjourned at 3:10 P.M.

HERBERT V. PROCHNOW
Secretary.

On September 20, 1949, President Brown, accompanied by Mr. Fleming and Mr. Burgess, presented the following letter and Resolution to Senator Burnet R. Maybank:

FEDERAL ADVISORY COUNCIL

September 19, 1949

The Honorable Burnet R. Maybank
Chairman, Committee on Banking and Currency
United States Senate
Washington 25, D. C.

My dear Senator Maybank:

On behalf of the Federal Advisory Council, I am pleased to enclose for your consideration a Resolution which the Council passed today with reference to HR-1689.

It is the opinion of the Council that to leave the Board of Governors in the salary classification in which they are placed in the House Bill may have far-reaching repercussions in the conduct of the Federal Reserve System in the future.

Respectfully yours,

(Signed) E. E. Brown
President

Enclosure

RESOLUTION OF THE FEDERAL ADVISORY COUNCIL OF THE FEDERAL RESERVE SYSTEM WITH RESPECT TO H. R. 1689, SETTING NEW SALARY SCHEDULES FOR VARIOUS GOVERNMENT OFFICIALS

"The Federal Reserve System is this country's Central Bank. Its decisions are of grave importance for the Nation's well-being. They influence the trend of business and employment.

"The Board of Governors of the Reserve System is the top command of the System. It should be manned by the ablest and best qualified people in the country. When the System was set up, the salaries of the Board were placed at the same level as members of the Cabinet and that relationship has been continued until the present.

"H. R. 1689 would break this sound tradition by treating the Board simply as a minor regulatory agency. This would lower the prestige of the Board and make it much more difficult to persuade able men to be its members. It would impair its influence upon banks and the public and cripple it for its essential service to the Nation.

"We recommend that members of the Board be placed on a higher salary level, preferably $20,000."

* * * * * * * * *

September 19, 1949

REPORT OF SUB-COMMITTEE OF THE FEDERAL ADVISORY COUNCIL ON F.D.I.C. ASSESSMENTS

This Sub-committee of the Advisory Council was appointed with power at the meeting of the Council on September 20, 1949 to give further consideration to Federal Deposit Insurance assessments in the light of the study prepared by the Staff of the Federal Reserve Board. After individual consideration of the problem, the Committee has met in Washington on October 4 and 5, and the following are its suggestions to the Federal Reserve Board.

The Committee wishes first to express its appreciation of the breadth and thoroughness of the study prepared by the Board's Staff. This is the most complete assembling of data and consideration of the questions at issue that the Committee has seen. In general, the Committee finds itself in concurrence with the broad approach to the problems and the line of reasoning of the Staff report, with reservations at some points.

The greatest difficulty may lie not in the broad objectives to be sought, but in securing agreement on a program. The American Bankers Association has a committee which has been at work on the subject for six years and has been carrying on conversations with the Federal Deposit Insurance Corporation as to modifications in the law. A number of other government agencies are concerned in the matter. From various sides many different suggestions have been made. It is our belief that the Federal Deposit Insurance Corporation is the agency which should present to the Congress a specific program based on its experience and studies. While the Federal Reserve System is broadly concerned in the matter, this is not primarily a Federal Reserve problem, and the Council at its two preceding meetings has given the Committee guidance in not wishing to sponsor a specific detailed plan. The Committee, therefore, in this report will rather emphasize certain principles which should be followed.

1. *Reduction of assessment.* The Committee can speak for the Council in its emphatic agreement with the Staff report as to the desirability of a prompt and substantial reduction in F.D.I.C. assessments. The Staff report reviews convincingly the loss experience both under the F.D.I.C. and previously. The capital of the banks in the country is now thirteen billion dollars. The F.D.I.C. at the end of this year will have one billion two hundred million of reserve funds and borrowing capacity at the Treasury of an additional three billion dollars. These are substantial sums in relation to fifty billion dollars of "risk assets" held by banks, on most of which we believe the risk is slight.

The point which the Committee would emphasize more vigorously than is done in the Staff report is the present need for larger bank earnings in order to accumulate bank capital more rapidly and to reopen the bank share market by giving the bank shareholder a fairer return. Bank shares are now selling at a heavy discount from their liquidating value, and most banks find it difficult to sell their shares in the market at fair prices to obtain new capital. Thus, from a long-range point of view of the strength of the American banking system and its capacity to finance expanding American business, the bank capital position needs to be improved over a period both by earnings and by the sale of securities in the market. A reduction in F.D.I.C. assessments will be a material aid towards this objective.

2. *Nature of assessments.* The Council has steadily taken the position that in any revision of F.D.I.C. assessments "provision should be made for maintaining the integrity of the fund" by the continuation of some assessment, and the characteristics of this assessment should be (a) that fluctuations in the amounts should be statutory, with variations set by the law rather than by any board's current decision, (b) that the maximum assessment in any one year should not exceed 1/12 of 1%, and (c) that the annual assessment should be based on previous experience as to losses and expenses of the corporation, which together have recently been running under ten million dollars a year.

In the matter of the top assessment, the Staff report suggested 1/10 of 1% rather than the present 1/12. We believe that 1/12 is large enough, and it is accepted by the banking community and by the public as an appropriate maximum rate.

As to the length of past experience on which the changes in the assessment should be based, the Staff report makes the suggestion that a ten-year moving average is a sounder basis than a single previous year's experience. This avoids imposing a severe increase in the assessment at a time of depression. The Committee is impressed with the Staff proposal on this point, and believes this is one of the details on which the F.D.I.C. might be asked to make a definite recommendation. The question is partly one of the public reaction to reductions in the fund and the length of time that it would take to restore losses incurred. Our general feeling is that an average of a shorter period than ten years might be more acceptable from the public point of view.

3. *Coverage.* The Advisory Council at its May meeting stated its opposition to an increase in the coverage over $5,000. This Committee recognizes, however, the conclusion of the Staff that an increase in the coverage would not be inconsistent with or should not interfere with a substantial reduction in the assessment. We also recognize that there is a certain amount of agitation for an increase in the coverage, particularly on the part of small banks. It is our belief, however, on the basis of surveys made by the American Bankers Association and other agencies, that this agitation is not substantial in scope, and we entertain doubt as to whether, in fact, smaller banks would be materially benefited in their deposits by an increase in the coverage. The matter should, however, be decided on broader public considerations. There does not appear to be from the public, as distinguished from the banks, any demand for an increase in coverage, and the present coverage does protect the small depositor, for whom it was primarily intended.

While we recognize that as it has been operated, deposit insurance has, in a great number of cases, protected entire banks through the purchase of assets, we are not convinced that situations may not arise in the future where the other method originally contemplated in the Act, of liquidating the bank and paying off from deposit insurance deposits of $5,000 and less, may not be a desirable method of procedure. If that proves to be the case, the limitation on the coverage will be conservative and desirable. We understand that the F.D.I.C. is making a survey of this problem, and suggest that final recommendations be deferred pending its completion.

It should be noted that the Federal Savings and Loan associations are now operating under an insurance program which also has a $5,000 limit, and that any change in the F.D.I.C. coverage may well be taken as a basis for a demand for an increase in the coverage in this other field, where the experience is still very limited and where a change now would involve substantial risks. Every extension of the principle of government guaranties needs to be examined with the utmost care before adoption.

