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CONFIDENTIAL REPORT

OF

FINANCE COMMITTEE MEETING

HOUSING ADVISORY COUNCIL

Suppl. [1]

JANUARY 15, 1935

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U. S. FEDERAL HOUSING ADMINISTRATION

WASHINGTON, D. C.

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Housing Advisory Council - Finance Committee Meeting - 1/15/35
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The second meeting of the Finance Committee convened at 10:00 A. M., January 15, 1935, on the call of the Chairman, Mr. Robert V. Fleming. The purpose of the meeting is to decide the questions listed in the following agenda:

(References are to Transcript of December 17-18 Meeting)

A - Title I (a) Should the limit of $2,000. for insurable loans be raised or should there be no limit?

(b) Should scope of application be enlarged to include renovation and modernization of multi-family dwellings, commercial buildings and industrial plants?

(c) Should the expiration date of December 31, 1935, for this Title be extended?

(Ref.: Pages 43,47,51,52 and 53 of Transcript)

B - National Mortgage Associations:

(a) Should capital requirement of $5,000,000. be reduced; and if so, to what amount?

(b) Should they be allowed to issue obligations 15 times instead of 10 times their capital stock?

(c) Should the National Banking Act and the Federal Reserve Act be amended to permit member banks to invest in stock of National Mortgage Associations?

(Ref.: Pages 21,22,23,24,59,60,66,70,71 and 75 of Transcript)

(d) Is it desirable that a Mortgage Discount Bank be established?

(e) Is it desirable to make insured mortgages eligible for rediscount with the Federal Reserve Banks?

(Ref.: Pages 67, 68, 69, 106 and 107 of Transcript)

C - Insured Loans: (a) What measures, if any, should be adopted if the National Mortgage Association does not materialize, to import liquidity to funds impounded in mortgage loans?

(Ref.: Pages 66,67,68,69,71,73,74,80,81,82,83,106 and 107 of Transcript)

(b) Should the limitations on interest rates that may be charged by mortgagees (5% to 6%) be altered?

(Ref.: Pages 45 and 46 of Transcript)

D - Such additional questions as may be proposed by Mr. Moffett or Members of the Finance Committee.

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Those members present were:	Members of the Federal Housing Administration present were:
Mr. Robert V. Fleming, Chairman	Mr. James D. Dusenberry
Mr. F. S. Cannon	Mr. J. Howard Ardrey
Mr. R. R. Rogers	Mr. Stewart McDonald
Mr Charles A. Miller	Mr. Roger Whiteford
Mr. Wayne F. Palmer, Exec. Secy.	Mr. Ward M. Canaday
	Mr. Abner Ferguson
	Mr. D. A. Reinbrecht

The Chairman asked for consideration of the following question:

A (a) QUESTION: Should the limit of $2,000. for insurable loans be raised or should there be no limit?

It was the opinion of all members of the committee that to substantially increase the $2,000. limit would be to take this class of loans out of the class of character loans. It was stated that for single dwellings there was practically no demand for an increase in the limit. Consequently, any increase would merely be in the interest of multi-family dwellings and commercial enterprises, which groups have other means of securing money rather than under the provisions of Title I of this Act. It was further felt that, if these larger projects were able to meet the requirements of Title I, of an annual earning power of five times the loan, any loaning institution would be prepared to meet its requirements. Lastly, it was felt that there was no experience on which to base insurance rates for the type of loan proposed. It was thought that the hazard of loans running to larger amounts would be so much greater than the $2,000. character loans as to make this type of business highly undesirable.

VOTE: "Should the limit of $2,000. for insurable loans be raised or should there be no limit?" It was unanimously voted that the limit of $2,000. for insurable loans should not be increased.

A (b) QUESTION: Should the scope of application be enlarged to include renovation and modernization of multi-family dwellings, commercial buildings and industrial plants?

Mr. Rogers stated that all of the arguments on the previous question applied to this question, and without further discussion the Chairman called for the question.

VOTE: "Should the scope of application be enlarged to include renovation and modernization of multi-family dwellings, commercial buildings and industrial plants?" It was unanimously voted not to enlarge the scope of applications to include renovation and modernization of multi-family dwellings, commercial buildings and industrial plants.

A (c) QUESTION: Should the expiration date of December 31, 1935 for this Title be extended?

Mr. Reinbrecht stated that at the rate of increase in loans under Title I, it was obvious that, some time between August of this year and the end of the year, the funds available for Title I would be exhausted. It was therefore decided to increase the scope of this question to include a recommendation to the Administrator to increase the insurance fund available under Title I. Mr. Miller stated that the date of expiration of Title I should be extended because there are many people who are not attempting to secure loans now but who will at a later date, as they get more confidence. Mr. Fleming felt that the one year contemplated by the present law was too short a period in which to educate the banking institutions of the country in this type of loan and if extended to December 31, 1936, we would have a good yardstick to see how it is going to work out. By that time the banks will become keen for this type of business. Mr. Whiteford stated that to date the Federal Housing Administration had been called upon to pay only one loss on a loan of this type and that on a $220.00 project. Mr. Rogers expressed the opinion, which was concurred in by all present, that in any additional amount the Administration requested that due consideration should be given to a gradual tapering off in Title I. Therefore, it might be advisable to ask for an amount not in excess of $100,000,000.. Mr. Fleming felt that the Administrator should be advised of this thought but that the actual amount should be established by the staff.