4. *Simplification of accounting basis for assessments.* The Committee agrees completely with the Staff report as to the desirability of simplifying the basis for assessment and bringing it into harmony with the definitions in the Call Reports of the Comptroller and the Federal Reserve. The present uncertainties are disturbing, and a considerable savings in expenses could be effected by the proposed procedure.

5. *Relationship of size of fund to deposit total.* The Committee has given consideration to the suggestion of the Staff report that the fund be related to total bank deposits. It is the Committee's feeling that this is an unnecessary complication of the program. Legislation on this subject should be as simple as possible. The various proposed plans now under consideration for the continuation of assessments make provision for a continued increase in the fund year by year, in addition to the coverage of expenses and losses. This increase

in the fund is in the neighborhood of 3%, which is about the same rate of growth as in the country's business. It seems to us, therefore, that there is adequate provision for growth without introducing an additional formula. If there were a formula, we would question basing it on total deposits.

6. *Treatment of new members*. The Staff report raises the question whether new members of the F.D.I.C. system should pay larger assessments for a few years. It is our belief that this is a question which could well be left to the F.D.I.C. for its recommendation. New members would necessarily have small resources, and the contribution to the fund would be in negligible amounts.

Signed W. Randolph Burgess

Frederic A. Potts

Robert V. Fleming, Chairman

October 5, 1949

NOTE: This transcript of the Secretary's notes is not to be regarded as complete or necessarily entirely accurate. The transcript is for the sole use of the members of the Federal Advisory Council. The concise official minutes for the entire year are printed and distributed later.

H. V. P.

The Secretary's notes on the meeting of the Federal Advisory Council on September 18, 1949, at 2:15 P.M., in Room 932 of The Mayflower Hotel, Washington, D.C. All members of the Federal Advisory Council were present except Mr. Hemingway.

IN VIEW OF CHANGED ECONOMIC CONDITIONS AND THE PRESENT LEVEL OF THE GOVERNMENT SECURITIES MARKET, WHAT SHOULD BE THE POLICY OF THE FEDERAL RESERVE SYSTEM WITH RESPECT TO THE REDISCOUNT RATE?

E. E. Brown understands the Board of Governors may be pressing for a lower rediscount rate, whereas he has heard that the bank members on the Open Market Committee do not desire to make a change in the rate.

Potts states that Williams of the Federal Reserve Bank of Philadelphia tells him he is against any change now.

Burgess does not believe a reduction in the rediscount rate would be of any benefit to business now.

E. E. Brown. Lowering the rediscount rate to 1 1/4 per cent would probably reduce the certificate rate to one per cent. From January to May the Board was fighting inflation. After that each step the Board took was to fight deflation. It is questionable whether the present business upturn is permanent. If inflation is still a threat, then the rediscount rate should not be lowered.

Potts believes that the best reason for not lowering the rediscount rate now is the upturn in business. No one knows for certain whether this upturn is permanent. Deficit financing is also inflationary.

Burgess. We are in a state of prosperity and should not do now what should be done at the bottom of a depression.

Congdon agrees with the comments of Burgess and Potts.

Atwood agrees with the previous comments. He states that the rediscount rate is so low now that it would be advisable to retain the little power the Board has left in the rate.

Odlin states that the Board should withhold action now and retain some of the power still remaining in the present rate.

Kemper agrees with the previous comments but is inclined to think the Board will reduce the rate.

J. T. Brown agrees with the views already expressed. He sees no good reason for reducing the rate.

Woods sees no logical reason to reduce the rate.

Spencer is in agreement with the previous comments.

Odlin emphasizes that the rediscount rate should be a penalty rate.

E. E. Brown states that the conclusions submitted to the Board might include the following points: (1) no change should be made in the rediscount rate, unless there is an important or marked change in the level of the economy; (2) a reduction in the rate would only bring easier money rates and money rates now are historically low. In May or June when there was greater business uncertainty there may have been some justification for reduction; (3) with deficit financing, and with business now increasing, it is not desirable to encourage a possible inflationary trend.

Burgess. The business recession was never fully completed. It is better not to overstimulate the economy now.

E. E. Brown. Except during war, the rediscount rate should be a penalty rate and it should have some stability.

Odlin believes that the views of the Council on this point should be stated positively rather than negatively. It would be better to state that the Council is in favor of retaining the present rediscount rate rather than that the Council is opposed to changing the rate.

Kemper. By cheapening money too much we may engender false optimism.

WHAT ARE THE VIEWS OF THE COUNCIL AS TO BUSINESS TRENDS DURING THE REMAINDER OF 1949?

E. E. Brown. The business trend is moderately upward and barring serious strikes in such industries as steel, coal, and the railroads, the trend may continue upward for the balance of the year.

Congdon believes the economy has passed the low point in the recent swing of the cycle, and the trend may be upward in the months immediately ahead.

Burgess. There are three developments which may threaten the continuance of the upward trend. These threats to the upward movement are: (1) strikes; (2) the British situation; and (3) the hesitancy of some business concerns to make capital expenditures.

Fleming. The statistics indicate that in the months ahead we shall have deficit financing by the Federal government, together with substantial sums of money being expended by state and local governments.

E. E. Brown thinks the present rediscount rate should be retained. Business is at least temporarily on the upgrade. Interest rates are already historically low. When the business trend was downward several months ago, it might have been possible to justify a decrease in the rediscount rate. However, with deficit financing, and with the pressure for higher wages, there is no assurance that the inflationary spiral may not start again.

Congdon. If the rediscount rate is reduced, resulting in higher prices for government securities, the problem of handling the government security markets will be further complicated.

E. E. Brown. A reduction in the rediscount rate would complicate and make far more difficult the Treasury and Open Market Committee responsibilities in connection with the government security markets.

DOES THE COUNCIL HAVE ANY COMMENTS TO MAKE ON THE CREDIT POLICY ACTIONS TAKEN BY THE FEDERAL RESERVE SYSTEM SINCE THE LAST MEETING OF THE COUNCIL?

E. E. Brown. The System has not put out bonds the Federal Reserve banks hold.

Burgess. The Federal Reserve banks have not pumped out bonds into the market. Buyers could not get them and the markets were forced up.

E. E. Brown. The bond market unpegging was a step in the right direction.

Fleming states that the Council may say it was in sympathy with the reduction in reserves, but believes it would have been helpful if the System had released securities to the market more promptly.

E. E. Brown thinks that the memorandum to the Board may state approval of the reductions in reserve requirements and agreement with the June statement indicating a departure from the policy of maintaining a fixed pattern of rates. The Council may also state that securities were not fed out soon enough.

Congdon believes the Council may approve the June statement, but may state that more prompt action in supplying the market with securities would have been advisable.

Burgess. It would have been desirable to have unloaded some of the bond holdings of the System.

Woods. The Board may argue that selling bonds would have absorbed some of the released reserves.

Fleming believes that the Council may approve the policies in general, but state that more prompt astion in supplying the market with securities would have been desirable.

E. E. Brown states that lowering the reserve requirements and the June statement may have been helpful in causing business to take an upturn, or at least may have stimulated the upturn.

Burgess thinks the stimulation in business was due primarily to the necessity of increasing inventories.

Potts believes the Board's actions have been helpful, but that low inventories were a factor.

Congdon believes that the Board's actions were a minor factor.

Fleming. The inventory situation was a major factor, but the Board's actions helped.

Odlin believes the Board's actions were good.

Kemper thinks the Board's actions constituted one of the major factors in stimulating business.