VOTE: "Should the expiration date of December 31, 1935 for this Title be extended?" It was unanimously voted that the expiration date of Title I should be extended to December 31, 1936 and, if necessary, the Federal Housing Administration, after examination of the subject, should ask for such additional funds for insurance purposes as might be necessary to carry out the intention of this proposed amendment but in an amount not to exceed $200,000,000.

B (a) QUESTION: Should the requirement for National Mortgage Associations of $5,000,000. in paid-in capital be reduced, and if so, to what amount?

After an extended discussion, in which much doubt was expressed, particularly by Mr. Rogers, as to the feasibility of Title III, the thought of the Committee was summarized as follows: that there would be great danger in reducing the capital of National Mortgage Associations below $5,000,000. for two reasons; first, that with a lower capitalization there is grave doubt in the minds of the Committee as to National Mortgage Associations being able to carry their overhead because of the restricted volume of business; second, because it would inevitably cause increased risk to the purchasers of the debentures who would probably be of that class in the community upon

whom such risks should be most reluctantly placed.

VOTE: "Should the requirement of $5,000,000. in paid-in capital for National Mortgage Associations be reduced, and if so, to what amount?" The vote was unanimously "No".

B (b) QUESTION: Should National Mortgage Associations be allowed to issue obligations 15 times instead of 10 times their capital stock?

VOTE: After amending the question by the addition of the phrase "provided the $5,000,000. capital is maintained", it was unanimously voted "Yes".

B (c) QUESTION: Should the National Banking Act and the Federal Reserve Act be amended to permit member banks to invest in stock in National Mortgage Associations?

It was the general opinion of all present that any recommendations made to Congress for amendments to the National Banking Act should comply as closely as possible to the present practice of the Federal Reserve System. Mr. Miller stated that it was undoubtedly better to count on recognized financial institutions for developing a system of National Mortgage Associations rather than to look to individuals. He felt that there was more interest on the part of banking agencies, now burdened with mortgage portfolios, to work out their own salvation through this method. He stated that, even though there was no return on the money invested, the advantage to them would be great enough to warrant their investment in these Associations. Upon the request of Mr. Fleming, Mr. Palmer gave the information on the existing Federal Reserve Banks. The smallest paid-in capital is at Minneapolis, in the amount of $3,132,000.; Dallas, Texas, has $4,048,000.; Kansas City has $4,052,000.; St. Louis has $4,088,000.; and Atlanta has $4,369,000.. It was the opinion of those present that it would be undesirable to attempt to establish National Mortgage Associations in every Federal Reserve District. It would be better to have stronger Associations in the larger centers. Mr. Rogers stated that if history repeats itself, the banks will be sorry that they have ever mixed up in a business about which they know nothing. The banks know little about the mortgage business. If they studied history they would think twice before investing in National Mortgage Associations. Mr. Cannon felt that the strength of the National Mortgage Associations, organized under bank subscriptions, would be that the banking interests were themselves concerned in the management.

VOTE: "Should the National Banking Act and the Federal Reserve Act be amended to permit member banks to invest in stock in National Mortgage Associations?" Messrs. Fleming, Miller and Cannon voted "Yes", Mr. Rogers voted "No".

QUESTION: (not in the Agenda) To what amount should banks be

limited in subscribing to National Mortgage Associations?

Mr. Fleming stated that banks are now limited to subscription of 6% of their capital stock and surplus in Federal Reserve Bank stocks. Of this amount, 3% is immediately paid in. Mr. Miller stated that he believed it would be necessary for the banks to subscribe not only to capital but to surplus in the National Mortgage Associations in order that those Associations would not show a loss immediately upon the start of the operation.

VOTE: It was voted that the Committee recommend:

To amend Section 5136 of the revised statutes of the United States as amended.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That Section 5136 of the revised statutes of the United States, as amended, relating to the corporate powers of National Banking Associations to deal in investment securities be amended by adding at the end of paragraph 7 of said Section 5136, as amended the following:

Provided that nothing herein contained shall be taken to prevent the purchase by the association of shares of stock of National Mortgage Associations, authorized to be organized under the provisions of Section 301 of the National Housing Act approved June 27, 1934, and the association is hereby authorized to purchase and hold stock in such National Mortgage Associations to an amount not in excess of six per cent of its capital stock.

To amend Section 9 of the Federal Reserve Act as amended.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That Section 9 of the Federal Reserve Act dealing with the membership of state banks in the Federal Reserve System be the same is hereby amended by adding to the end of said Section 9 as amended, the following:

Provided that state member banks shall be and hereby are authorized to purchase and hold shares of stock in the National Mortgage Associations authorized to be organized under the provisions of Section 301 of the National Housing Act approved June 27, 1934 to an amount not in excess of six per cent of their capital stock.

Mr. Rogers did not vote because of his vote on the previous question. Messrs. Miller, Cannon and Fleming voted "Yes".

It was voted to recommend to the Administrator to consider whether or not it is advisable to limit the period that the above powers may be given to member banks. The vote on this resolution was unanimous.

B (d) QUESTION: Is it desirable that a Mortgage Discount Bank be established?

Mr. Rogers stated that this subject has been agitated for a great many years by the real estate interests of the country. If mortgage discount banks could be established by private capital there would be no objection to it. If it were sponsored by the Government, he feels that in the end this would mean tax exemption on this type of security as well as political control. He would be strongly opposed to it. Mr. Fleming thought that every effort should be made to develop Title III rather than to go into other unexplored fields such as Mortgage Discount Banks.

VOTE: "The time is not opportune for further consideration of Mortgage Discount Banks". Mr. Rogers did not vote. Messrs. Fleming, Miller and Cannon voted in the affirmative.

B (e) QUESTION: Is it desirable to make insured mortgages eligible for rediscount with the Federal Reserve Banks?

VOTE: The vote on this question was unanimously "No".

C (a) QUESTION: What measures, if any, should be adopted if the National Mortgage Association does not materialize, to import liquidity to funds impounded in mortgage loans?

VOTE: It was voted that this question should be carried over until the next meeting of the Finance Committee. Special studies would be submitted at that time. Professor Kemmerer of Princeton and Mr. Howard M. Jefferson will be consulted in regard to Mortgage Discount Banks in other countries.

C (b) Should the limitations on interest rates that may be charged by mortgagees (5% to 6%) be altered?

Mr. Ardrey, in much detail, explained to the Committee the basis of the present interest rates.

VOTE: It was unanimously voted by the Committee "that the rates established by the Administrator should be given a trial before there

should be any consideration of a change".

QUESTION: Should we recommend that there be some loosening up in the regulations to the end that an insured mortgage would remain insured if sold to an individual, provided the mortgagee who sells the mortgage agrees to continue to service it?

There was an extended discussion, with everyone agreeing as to the necessity for making insured loans more readily salable and transferable.

VOTE: It was voted that the staff, as well as the Finance Committee, study into this question, particularly in view of the questionable status at this time of Title III.

The question was raised as to whether or not it would be possible to insure the debentures of the National Mortgage Associations as well as mortgages. There was no decision on this question but it will be listed on later Agendas of the Finance Committee.

The meeting adjourned at 3:10 P. M.

Chairman, Finance Committee

Executive Secretary

Housing Advisory Council - Finance Committee Meeting - 1/15/35

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Mr. F. S. Cannon	Mr. J. Howard Ardrey
Mr. R. R. Rogers	Mr. Stewart McDonald
Mr. Charles A. Miller	Mr. Roger Whiteford
Mr. Wayne F. Palmer, Exec. Secy.	Mr. Ward M. Canaday
	Mr. Abner Ferguson
	Mr. D. A. Reinbrecht

The Chairman called the meeting to order.

MR. FLEMING: Gentlemen, the first question up for consideration of this committee is under Title I - Should the limit of $2,000. for insurable loans be raised or should there be no limit? The law now has the $2,000. limit.

MR. CANNON: At the rate we are going now, where would we land?

MR. REINBRECHT: We will hit the billion dollar mark at the end of the year if we continue at the present rate. The best estimate we have made is at present between $500,000,000. and $600,000,000. which would mean $100,000,000. of the reserve out of the $200,000,000. The question, as I understand it, was put up with the idea of raising the limit to $50,000., with the idea of bringing in apartment houses, stores, etc. I don't know how far you are going to go with regard to the intent of the Act.

MR. CANNON: I always thought that the Act covered residential repairs.

MR. MILLER: It seems to me it is pretty dangerous to make any considerable increase right now. In big cities you have personal risks of an entirely different class. I would like to see a lot of rehabilitation, but I am afraid your percentage of loss will increase. The banking institutions would have something to say about that. They would not make large loans simply because they would be insured to 20%. I don't think we would accomplish a great deal. In regard to apartment houses and factories that can stand rehabilitation, there are other means of getting the money rather than under the provisions of Title I. There are no applications for loans in New York except for the outside territory. I think the risk would be out of all proportion. The R.F.C. has started a new scheme by making industrial loans. We do not want to rehabilitate industrial plants with Housing money. I would like to see the insurance on insurable risks increased to cover multiple dwellings, but as far as uninsured loans go I think we would be stuck a lot.

MR. FLEMING: I thought there should be a little survey made to see whether there was a demand for that. My feeling is that when you get in the larger sums, particularly up to $50,000., the 20% insurance in volume does not mean anything. It does mean a good deal with the small volume, and has a tendency for greater liberality. But when you get up into the higher sum it is like industrial loans through the R.F.C. There will not be enough volume so that your guarantee will amount to much. Maybe bankers are too hardshelled. But when you are making a loan and you are taking 80% of it yourself, the 20% protection is not going to sway your judgment.

MR. MILLER: It seems to me, in volume, you can make character loans of $2,000. with a great deal of safety, but if you go to make large loans you get stuck.

MR. FLEMING: The rules of the Federal Housing Administration must be_____

MR. ROGERS: You cut out apartment houses?