J. T. Brown. The Board's actions were important, plus the inventory situation.

Woods. The Board's actions were helpful, and it may have been coincidence that they came simultaneously with the upturn.

Spencer. The Board's actions were helpful.

Atwood believes the Board's actions were coincidental with the upturn.

Burgess. The Board moved in the right direction.

J. T. Brown. The Board's actions were timely.

E. E. Brown. The Council believes the Board's actions in reducing reserve requirements and in announcing the policy that looked toward the unpegging of the bond market have been encouraging influences on business sentiment.

Burgess. There is the question of whether the System was prompt enough in supplying the market with securities early in July.

E. E. Brown. Looking backward, somewhat prompter action in releasing government securities might have been desirable.

Congdon believes the Council may approve in principle the Board's actions and agree they were helpful in the limited area in which such influences operate.

Burgess states that the Council may say it is in agreement with the June announcement, as the Council understands it, and with the reductions in reserves that have been made.

E. E. Brown. The Council may add in its statement that looking backward, the Council believes it would have been helpful if the System had released securities to the market more promptly in late June and early July.

Burgess. The market was very clumsily handled.

E. E. Brown. The Council may also state it feels there has been a tendency to drive interest rates lower, which was unfortunate.

Burgess. The Council may state it does not feel it was necessary to permit interest rates to fall so low.

DOES THE COUNCIL WISH TO EXPRESS ANY OPINION AT THIS TIME WITH RESPECT TO THE FUTURE REFUNDING PROGRAM OF THE TREASURY?

Fleming. The Treasury is taking the first step in December to lengthen maturities. The Council may state it believes the Treasury's announcement relative to the bonds maturing in December is a step in the right direction and should be continued as the program develops. It should include intermediate and longer-term issues. In the judgment of the Council, too large a proportion of the Federal debt is now in short-term securities, especially when it is considered in connection with savings bonds which are demand obligations. Moreover, the long-term issues are steadily becoming of shorter maturity.

E. E. Brown notes that all members of the Council are in agreement with Fleming's comments.

WHAT ARE THE VIEWS OF THE COUNCIL WITH RESPECT TO THE FOLLOWING LEGISLATIVE PROPOSALS:

a. A BASIC REVISION IN THE LAW RELATING TO RESERVE REQUIREMENTS WHICH WOULD BASE REQUIREMENTS ON TYPES OF DEPOSITS RATHER THAN LOCATION OF THE BANK, AND WOULD BE APPLICABLE TO NONMEMBER AS WELL AS MEMBER BANKS.

Odlin. The Council may say at the outset that it is opposed to subjecting nonmember banks to regulation by the Board of Governors.

E. E. Brown. The Council may state that it is unanimously of the opinion that neither the Federal Reserve Board nor any Federal agency should have authority to fix the reserve requirements of nonmember banks. The uniform reserve system is probably a more logical one than the basis of determining reserves by cities. There is also a fundamental question of whether reserve requirements should be fixed by law.

Congdon. Any change in the present basis is unsettling. There is perhaps some fault in the present reserve requirements, and the whole matter should be given further study.

Odlin. The present arrangement for determining reserves works quite well and there is no reason to change simply to change.

E. E. Brown believes the Bopp proposal is more logical than some proposals previously made.

Burgess. The Council may state it would be pleased to give further study to the matter. Any change is upsetting. The Council is opposed to including nonmember banks. There should be a ceiling on reserves which would permit banks to live.

E. E. Brown. The Council may first say that nonmember banks should not be subject to the authority of the Board or any Federal agency. It may then state that as to member banks the Council recognizes some lack of logic in the present basis, but the country has adjusted itself to this arrangement and the banking system has operated well under it. Before the Council expresses an opinion on a change to another basis, the Council would need an opportunity to study specific proposals and their effects on groups of banks and on the banking system.

WHAT ARE THE VIEWS OF THE COUNCIL WITH RESPECT TO THE FOLLOWING LEGISLATIVE PROPOSALS:
b. THE AUTHORITY OF THE FEDERAL RESERVE BANKS WITH RESPECT TO INDUSTRIAL LOANS.

E. E. Brown. In connection with this item, the Council may call attention to its statement to the Board on March 11, 1947, relative to S. 408. At that time it appeared possible to restrict R. F. C. loans to emergency situtations. At present it does not appear to be possible so to restrict the R. F. C. The Council is opposed to two government agencies having lending or guarantee powers in the same field. The Council would prefer to leave Section 13b as it stands.

Atwood favors the statement which E. E. Brown has made and all members of the Council agree.

WHAT ARE THE VIEWS OF THE COUNCIL WITH RESPECT TO THE FOLLOWING LEGISLATIVE PROPOSALS:
c. H. R. 5749, INTRODUCED IN THE HOUSE OF REPRESENTATIVES BY CHAIRMAN SPENCE ON JULY 25, 1949, "TO AMEND SECTION 9 OF THE FEDERAL RESERVE ACT, AS AMENDED, AND FOR OTHER PURPOSES". THIS BILL, PROPOSED BY THE BOARD, RELATES TO CAPITAL REQUIREMENTS FOR MEMBERSHIP AND THE ESTABLISHMENT OF BRANCHES BY MEMBER BANKS.

Fleming believes the Council should approve H.R. 5749.

E. E. Brown asks for an expression of opinion from each member of the Council and all approve H.R. 5749.

THE BOARD WOULD LIKE TO HAVE THE VIEWS OF THE MEMBERS OF THE COUNCIL ON THE PROPOSAL CONTAINED IN THE ENCLOSED LETTER DATED AUGUST 10, 1949, ADDRESSED TO MR. LEONARD, DIRECTOR OF THE BOARD'S DIVISION OF BANK OPERATIONS, BY MR. JOSEPH J. LAWLER, THIRD ASSISTANT POSTMASTER GENERAL, OUTLINING A PLAN WHICH THE POST OFFICE DEPARTMENT HAS UNDER CONSIDERATION WITH RESPECT TO ISSUANCE AND COLLECTION OF POSTAL MONEY ORDERS. THERE IS ALSO ENCLOSED A COPY OF A MEMORANDUM PREPARED BY MR. LEONARD UNDER DATE OF AUGUST 11, 1949, REGARDING A MEETING OF REPRESENTATIVES OF THE POST OFFICE DEPARTMENT WITH MEMBERS OF THE BOARD'S STAFF AT WHICH THE PROPOSAL WAS DISCUSSED.

E. E. Brown. This proposal tends to place money orders on the same basis as cashier's checks. It may cut down the sale of cashier's checks.

Fleming. It would be an improvement as to mechanics, but the rate charged may determine how competitive it will make Postal money orders to cashier's checks.

Kemper. It would compete with special types of checking accounts, and may also tend to make some persons do their banking at the post office.

Congdon does not believe it will change the habits of the people a great deal.

J. T. Brown agrees and says that in many small towns the postmaster is the orneriest person in town. Consequently, the banks should have no trouble in competing.

E. E. Brown. The Council cannot logically oppose the proposal from an expense basis. The post office agrees to pay the costs, but the question of whether it makes the post office more competitive with the banks is a matter for consideration. From the operating standpoint it improves the present situation, but it may take some transactions out of the banks and make the post office more competitive with the banks. Perhaps the Council can state that it has no objection to the proposal provided the Federal Reserve banks are fully reimbursed for their expenses in handling these items, including a reasonable amount for overhead.