MR. FLEMING: Yes, it is an individual proposition.

MR. MILLER: If an individual has an income of five times the loan, he won't need help.

MR. CANNON: I don't think we ought to change this.

MR. FLEMING: Unless you are going to change the whole intent of the law, I think you have to stay at $2,000.

MR. CANNON: Do you think a slight liberalization will create any movement for quick action?

MR. MILLER: I would rather not stir Congress up.

MR. REINBRECHT: The biggest part of the loans so far are under $1,000. Only about 1% of the total loans are between $1,900. and $2,000. The real demand is for the smaller loans. Since Regulation #11 has been worded where it says that not more than $2,000. can be expended on one piece of property without the approval of the Administrator, we have had a number of requests for loans for from $2,500. to $4,000. up to $5,000. In proportion, it is not a great deal, but there are a good many cases that would come above the $2,000., and yet would not be large enough to come under Title II, or under a mortgage proposition, where the income is sufficient according to the present regulations to meet the requirements. But whether it is advisable to go to Congress to get the change from $2,000. to $5,000., is a question in my mind as to whether it is worth the trouble.

MR. FLEMING: I think Title I is doing a good job.

MR. REINBRECHT: There is every indication that a tremendous drive will be going on this Spring.

MR. FLEMING: We have made quite a number of loans. The majority of the applicants have not had bank accounts of any substantial amount.

MR. REINBRECHT: We have written out to all people who have made

loans and our advices have been that credit extended is brand-new credit.

MR. FLEMING: There have been other credits extended, but not under this plan.

MR. REINBRECHT: A lot has been extended under Building and Loan. But the banks especially, and even the finance companies have reported that the biggest part of their increase in business would not have been available had it not been for the modernization credit line.

MR. FLEMING: Our delinquents have been practically nothing.

MR. REINBRECHT: We sent out a questionnaire for delinquents among the institutions making the largest number of loans, and the finance companies have reported more delinquencies than banks, but they do not call them delinquencies when they are only one day old.

MR. FLEMING: Mr. Whiteford, we have been discussing the first question. I think the sentiments expressed by Mr. Cannon, Mr. Miller and myself are that we do not believe it is desirable to change the $2,000. limit. Mr. Miller expressed the opinion that for the little additional amount you might be able to raise, there would not be enough loans involved to agitate Congress. How do you feel about it, Mr. Rogers?

MR. ROGERS: I would agree with that. My first intent was to raise it. As to apartments, it usually requires $2,000. to $5,000. repairs before we can rent them, but Mr. Miller's statement about the R.F.C. takes care of that situation. It does not fall within the limits of character loans and I think I would be willing to go along with the Committee.

MR. FLEMING: It is a legitimate proposition.

MR. REINBRECHT: Of course, if the banks want to, they can have loans insured up to $2,000., and then make loans for $5,000.

MR. FLEMING: Do I take it that it is the opinion of the Committee that we answer Question A - Title I (a) by saying that we do not believe that the limit of $2,000. be changed at the present time? Is that satisfactory?

VOTE: It was unanimously voted that the $2,000. limit should not be changed.

MR. FLEMING: Regarding Question A - Title I (b), Should scope of application be enlarged to include renovation and modernization of multi-family dwellings, commercial buildings and industrial plants? What is your opinion?

MR. ROGERS: That is practically answered by A-(a).

MR. FLEMING: I think so. In view of the fact that we do not believe that the limit should be raised, (a) answers (b). We will now take up A (c) - Should the expiration date of December 31, 1935 for Title I be extended?

MR. CANNON: The indications are that if our work this Spring picks up, we will absorb a whole lot of this in the Summer.

MR. REINBRECHT: On the basis of the curve on the chart, up to the end of December you are practically past the billion dollar figure. We will come close to hitting the billion by the end of the year. It all depends on the intensive drive by the building supply dealers and the manufacturers under insurable loans.

MR. WHITEFORD: If that is done, will you not have done the necessary renovizing?

MR. ROGERS: I think it is a question of whether private industry is ready to go along. And if so, there is no need to extend the date. I think discussion should be put off until the next meeting.

MR. FLEMING: I imagine the Administrator wants to get this information in order to present to Congress any amendments. Of course you have to get amendments in early.

MR. MILLER: I cannot see why the powers cannot be increased. If we have not the money, the Administrator is not going on and insure beyond the money available. It seems to me that on the recovery, which I think will advance, there will be more demand. There are many people who do not go after the loans now, but if they get more confidence they will become good risks. I think a year from now we will be coming into better prospects. It is a mere question of whether we can get the money for another year. The building industry is not going to be so busy that it will have to bother with small loans for a year. If it is done with very little risk, I would like to see it done for another year.

MR. WHITEFORD: The risk to the Government will become greater if you extend the time. If Mr. Fleming's bank has made $500,000. worth of loans, and it has insured 20% of that amount, and these loans have been paid off, you have built up a reserve to where the bank is protected later on. The insurance feature is going to cost far more if you allow the banks the benefit of the insurance reserve out of good loans already made.

MR. FLEMING: I would like to see it extended for another year. One year is a pretty short time for the banking institutions. Only 300 or 400 knew anything about this type of personal loan. It will be sometime before they have a yardstick, and if you give them another year to see how it works, I believe the banks will go ahead. If you stop it off the end of this year they would wait and see how it turns out.

MR. WHITEFORD: Why would they wait to insure if they can get it for nothing? We look on it as practically 100% insurance.

MR. FLEMING: I would like to see this thing worked out so that the banks can go ahead on their own. If you extend it to Dec. 31, 1936, we will have a pretty good yardstick to see how it is going to work out. I think by that time they will become keen enough for this business, so that they will know what are good risks, like the Morris Plan Bank.

MR. WHITEFORD: Of course they want to be as keen as possible, like

the Morris Plan Bank. The first loss of the Morris Plan Bank was on a loan of $120 made on a little house which was worth only $200 or thereabout. I understand the man who defaulted was on the relief roll of New Jersey.

MR. REINBRECHT: Excuse me, you are wrong. The man lost his job and then went on the relief.

MR. WHITEFORD: Mr. Nickson was giving me the story. I don't think that when the banks build up a reserve they are going to be so careful about these loans as they are now.

MR. FLEMING: I hate to think that.

MR. REINBRECHT: Most of the letters we get from the banks all over the country say that they will not lose if they can possibly help it.

MR. WHITEFORD: The story was concerning oil burner loans, and that the banks would not make the loans. But the truth was that they would not make them for more than three years. We are making them for five years.

MR. FLEMING: Gentlemen, what is your pleasure? Should we ask that this Title I be extended to Dec. 31, 1936, and in the event that the guarantee funds are used up, should there be an additional appropriation?

MR. CANADAY: I discussed that this morning with Mr. Moffett and he was of the opinion that we should not ask for an extension. He thought private capital would be able to take care of this by the end of the year. I felt this morning that we ought to have a longer period, but thought you would be interested in having his comments on it. Mr. Moffett ought to know what we think about it.

MR. DUSENBERRY: We would like to get the opinion of this Committee. We believe it will work out all right. I do not believe the loss is going to be great. I believe that many institutions will go on their own - become educated by that time, and that maybe by the close of 1935 in Title I, that you are going to have a test of the loans as to how they are going to work out. The tendency will be to stop and watch and see how the thing is going to work out.

MR. ROGERS: Mr. Chairman, is the extent of time also involved in further appropriation?

MR. FLEMING: It will be coupled with it.

MR. REINBRECHT: It will be used up by August; used up in the sense that if the billion dollars is used then it will be used up; but if you work out a reinsurance on the basis of the loans that have been paid off, which is a possibility even under the present Act, (I cannot give details on it) where an institution has built up a tremendous reserve, there is no reason why that cannot be worked out as a reinsurance with those particular institutions.

MR. FLEMING: Well, I think it will work out that way.

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MR. ROGERS: How would it do to discuss the extension of time coupled with appropriation of $100,000,000. instead of $200,000,000? Wouldn't that perhaps bridge over the gap between fear on the part of the banks, and still carry?

MR. FLEMING: I think that we could word the answer that it should be extended to December 31, 1936, and that such additional funds should be appropriated not to exceed $100,000,000. after examination of the reinsurance features that might be developed.

MR. CANNON: Take our Building and Loan Associations; they are just getting into this. They are handling long-term loans and short-term loans.

MR. WHITEFORD: Here is another angle to that. It was voted to insure 5-year and 10-year loans, so that is going to increase the amount a good deal. You go to a 10-year limit. Of course, we only insure the whole loan for 5 years. That is going to add to the bulk of the insurance a good deal.

MR. CANNON: On your repayment you would have ample coverage. I think that will work out very nicely; bring a lot more into the game.

MR. WHITEFORD: It will bring more insurance in.

MR. FLEMING: I would rather see us make a recommendation to extend Title I to December 31, 1936, and that the Housing Administration apply to Congress for such additional funds as are necessary or desirable to carry that into effect. I do not say $100,000,000. or even $50,000,000.

MR. REINBRECHT: Nobody knows what the figures are going to be; we don't know when it is going to be used up.

MR. ROGERS: If the Housing Administration is going into another $200,000,000., and then at the end another $200,000,000., it is going to keep on.

MR. FLEMING: It would be public psychology.

MR. REINBRECHT: According to the Gompers' curve, figured on a billion dollars at the end of the year, we have so far been keeping in line with the curve and know what this spring drive is going to be at the end of 1935, but I did also say it was anybody's guess because the drive might be so big that the billion dollars might be used up prior to the end of the year, even as early as December 1. There isn't anybody that can do it. It is a guess.

MR. ROGERS: Do you think it would set better with Congress?

MR. FLEMING: Don't think you can tell the scope of the drive.

MR. REINBRECHT: No one can.

MR. FLEMING: Mr. Rogers' point is that it will set better with

Congress.

MR. ROGERS: I think it would set better. I think there is going to be a lot developed out of this plan. No question about it.

MR. FLEMING: After you become oriented I think a lot of personal loans will develop.

MR. ROGERS: I think so, too.

MR. FLEMING: I don't think they will know how good the 3 or 5 year credit is in one year.