Woods thinks that it may result in small banks losing some business, but it will not be particularly harmful.

Potts states that a committee of the American Bankers Association has approved it.

SHOULD THE HOLDING COMPANY BILL NOT INCLUDE AN EXEMPTION FOR WHOLLY-OWNED TRUST COMPANIES?

E.E. Brown asks the opinion of the members of the Council on this question and the members unanimously approve the exemption of wholly-owned trust companies from the provisions of the holding company bill.

Burgess reports that the Board had turned down the request for such exemption.

Spencer reads a copy of a letter he received from the Board on this matter.

Odlin. It would seem unwise to draw the bill so it incurs the enmity of those whom the bill is not intended to reach.

E. E. Brown. The Council may state that it believes the holding company bill should be amended to exempt wholly-owned trust companies not doing a commercial banking business. The Council believes such an exemption would not interfere with the primary purpose of the bill.

THE QUESTION OF THE ATTITUDE OF THE FEDERAL RESERVE BOARD TOWARD H. R. 5512 WHICH WOULD GIVE THE FEDERAL LAND BANKS THE POWER TO BORROW FROM THE FEDERAL RESERVE BANKS FOR ONE YEAR AT THE FEDERAL RESERVE DISCOUNT RATE

Fleming states that Riefler told him the Board did not wish this power.

Burgess thinks the Council ought to ask the Board why the Board did not object to H. R. 5512.

E. E. Brown. No government agency should have the power to borrow from the Federal Reserve banks.

Burgess. The Federal Reserve banks can buy land bank bonds when these bonds are within six months of their maturity. The Council may state it is opposed to H. R. 5512 and would appreciate knowing the position of the Board on the bill.

E. E. Brown. The Council may report that it believes the provisions of H. R. 5512 are unsound and that the adoption of such legislation would open the door to requests for similar privileges by the R. F. C., the Commodity Credit Corporation and other government agencies.

THE BOARD HAS SENT TO THE MEMBERS OF THE COUNCIL A CONFIDENTIAL STAFF STUDY RELATIVE TO DEPOSIT INSURANCE COVERAGE AND THE RATE AND BASE OF DEPOSIT INSURANCE ASSESSMENTS. THE BOARD WOULD APPRECIATE THE CURRENT VIEWS OF THE COUNCIL CONCERNING ANY CHANGES THAT SHOULD BE MADE IN DEPOSIT INSURANCE COVERAGE AND THE RATE AND BASE OF DEPOSIT INSURANCE ASSESSMENTS.

E. E. Brown reviews briefly some of the provisions of the staff study relative to deposit insurance coverage and the rate and base of deposit insurance assessments. Each member of the Council has received a copy of this confidential staff study.

Burgess. The Council may report that it is not prepared to make detailed recommendations without a further study of the matter. The Council may call attention to the views it expressed to the Board of Governors on May 17, 1949.

E. E. Brown asks the Secretary to read the statement the Council made to the Board on May 17, 1949.

Kemper believes the small banks want more coverage. Practically speaking, he thinks that it makes no difference if the coverage is increased. The only chance of the bill being enacted into law depends upon an agreement to increase the insurance coverage.

E. E. Brown. The Council may call attention to its statement of May 17, 1949. The Council may then add that it understands the whole matter of deposit insurance coverage and assessments is still under consideration. If the assessments are reduced, it is possible the Council may not object to a moderate increase in coverage. Brown thinks there is some merit in the proposal to determine the assessment on a five-year basis instead of one year.

Burgess believes the Council may cite its previous comments to the Board on the subject as expressed on May 17, 1949. The Council may also state it appreciates the opportunity of considering the confidential staff study. It may further call attention to the following two points which impressed the Council as throwing more light on the subject: (1) the possibility of an increase in coverage at the same time that there is a decrease in the assessment; and (2) the use of a period of years, instead of one year, as a basis for determining the assessment.

Congdon. As a third point, the Council might mention the simplification of the base for determining the assessment.

Burgess. The Council may also state that pending an opportunity for further discussion, the Council does not wish to commit itself to the specific proposals of the study.

Potts does not find country bankers with whom he has discussed the matter desirous of increasing the insurance coverage.

DISCUSSION OF H. R. 1689.

E. E. Brown states that McCabe had telephoned him about bill H. R. 1689. McCabe feels it is better to have no bill than to have this one. Any amendments must now come from the floor. The Administration has indicated it wants the House bill passed without change. McCabe thinks nothing can be done except perhaps to talk with those close to the Administration. Brown believes $18,000 would be considered satisfactory.

Fleming thinks a resolution could be passed and sent to Senator Maybank.

Burgess suggests the Chair draw an appropriate resolution and send it to Secretary Snyder and Senator Maybank.

Potts thinks it would be desirable for Spencer to see Senator Flanders.

Odlin. Each Council member might write the senators from his state, if time permits.

E. E Brown asks Burgess to prepare a resolution suggesting that the salaries be raised to $18,000 and preferably to $20,000.

****

There was a discussion on the questionnaire which the Joint Committee on the Economic Report had sent to a number of bankers. It developed that not all members of the Council had received the questionnaire. It was the decision of the Council that this was not a matter appropriate for consideration by the Council.

The meeting adjourned at 6:37 P.M.

THE COUNCIL CONVENED AT 10:00 A.M. ON SEPTEMBER 19, 1949, IN ROOM 932 OF THE MAYFLOWER HOTEL, WASHINGTON, D. C. ALL MEMBERS OF THE COUNCIL WERE PRESENT EXCEPT MR. W. L. HEMINGWAY.

The Council prepared and approved the attached Confidential Memorandum to be sent to the Board of Governors relative to the agenda for the joint meeting of the Council and the Board on September 20, 1949. The Memorandum was delivered to the Secretary of the Board of Governors at 1:00 P.M. on September 19, 1949. It will be noted that each item of the agenda is listed with the comments of the Council on the item.

The meeting adjourned at 12:40 P.M.

CONFIDENTIAL

MEMORANDUM TO THE BOARD OF GOVERNORS
FROM THE
FEDERAL ADVISORY COUNCIL
RELATIVE TO THE AGENDA FOR THE JOINT MEETING
ON SEPTEMBER 20, 1949

1. In view of changed economic conditions and the present level of the Government securities market, what should be the policy of the Federal Reserve System with respect to the rediscount rate?

The Council believes that under current conditions it is desirable to retain the present rediscount rate. Any reduction in the rate now would only tend to ease money rates at a time when rates are historically very low. With deficit financing, and with business showing some improvement, it is not desirable to lend encouragement to a possible inflationary trend. Normally the rediscount rate should be a penalty rate. The present rate is low for a period of relative prosperity. A reduction in the rediscount rate now would also tend to increase the prices of Government securities and would therefore make more difficult the Treasury and Open Market Committee responsibilities in connection with the Government security markets.

2. What are the views of the Council as to business trends during the remainder of 1949?

The business trend at present is moderately upward from its low of recent months, and it is probable that it will continue upward for the remainder of 1949. Developments which might threaten a continuance of this trend are strikes in such major industries as steel, coal and the railroads and effects of the British devaluation.

3. Does the Council have any comments to make on the credit policy actions taken by the Federal Reserve System since the last meeting of the Council?

The Council is in agreement with the June statement indicating a departure from the policy of maintaining a fixed pattern of rates. The Council also approves the reductions in reserve requirements that have been made. These actions have been an encouraging influence on business sentiment. Looking backward, the Council believes it would have been helpful if the Federal Reserve System had released securities to the market more promptly in late June and early July and if interest rates had not been permitted to fall so low. The Council also believes the whole bond market would be in sounder condition if the System had released and were currently releasing bonds more freely from its portfolio.

4. Does the Council wish to express any opinion at this time with respect to the future refunding program of the Treasury?

The Council believes that the Treasury's announcement that it proposes to issue notes to refund the bonds coming due in December is a step in the right direction. As the program develops, it should include refunding into both intermediate and longer-term issues. Too large a proportion of the Federal debt is now in short-term securities, especially when considered in connection with the amount of savings bonds outstanding and with the steadily shortening maturities of the present long-term issues.

5. What are the views of the Council with respect to the following legislative proposals:

a. A basic revision in the law relating to reserve requirements which would base requirements on types of deposits rather than location of the bank, and would be applicable to nonmember as well as member banks.

(a) The Council is unanimously of the opinion that neither the Board of Governors nor any Federal agency should have authority to fix the reserve requirements of nonmember banks.

As to the reserves of member banks, while the Council recognizes that there is some lack of logic in the present basis for determining reserves, the banking system has over the years grown up with this arrangement and has operated effectively under it. Before the Council expresses its opinion on a change to some other basis, the Council desires more opportunity to study specific proposals and their effects on individual banks and on the banking system.

b. The authority of the Federal Reserve Banks with respect to industrial loans.

(b) On March 11, 1947, the majority (with a minority dissenting) of the Council supported S. 408 with certain amendments but with the following qualification:

"The Council's support, with these amendments, of Bill 408 is given in the belief that some safety valve is desirable for emergency credit situations, and with the recommendation that the lending and guarantee powers of certain other government agencies, including the R. F. C., should be greatly curtailed, and in many instances should be terminated."

At the time of the above statement by the Council, Congress was considering a restriction of the lending and guarantee powers of the RFC to emergency situations. Subsequent legislation has continued the RFC with broad powers, and there is no present prospect of reducing these powers. The Council is opposed to two government agencies having lending or guarantee powers in the same field and therefore would not favor giving additional guaranteeing powers to the Federal Reserve Banks in the industrial field.

c. H.R. 5749, introduced in the House of Representatives by Chairman Spence on July 25, 1949, "To amend Section 9 of the Federal Reserve Act, as amended, and for other purposes." This bill, proposed by the Board, relates to capital requirements for membership and the establishment of branches by member banks.

(c) The Council favors H.R. 5749.

6. The Board would like to have the views of the members of the Council on the proposal contained in the enclosed letter dated August 10, 1949, addressed to Mr. Leonard, Director of the Board's Division of Bank Operations, by Mr. Joseph J. Lawler, Third Assistant Postmaster General, outlining a plan which the Post Office Department has under consideration with respect to issuance and collection of Postal money orders. There is also enclosed a copy of a memorandum prepared by Mr. Leonard under date of August 11, 1949, regarding a meeting of representatives of the Post Office Department with members of the Board's staff at which the proposal was discussed.

The Council favors the proposal relating to the issuance and collection of Postal money orders provided the Federal Reserve Banks are fully reimbursed for their total expense in handling these items including a reasonable amount for overhead.

7. Should the holding company bill not include an exemption for wholly-owned trust companies?

The Council believes that the holding company bill should be amended to exempt wholly-owned trust companies not doing a commercial banking business. Such an exemption would not interfere with the primary purpose of the bill.

8. The question of the attitude of the Federal Reserve Board toward H.R. 5512 which would give the Federal Land Banks the power to borrow from the Federal Reserve Banks for one year at the Federal Reserve discount rate.

In the judgment of the Council the provisions of H.R. 5512 would provide for an improper use of central banking facilities and are unsound. The adoption of such legislation would inevitably lead to pressure for similar privileges by other Government lending agencies. The Council would appreciate knowing the position of the Board on this bill.

9. The Board has sent to the members of the Council a confidential staff study relative to deposit insurance coverage and the rate and base of deposit insurance assessments. The Board would appreciate the current views of the Council concerning any changes that should be made in deposit insurance coverage and the rate and base of deposit insurance assessments.

On May 17, 1949, the Council made the following statement to the Board of Governors regarding the subject of deposit insurance:

"The Council is familiar with the discussions on this matter which the Federal Deposit Insurance Corporation has had with a committee of the American Bankers Association. Without being committed to any particular formula, the Council favors in general an approach to this subject on the basis of these discussions.

"Specifically, the Council believes any legislation should include the following points:

A. No increase should be made in the present insurance coverage of $5,000;

B. The maximum assessment in any one year should not exceed one-twelfth of one per cent;

C. Provision should be made for maintaining the integrity of the fund by establishing a statutory formula for an automatic scale of assessments, based on the previous years' losses and expenses, to range from no assessment, or an assessment of a nominal amount, under present conditions, to a maximum of one-twelfth of one per cent per annum.

"In any study for the purpose of determining the adequacy of Federal Deposit Insurance Corporation funds and the rate of assessments, the Council suggests the importance of considering not only the possible losses of the Federal Deposit Insurance Corporation but also the effect on bank earnings, capital and dividends of the steady drain of assessments. These assessments reduce the power of the individual bank to make its own provision for losses."

The Council appreciates the opportunity it has been given to examine the confidential staff study, which the Council regards as an important contribution to the consideration of this subject. The Council also appreciates the interest the Board is taking in these phases of Federal deposit insurance which are of such vital importance to all banks. In the light of discussions now taking place among various interested groups, the Council does not at this stage of these discussions wish to commit itself to specific proposals. In the meantime the Council will give the matter further study.

10. Discussion of H.R. 1689.

In connection with H.R. 1689, the Council has unanimously approved the resolution which follows for transmission to Senator Maybank as Chairman of the Senate Committee on Banking and Currency:

RESOLUTION

"The Federal Reserve System is this country's Central Bank. Its decisions are of grave importance for the Nation's well-being. They influence the trend of business and employment.

"The Board of Governors of the Reserve System is the top command of the System. It should be manned by the ablest and best qualified people in the country. When the System was set up, the salaries of the Board were placed at the same level as members of the Cabinet and that relationship has been continued until the present.

"H.R. 1689 would break this sound tradition by treating the Board simply as a minor regulatory agency. This would lower the prestige of the Board and make it much more difficult to persuade able men to be its members. It would impair its influence upon banks and the public and cripple it for its essential service to the Nation.

"We recommend that members of the Board be placed on a higher salary level, preferably $20,000."

* * * * * * *

On September 20, 1949, at 10:45 A.M., the Federal Advisory Council held a joint meeting with the Board of Governors of the Federal Reserve System in the Board Room of the Federal Reserve Building.

All members of the Council were present except Mr. Hemingway. The following members of the Board of Governors were present: Chairman McCabe; Governors Eccles, Szymczak, Draper, Vardaman and Clayton; also Mr. Carpenter, Secretary of the Board of Governors.

DISCUSSION OF H. R. 1689.

E. E. Brown suggests that with the permission of the Board, the Council would like to discuss first the last item on the agenda dealing with H. R. 1689. The members of the Council feel that from the long viewpoint, this item is perhaps the most important one on the agenda. The discussion was off the record.