MR. ROGERS: The theory of guarantee is getting greater and greater. I would say on that theory that they should be willing to stop any funds on their tapering off. They could run on two or three years and still be taken care of out of this reserve that has been created.

MR. MILLER: In many States the building and loan associations are not permitted to loan except under the guarantee of this Act. Banks have been very slow to adopt this. It is coming along, and as far as I have been able to learn their experience has been uniform, but at the end of this year it will not amount to anything. I think that six banks, the last I heard, were actually engaged in making these loans. At the end of the year if we have 20 we will be doing well. Seeing the experience, the time might be extended.

MR. FLEMING: A great many institutions have been hesitant on account of State laws.

MR. CANNON: We will not have a clear way of procedure until the legislatures have completed their work late in the spring.

MR. FLEMING: How do you feel about Mr. Miller's suggestion?

MR. MILLER: I would rather prefer your suggestion that we let the Administration decide that question.

MR. CANNON: Your suggestion indicated that it would be an extension made.

MR. FLEMING: Do I take it that the Committee votes we make a definite recommendation that the expiration date of Title I be carried forward to December 31, 1936, and if necessary the Federal Housing Administration, after examination of the subject, ask for such additional funds for insurance purposes as might be necessary to carry it out, not to exceed $200,000,000? Without objection, that will be the decision of the Committee. For the benefit of those members of the staff that were late, Mr. Fleming briefly outlined the earlier votes of the Committee on Items A (a) and A (b). This reopened the discussion on these points but without a change in the action of the Committee.

MR. CANADAY: I had some discussion with Mr. Moffett about that, and I also had a memorandum from Mr. Deane referring to the advisability of banks permitting loans up to $2,000. on individual apartments in an apartment building where the building is made up of individual units, where it is cooperative or where it is not cooperative. That is one of the places we have a great deal of pressure, and there is some question about what we may have the right to do, under present jurisdiction treating it as a dwelling, but there is also the question which may have been discussed before I came in, -- the fact that in many instances, if we could lend to manufacturing institutions or to various types of organizations that have machinery or heavy goods or anything of that kind, we could enlarge this activity very considerably. Los Angeles has just projected a plan for one hundred million dollars worth of business this spring; another asks for the right to expand this type of loan to include larger loans on business property and various ranches, etc., and we felt after considering the need at some length it would be advisable to raise these limits substantially, and I just give you that as a reaction of the Administration.

MR. FLEMING: We feel that we are getting beyond the character loan if you do that.

MR. CANADAY: That raises a bright subject as to whether, if you go beyond the character loan, the business institution should be allowed to borrow on its credit, whether that should be included in this type of insured loan.

MR. FLEMING: I think it would be the feeling of the Members of the Committee, that with a larger amount up to $50,000. you are getting into a different breed of pup entirely. It is the question of the income of the individual and you have also the question involved as to the insurance feature. Take a whole lot of character loans of small amount. Your volume of insurance covers a good deal, but when you get into these larger loans you do not have as many of them, and it comes down to the question as to whether the loan is good or not. If not good, he does not care anything about the insurance feature at all. That has been demonstrated.

MR. CANADAY: Do you feel that there is a vacant spot in the present Act between what the present Act does and what private capital is willing to loan?

MR. FLEMING: I have not checked with all the institutions, but the observations that we have made here are that people who want larger credit than $2,000., are able to stand on their own. We have made quite a number of loans. The people that want the insured loans are mainly the people who haven't any banking relationships to make loans of that type.

MR. McDONALD: Mr. Moffett has the feeling that if the scope were enlarged so that manufacturers might get loans of larger sizes, they might modernize equipment or build additions. The fact that there was an insurance would act as a kick-off.

MR. WHITEFORD: You wouldn't raise the amount above $2,000.?

MR. McDONALD: No.

MR. WHITEFORD: Any business concern that is well conducted has set up a reserve for depreciation and obsolescence. It seems the object would be to induce them to use the money that they have set up, for modernization. They have kept their depreciation money and have not spent it. The little fellow, who does not have depreciation, if allowed to modernize or improve within the $2,000., might bring more by including a commercial property. Mr. Deane has asked a number of times with the idea of spending $2,000. per apartment unit on an apartment house, and I advised him that under the Act it was contemplated that there was no right to insure that kind of a loan. What will happen is this: Take an apartment house of 50 apartments, $2,000. per apartment, that is $100,000. That is more than the equity in many cases is worth. They have trusts on them that they can't even carry, and the banking institution that may lend that money, if it has a substantial reserve, will say it will not cost us anything; we can make this loan; we are protected in the long run; and they are bound to make a bad loan. That is not character loan. I feel that this, in the last analysis, is not the kind of business that the Government should be in anyhow, and $200,000,000. in my judgment is enough for the Government to advance by way of insurance. It has done a pretty good job, and we will have reached most of the desirable loans of that character. Why do you want to keep the Government in that kind of business? This is the only Santa Claus part of the Act. I am not in favor of Santa Claus.

MR. FLEMING: I do not think there will be many institutions that will make these loans anyway. It would not cost us anything. I do not think many of them will do that. Many of them are proud of their record.

MR. WHITEFORD: Without financial ability, banking institutions cannot make an apartment house loan like that and let $50,000. be spent for reinvestment.

MR. FLEMING: I do not think anyone would purposely go in to make $50,000. loans.

MR. MILLER: If you make $2,000. loans on apartments so-called, that would mean that you would make $20,000. loans on several apartments.

(Mr. Miller spoke so low that it was impossible to take down his remarks.)

MR. ROGERS: I concur in what Mr. Miller says. We spent some $5,000,000. last year. Of course there would be a tremendous waste in it if we had spent $12,000,000., and I agree with Mr. Miller.

MR. FLEMING: This brings us to National Mortgage Associations. The first question is B-(a) Should capital requirements of $5,000,000. be reduced; and if so, to what amount? Mr. Miller, what is your view?

MR. MILLER: I don't want to object to everything, but I am thinking about the debentures. Under this plan their safety, and the price at which debentures can be sold, and bought by widows and orphans, depends on whether the capital is sufficient to cover the items not covered by insurance; whether it can cover taxes; whether it will cover the interest; and I must say that I have seen people who would buy these debentures, if this is not successful, who will go thru seven different kinds of Hades because

everybody guessed wrong. I should hate to see them feel that they were deceived by the U. S. Government by buying a certificate representing government insurance and then find that by reason of lack of capital the thing went down to disaster, and while they got the principal back, they met with a loss of the interest. In the metropolitan areas I have tried to figure out how Mortgage Associations could operate with less than $5,000,000., being limited then to borrowing ten times its capital, so that if you had $1,000,000. you could borrow $10,000,000. The spread is so slight, as between the prices at which they can be sold, that I am at a loss as to how it can be operated unless you have a volume to help carry the overhead. These things will not sell themselves. They will be under large expense, at least at the beginning. The public does not run to the National Mortgage Association and buy certificates. It will have to be explained to them. This will run up the cost. I put down figures as to what I thought it would cost to run the National Mortgage Association, and assuming that they had enough capital to borrow $50,000,000., even then they might keep out of the red, but it will be close. You are going to have National Mortgage Associations go along for a little while and not make money. I am afraid the holders of the debentures will eventually meet with losses unless you provide ample capital. I am familiar with it. They say people will not put in $5,000,000. to start a new plan without knowing definitely what their commitments will amount to, what it is going to cost to operate, at what price debentures can be sold, etc.; therefore, they say that they will be willing to start with $1,000,000. which they are willing to risk, but we will limit our losses to that. They are risking not only their capital but the money of the confiding public who is going to be sold these debentures, so that they are practically guaranteed by the U. S. Government. The $5,000,000. they thought would help. The capital has met with tremendous opposition with relation to the debenture holders and the loss that they might have. Don't let's get the Government of the Federal Housing Administration into the unpopular position that the mortgage companies have got themselves into. If the Government did the same trick and they met with a loss, I think the Government would be promoted into the position of Public Enemy Number One.

MR. FLEMING: Mr. Ardrey, can you throw any light to us on what has occurred in regard to formation of Mortgage Associations; what objections, what comments, etc.?

MR. ARDREY: I have not found anybody really interested in the organization of National Mortgage Associations, except either building material people who recognize it is essential to get the thing going, and also a few mortgage companies who wanted to rehabilitate under this Act. Particularly, a large building and loan association on the Pacific Coast was willing to go into receivership, and insure mortgages as a means of liquidation. The objections I have met are, in the first place, that they do not want to get $5,000,000. capital together until they see a sufficient market. I think that Title II, guaranteeing up to July 1, 1937, instead of being a help is a harm, when they begin to figure what will happen after then. Of course it is pretty difficult to interest anybody in putting up $5,000,000. to organize National Mortgage Associations where the spread is so narrow. Take the sharp man, I think he can make money, but there is no particular inducement, if you can buy bank stock for 70

cents or 75 cents on the dollar. At 5% interest rate and 4% debentures, I think you can figure out there is profit, but they cannot make so much money that there is an inducement for them to come in. If you try to sell bonds against the maturities, the longer the bond the higher the rate. One objection they find is with the same experience of all other companies, they are so uncertain as to moratoria. These are the principal objections. We have had two or three groups proposing to organize National Mortgage Associations with a smaller amount of capital. My feeling is that the smaller the capital, the less public confidence. Relatively, they are just as strong. But the $5,000,000. sounds more to the public than $2,000,000. While it is a matter of expediency, my own feeling is that you cannot have them everywhere. I do not believe they are going to spring up in every one of the districts. In the three or four cities where you might promote them among financial institutions, you can get it as quickly with the $5,000,000. as you could with $2,000,000. I think a $2,000,000. Association in New York would be an absurdity. We have not had anybody show a willingness.

MR. McDONALD: When you get down to the question of whether the Banking Act should be amended, that practically answers the first and second questions.

MR. FLEMING: That simply opens up an avenue as to capital subscribed.