IN VIEW OF CHANGED ECONOMIC CONDITIONS AND THE PRESENT LEVEL OF THE GOVERNMENT SECURITIES MARKET, WHAT SHOULD BE THE POLICY OF THE FEDERAL RESERVE SYSTEM WITH RESPECT TO THE REDISCOUNT RATE?

E. E. Brown reads Item 1 on the agenda, as given above, and the conclusions of the Council as submitted in its Confidential Memorandum to the Board, dated September 20, 1949. A copy of this Memorandum is a part of these notes. Brown adds that the Council feels the low point of business may have been reached in June and July. New orders in some lines are much higher. The anticipated budget deficit and possible further wage increases are inflationary. However, business turned upward before all lines of business had experienced the effects of the recession.

McCabe calls attention to the Council's comments on the dangers of strikes in such major industries as steel, coal and the railroads. Strikes in these industries would tend to depress business.

Congdon. The lowering of the rediscount rate would have little influence on such developments as strikes.

WHAT ARE THE VIEWS OF THE COUNCIL AS TO BUSINESS TRENDS DURING THE REMAINDER OF 1949?

E. E. Brown states that Items 1 and 2 on the agenda are closely related and it may be desirable to discuss them together. Brown reads the conclusions of the Council on Item 2, as expressed in the Confidential Memorandum to the Board, which is included in these minutes. The business trend looks moderately upward, except for the strike threats and the British situation. The prospects for 1950 are not as clear as they are for the balance of 1949.

McCabe then asks that the remainder of the discussion on Items 1 and 2 be off the record.

DOES THE COUNCIL HAVE ANY COMMENTS TO MAKE ON THE CREDIT POLICY ACTIONS TAKEN BY THE FEDERAL RESERVE SYSTEM SINCE THE LAST MEETING OF THE COUNCIL?

E. E. Brown reads the Item above and the comments of the Council as given in the Confidential Memorandum to the Board. Brown states that the last sentence in the Council's conclusions on this Item as given in the Confidential Memorandum to the Board refers especially to ineligible securities.

McCabe states that up to the present time, the Board has tried to let the long-term market operate freely. He asks whether the Council thinks the market is too free.

Burgess does not think the market is too free. He states that the market was hit with a sledge hammer in the June statement. The market is seldom told that bonds are a buy. A very heavy weight of influence was put on one side of the market.

E. E. Brown. Looking backward, the Council feels it would have been helpful if the System had released securities to the market more promptly in late June and early July. He compares the situation to that of a well known grain speculator in past years who bought 100 million bushels of wheat and then announced that he believed in free enterprise but would not sell any of his wheat.

Eccles thinks the Council is inconsistent in its conclusions on this Item. There were two pegs in the market - a short-term peg and a long-term peg. The Board thought the short-term rate should be free, but the Treasury would not agree. Now there is actually a short-term peg of one and one-eighth per cent. At present the intermediate and long-term market should be free, but if an inflationary situation develops again, the long-term market should be pegged. The Board went as far as the Treasury and the twelve Federal Reserve presidents would go in the June statement.

MCabe. It is difficult, with conflicting viewpoints, to get agreement on policy matters.

Burgess. The Council has gone a long way in its comments to indicate that the Board did a good job.

DOES THE COUNCIL WISH TO EXPRESS ANY OPINION AT THIS TIME WITH RESPECT TO THE FUTURE REFUNDING PROGRAM OF THE TREASURY?

E. E. Brown reads Item 4 as given above, and the conclusions of the Council as expressed in the Confidential Memorandum to the Board. Brown also suggests a statement might be made that the long-term bonds will not be pegged.

McCabe does not believe one-third of the bankers would agree with the idea of taking support away from the long-term bonds.

Eccles thinks it is wrong to load the public with long-term bonds and then pull the peg.

E. E. Brown believes the public should be told the peg is removed before long-term refunding is done.

Clayton asks whether the second sentence in the Council's conclusions on this point should not read "As the program develops and under more normal conditions".

McCabe. The Board is in general agreement with the Council's views on this Item of the agenda.

WHAT ARE THE VIEWS OF THE COUNCIL WITH RESPECT TO THE FOLLOWING LEGISLATIVE PROPOSALS:

a. A BASIC REVISION IN THE LAW RELATING TO RESERVE REQUIREMENTS WHICH WOULD BASE REQUIREMENTS ON TYPES OF DEPOSITS RATHER THAN LOCATION OF THE BANK, AND WOULD BE APPLICABLE TO NONMEMBER AS WELL AS MEMBER BANKS.

E. E. Brown reads Item 5 a. as given above, and the conclusions of the Council as expressed in the Confidential Memorandum to the Board. A copy of this Memorandum is a part of these notes. Brown states that before the Council expresses its opinion on a change to some other basis it would need more specific proposals than are to be found in either the Bopp proposal or in the speech that Mr. Szymczak made at the School of Banking at Madison.

McCabe states that he is confused by the many different reserve requirements over the United States. He asks who will take the lead if the correspondent banks do not take it in correcting the present inadequacies and inconsistencies in reserve requirements in various states.

Congdon asks whether the bankers associations might not take the lead. He thinks they might do something as a means of strengthening the banking systems in their respective states, and to meet what some of them may consider the threats of the Federal Reserve System.

Eccles says that if he were a reserve city banker, he would not wish to lose correspondent bank balances to the Federal Reserve System. The trouble is that the correspondent bankers wish to discharge part of the functions of a central bank. The maintenance of the dual banking system is not a part of this question.

Vardaman reports that he has finally come to the conclusion that there must be some uniformity of reserve requirements over the country. The A.B.A. is the logical group to further a "Uniform Reserve Act" similar to the Uniform Negotiable Instruments Act. Otherwise, Vardaman feels sure we shall eventually have Federal control.

J. T. Brown. Reserve requirements antedate the Federal Reserve System by a half century. In the past, banking authorities did not think of reserves as a means of managing the money market. They thought of reserves as a means of protecting banks. Now reserves are considered by some authorities as an instrument for managing the money market. If we could get away from the idea that reserves must be kept only with Federal Reserve banks, and if reserves could be counted when they are kept with correspondent banks, it would be possible to get the approval of bankers in his territory for the idea.

Szymczak replies that this is essentially the uniform reserve plan.

E. E. Brown states other questions are involved, such as the question of whether reserve requirements should be fixed by law, and whether the Board should have the right to vary the requirements.

Burgess. The A.B.A. has part of its staff working on a uniform banking code, and many changes have been effected in the direction of uniformity in banking laws in various states. The A.B.A. has been working along these lines for a long time. Burgess believes as much as ninety per cent of the deposits are now represented by Federal Reserve membership or are in states having good reserve laws.

WHAT ARE THE VIEWS OF THE COUNCIL WITH RESPECT TO THE FOLLOWING LEGISLATIVE PROPOSALS:

b. THE AUTHORITY OF THE FEDERAL RESERVE BANKS WITH RESPECT TO INDUSTRIAL LOANS.

E. E. Brown reads Item 5 b. as given above and the conclusions of the Council as expressed in the Confidential Memorandum to the Board which is included in these minutes.

McCabe states he does not think it is necessary to discuss this Item.

WHAT ARE THE VIEWS OF THE COUNCIL WITH RESPECT TO THE FOLLOWING LEGISLATIVE PROPOSALS:

c. H. R. 5749, INTRODUCED IN THE HOUSE OF REPRESENTATIVES BY CHAIRMAN SPENCE ON JULY 25, 1949, "TO AMEND SECTION 9 OF THE FEDERAL RESERVE ACT, AS AMENDED, AND FOR OTHER PURPOSES". THIS BILL, PROPOSED BY THE BOARD, RELATES TO CAPITAI REQUIREMENTS FOR MEMBERSHIP AND THE ESTABLISHMENT OF BRANCHES BY MEMBER BANKS.

E. E. Brown reads Item 5 c. as given above and the conclusions of the Council as expressed in the Confidential Memorandum to the Board which is included in these notes. There was no further comment by either members of the Board or the Council.

THE BOARD WOULD LIKE TO HAVE THE VIEWS OF THE MEMBERS OF THE COUNCIL ON THE PROPOSAL CONTAINED IN THE ENCLOSED LETTER DATED AUGUST 10, 1949, ADDRESSED TO MR. LEONARD, DIRECTOR OF THE BOARD'S DIVISION OF BANK OPERATIONS, BY MR. JOSEPH J. LAWLER, THIRD ASSISTANT POSTMASTER GENERAL, OUTLINING A PLAN WHICH THE POST OFFICE DEPARTMENT HAS UNDER CONSIDERATION WITH RESPECT TO ISSUANCE AND COLLECTION OF POSTAL MONEY ORDERS. THERE IS ALSO ENCLOSED A COPY OF A MEMORANDUM PREPARED BY MR. LEONARD UNDER DATE OF AUGUST 11, 1949, REGARDING A MEETING OF REPRESENTATIVES OF THE POST OFFICE DEPARTMENT WITH MEMBERS OF THE BOARD'S STAFF AT WHICH THE PROPOSAL WAS DISCUSSED.

E. E. Brown reads Item 6 as given above and the conclusions of the Council as expressed in the Confidential Memorandum to the Board which is included in these notes. Brown states that this proposal makes Postal money orders the equivalent of cashier's checks and it may take some income from small banks. The Council believes the expense of handling these items should be fully covered. The Council does not think the Federal Reserve banks should work for nothing.

Vardaman states that on this question he speaks as an individual member of the Board and not for the Board. This proposal will not affect the large city banks, but small town banks will suffer. There are over one and one-half million Postal money orders issued each day, or over 400 million a year. This represents a definite encroachment on the part of the government in the banking business.

E. E. Brown. If the Post Office Department is required to pay the complete costs of handling these items, the Department may be less enthusiastic about the plan suggested.

Vardaman. This proposal actually directs banking business into government channels.

SHOULD THE HOLDING COMPANY BILL NOT INCLUDE AN EXEMPTION FOR WHOLLY-OWNED TRUST COMPANIES?

E. E. Brown reads Item 7 as given above and the conclusions of the Council as expressed in the Confidential Memorandum to the Board which is included in these notes.

McCabe states it is difficult to work out this matter but he hopes something may be done.

Eccles. If we could get the National City Bank and the First National Bank to go to bat in working out something, we might make a concession.

Burgess replies that he has some suggested language ready, but would not present it at this joint meeting of the Board and the Council.

THE QUESTION OF THE ATTITUDE OF THE FEDERAL RESERVE BOARD TOWARD H. R. 5512 WHICH WOULD GIVE THE FEDERAL LAND BANKS THE POWER TO BORROW FROM THE FEDERAL RESERVE BANKS FOR ONE YEAR AT THE FEDERAL RESERVE DISCOUNT RATE.

E. E. Brown reads Item 8 as given above and the conclusions of the Council as expressed in the Confidential Memorandum to the Board which is included in these notes.

Clayton reports that the Board and the Council are in agreement on this matter. At the present time the Board would oppose this legislation. Legislation giving the Federal Land Banks power to borrow from Federal Reserve banks would result in other government agencies seeking the same privilege. The Board feels there is no need for this legislation. If the agricultural bloc presses for this legislation so that the legislation may pass, then the Board will work for a penalty rate. However, the Board would prefer the defeat of the legislation.

E. E. Brown thinks it is unwise to compromise on the legislation on the basis of a penalty rate. The legislation should be defeated.

THE BOARD HAS SENT TO THE MEMBERS OF THE COUNCIL A CONFIDENTIAL STAFF STUDY RELATIVE TO DEPOSIT INSURANCE COVERAGE AND THE RATE AND BASE OF DEPOSIT INSURANCE ASSESSMENTS. THE BOARD WOULD APPRECIATE THE CURRENT VIEWS OF THE COUNCIL CONCERNING ANY CHANGES THAT SHOULD BE MADE IN DEPOSIT INSURANCE COVERAGE AND THE RATE AND BASE OF DEPOSIT INSURANCE ASSESSMENTS.

E. E. Brown reads Item 9 as given above and the conclusions of the Council as expressed in the Confidential Memorandum to the Board which is included in these notes. Brown states the Council appreciates the Board's interest in this matter as it is of great importance to the banks. The staff report contains much valuable material. At the present time several interested groups are discussing this subject. Consequently, the Council does not wish at this stage of these discussions to commit itself to specific proposals. The Council stands on its former statement, as given to the Board on May 17, 1949, but is giving the whole matter further consideration.

Eccles believes the Council might have a committee meet with the Board to work on the matter, as the Chairman of the Board has been asked to make a report to the Joint Committee on the Economic Report by October 15. The Council could be very helpful by working with the Board and assisting the Chairman in the preparation of this report.

The meeting adjourned at 1:35 P.M.

****

The members of the Council and the Board agreed that the next meeting would be held on November 13, 14 and 15, 1949.

****

The Council convened at 2:30 P.M. in the Board Room of the Federal Reserve Building with all members of the Council present except Mr. Hemingway.

E. E. Brown asks what action the Council wishes to take in connection with the suggestion by the Board that the Council work with the Chairman of the Board on the report the Chairman has been asked to make to the Joint Committee on the Economic Report relative to Federal deposit insurance. Brown states that the Chairman of the Board must present his report by October 15, which probably means that any discussions relative to it will be held before October 1. In view of the short time available, it may be difficult to get all of the members even of the Executive Committee together for the necessary meetings. Brown suggests the appointment of Fleming as Chairman, with Burgess and Potts as members of a committee to work with the Chairman of the Board on this matter. On motion duly made and seconded, the members of the Council unanimously approved the appointment of the committee. Brown states that the views of the members of the Council are essentially the same on this subject, and the committee is fully aware of these views.

The meeting adjourned at 3:10 P.M.

****

On September 20, 1949, President Brown presented the following letter to Senator Burnet R. Maybank, together with the Resolution which follows; Mr. Brown was accompanied by Mr. Fleming and Mr. Burgess.

September 19, 1949

The Honorable Burnet R. Maybank
Chairman, Committee on Banking
and Currency
United States Senate
Washington 25, D. C.

My dear Senator Maybank:

On behalf of the Federal Advisory Council, I am pleased to enclose for your consideration a Resolution which the Council passed today with reference to HR-1689.

It is the opinion of the Council that to leave the Board of Governors in the salary classification in which they are placed in the House Bill may have far-reaching repercussions in the conduct of the Federal Reserve System in the future.

Respectfully yours,

E. E. Brown

President

Enclosure

RESOLUTION OF THE FEDERAL ADVISORY COUNCIL OF THE FEDERAL RESERVE SYSTEM WITH RESPECT TO H. R. 1689, SETTING NEW SALARY SCHEDULES FOR VARIOUS GOVERNMENT OFFICIALS

"The Federal Reserve System is this country's Central Bank. Its decisions are of grave importance for the Nation's well-being. They influence the trend of business and employment.

"The Board of Governors of the Reserve System is the top command of the System. It should be manned by the ablest and best qualified people in the country. When the System was set up, the salaries of the Board were placed at the same level as members of the Cabinet and that relationship has been continued until the present.

"H. R. 1689 would break this sound tradition by treating the Board simply as a minor regulatory agency. This would lower the prestige of the Board and make it much more difficult to persuade able men to be its members. It would impair its influence upon banks and the public and cripple it for its essential service to the Nation.

"We recommend that members of the Board be placed on a higher salary level, preferably $20,000."

****

September 19, 1949

REPORT OF SUB-COMMITTEE OF THE FEDERAL ADVISORY COUNCIL ON F.D.I.C. ASSESSMENTS

This Sub-committee of the Advisory Council was appointed with power at the meeting of the Council on September 20, 1949 to give further consideration to Federal Deposit Insurance assessments in the light of the study prepared by the Staff of the Federal Reserve Board. After individual consideration of the problem, the Committee has met in Washington on October 4 and 5, and the following are its suggestions to the Federal Reserve Board.

The Committee wishes first to express its appreciation of the breadth and thoroughness of the study prepared by the Board's Staff. This is the most complete assembling of data and consideration of the questions at issue that the Committee has seen. In general, the Committee finds itself in concurrence with the broad approach to the problems and the line of reasoning of the Staff report, with reservations at some points.

The greatest difficulty may lie not in the broad objectives to be sought, but in securing agreement on a program. The American Bankers Association has a committee which has been at work on the subject for six years and has been carrying on conversations with the Federal Deposit Insurance Corporation as to modifications in the law. A number of other government agencies are concerned in the matter. From various sides many different suggestions have been made. It is our belief that the Federal Deposit Insurance Corporation is the agency which should present to the Congress a specific program based on its experience and studies. While the Federal Reserve System is broadly concerned in the matter, this is not primarily a Federal Reserve problem, and the Council at its two preceding meetings has given the Committee guidance in not wishing to sponsor a specific detailed plan. The Committee, therefore, in this report will rather emphasize certain principles which should be followed.

1. Reduction of assessment. The Committee can speak for the Council in its emphatic agreement with the Staff report as to the desirability of a prompt and substantial reduction in F.D.I.C. assessments. The Staff report reviews convincingly the loss experience both under the F.D.I.C. and previously. The capital of the banks in the country is now thirteen billion dollars. The F.D.I.C. at the end of this year will have one billion two hundred million of reserve funds and borrowing capacity at the Treasury of an additional three billion dollars. These are substantial sums in relation to fifty billion dollars of "risk assets" held by banks, on most of which we believe the risk is slight.

The point which the Committee would emphasize more vigorourly than is done in the Staff report is the present need for larger bank earnings in order to accumulate bank capital more rapidly and to reopen the bank share market by giving the bank shareholder a fairer return. Bank shares are now selling at a heavy discount from their liquidating value, and most banks find it difficult to sell their shares in the market at fair prices to obtain new capital. Thus, from a long-range point of view of the strength of the American banking system and its capacity to finance expanding American business, the bank capital position needs to be improved over a period both by earnings and by the sale of securities in the market. A reduction in F.D.I.C. assessments will be a material aid towards this objective.

2. Nature of assessments. The Council has steadily taken the position that in any revision of F.D.I.C. assessments "provision should be made for maintaining the integrity of the fund" by the continuation of some assessment, and the characteristics of this assessment should be (a) that fluctuations in the amounts should be statutory, with variations set by the law rather

than by any board's current decision, (b) that the maximum assessment in any one year should not exceed 1/12 of 1%, and (c) that the annual assessment should be based on previous experience as to losses and expenses of the corporation, which together have recently been running under ten million dollars a year.

In the matter of the top assessment, the Staff report suggested 1/10 of 1% rather than the present 1/12. We believe that 1/12 is large enough, and it is accepted by the banking community and by the public as an appropriate maximum rate.

As to the length of past experience on which the changes in the assessment should be based, the Staff report makes the suggestion that a ten-year moving average is a sounder basis than a single previous year's experience. This avoids imposing a severe increase in the assessment at a time of depression. The Committee is impressed with the Staff proposal on this point, and believes this is one of the details on which the F.D.I.C. might be asked to make a definite recommendation. The question is partly one of the public reaction to reductions in the fund and the length of time that it would take to restore losses incurred. Our general feeling is that an average of a shorter period than ten years might be more acceptable from the public point of view.

3. Coverage. The Advisory Council at its May meeting stated its opposition to an increase in the coverage over $5,000. This Committee recognizes, however, the conclusion of the Staff that an increase in the coverage would not be inconsistent with or should not interfere with a substantial reduction in the assessment. We also recognize that there is a certain amount of agitation for an increase in the coverage, particularly

on the part of small banks. It is our belief, however, on the basis of surveys made by the American Bankers Association and other agencies, that this agitation is not substantial in scope, and we entertain doubt as to whether, in fact, smaller banks would be materially benefited in their deposits by an increase in the coverage. The matter should, however, be decided on broader public considerations. There does not appear to be from the public, as distinguished from the banks, any demand for an increase in coverage, and the present coverage does protect the small depositor, for whom it was primarily intended.

While we recognize that as it has been operated, deposit insurance has, in a great number of cases, protected entire banks through the purchase of assets, we are not convinced that situations may not arise in the future where the other method originally contemplated in the Act, of liquidating the bank and paying off from deposit insurance deposits of $5,000 and less, may not be a desirable method of procedure. If that proves to be the case, the limitation on the coverage will be conservative and desirable. We understand that the F.D.I.C. is making a survey of this problem, and suggest that final recommendations be deferred pending its completion.

It should be noted that the Federal Savings and Loan associations are now operating under an insurance program which also has a $5,000 limit, and that any change in the F.D.I.C. coverage may well be taken as a basis for a demand for an increase in the coverage in this other field, where the experience is still very limited and where a change now would involve substantial risks. Every extension of the principle of government guaranties needs to be examined with the utmost care before adoption.

4. Simplification of accounting basis for assessments. The Committee agrees completely with the Staff report as to the desirability of

simplifying the basis for assessment and bringing it into harmony with the definitions in the Call Reports of the Comptroller and the Federal Reserve. The present uncertainties are disturbing, and a considerable savings in expenses could be effected by the proposed procedure.

5. Relationship of size of fund to deposit total. The Committee has given consideration to the suggestion of the Staff report that the fund be related to total bank deposits. It is the Committee's feeling that this is an unnecessary complication of the program. Legislation on this subject should be as simple as possible. The various proposed plans now under consideration for the continuation of assessments make provision for a continued increase in the fund year by year, in addition to the coverage of expenses and losses. This increase in the fund is in the neighborhood of 3%, which is about the same rate of growth as in the country's business. It seems to us, therefore, that there is adequate provision for growth without introducing an additional formula. It there were a formula, we would question basing it on total deposits.

6. Treatment of new members. The Staff report raises the question whether new members of the F.D.I.C. system should pay larger assessments for a few years. It is our belief that this is a question which could well be left to the F.D.I.C. for its recommendation. New members would necessarily have small resources, and the contribution to the fund would be in negligible amounts.

Signed

W. Randolph Burgess

Frederic A. Potts

Robert V. Fleming, Chairman

October 5, 1949