MR. McDONALD: I have had experience with small banks in Iowa and Missouri, and they feel that if they subscribe to the National Mortgage Associations, and it will be possible to organize one in keeping with the size of their territory, they would superivse it, and they thought they could organize such an Association in inland territory with a capital of around $2,000,000. That is why we divided the territory into Federal Reserve Districts. Some of these districts are pretty thin. They certainly will not be able to organize one of $5,000,000. in my opinion - they might be able to form one with $2,000,000. capital in the territory mentioned, also Colorado and down South.

MR. FLEMING: It is debatable as to whether they should be given that power, but they could not invest depositors' money.

MR. McDONALD: That is the thought, that they would use part of the capital, and be allowed to discount, without recourse, mortgages for the amount of stock that they own.

MR. FLEMING: Discount or sell?

MR. McDONALD: Discount without recourse. You take the Iowa and some of the Illinois banks, they have small paper on home loans. That is popular investment on the part of the Western people.

MR. WHITEFORD: Why could you not modify the suggestion to leave it at $5,000,000. in certain Reserve Districts, and $2,000,000. in others? I think New York would want $5,000,000.

MR. MILLER: Could they make any money? I don't think the expense of living, salaries, etc., are as high out West.

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MR. WHITEFORD: Rents are less, clerk hire less, expense of living less, out West.

MR. FLEMING: In endeavoring to get people to organize National Mortgage Associations, if member banks would organize a mutual association through which they could sell their mortgages, they would expect to make their primary money out of the mortgages themselves.

MR. MILLER: The insured loans would be turned over to the mortgage company under Title II. The service charge is where they have made the money. So if you had a $1,000,000. mortgage company, with $10,000,000. of loans, that would be $11,000,000. Put it all in mortgages. There would be a maximum spread of 1%. You have at least half of that allowed immediately for salary accounts. The thing would have to be run by a man who would not get more than $10,000. and I don't think you can get an intelligent enough man to operate the thing safely for that figure. However, somewhere between $1,000,000. and $5,000,000. you might hit it.

MR. WHITEFORD: Suppose you allowed them to raise the multiple from ten to fifteen times?

MR. MILLER: I am trying to look out for the debenture holders if I can. The great mistake which the mortgage companies made was the feeling that they never were going to have another catastrophe, and they were spread out with so thin a margin that when the catastrophe came, they were sunk. If we operate over a great many years, we will run into depressed real estate conditions all over the country, and we must watch to see that no one gets pinched. If you take care of your overhead by letting them make loans up to 15 times the smaller capital, you increase the debenture holders. The Senate said the debenture holders would suffer. I said, "Nonsense - this is limited - those people will be safe - but if you go and dilute it, you will have something that won't be safe."

MR. WHITEFORD: Of course that capital can be invested under the law in non-insurable mortgages, but they cannot issue debentures against them.

MR. MILLER: Of course they may lose.

MR. FLEMING: They must be first mortgages subject to the approval of the Administrator.

MR. CANNON: I think Mr. Miller has presented it quite clearly. As to reducing it below $5,000,000. I know what our operating costs are, and I can see the possibility of danger is very grave when you get your capital down too low. There is no inducement to let them work it. I am afraid of the possibility. I object to the reduction of the capital investment.

MR. ROGERS: I subscribe to everything that has been said before, and say that even the $5,000,000. cannot be successful. I am convinced that there is a risk, and I would oppose a reduction below $5,000,000. but I don't think they can be successful with even the $5,000,000. capital, and I doubt that you can get people to subscribe on the present basis. If the debentures are tax exempt - Yes; but without it, I don't think there is a possibility of the National Mortgage Associations, as set up in the Act, being successful.

MR. FLEMING: If that be the feeling of the Committee, then there is no use having the Government rebuild the structure.

MR. ROGERS: That is my opinion.

MR. FLEMING: It comes down then to what can be done to create a form of organization that will allow a sale of these mortgages in order that institutions will step in.

MR. ROGERS: There would have to be a wider spread.

MR. WHITEFORD: You don't think Title III will work at all?

MR. ROGERS: That's the way I feel.

MR. FLEMING: How do you feel, Mr. Ardrey?

MR. ARDREY: I won't go that far. From my correspondence, I find that a very large percentage of the banks, who have already applied to be approved as mortgagees, have done so with the expectation that Title III was going to function. We put restrictions on the size of the banks because we have talked Title III, and we expected it to function, and we feel that small banks should not insure mortgages until the National Mortgage Associations were formed. If we do not do this, we should say that there are no National Mortgage Associations in sight, and those banks that want to make the loans can do so, with the expectation of having to hold them. You have $147,000,000. capital in the Federal Home Loan Bank, organized originally for distressed building and loan associations. I don't know how they are going to be made to operate in normal times. The capital is there and there might be some means of revamping. My observation has been so far that the banks and other institutions who made loans in 1927,1928 and 1929, and had 50% loans, are interested in the insurance feature because they are willing to reduce the rate, and did, and have a new mortgage which takes it out from under the moratorium in the States. I think Title II will function measurably without Title III.

MR. MILLER: It won't function without building loans.

MR. ARDREY: You won't draw the public into the mortgage market through Title II.

MR. ROGERS: I rather think you would. You are offering 80% mortgages. If made, and you offer it to one of the present institutions, I think you would get some new business. The mortgage business has been done in the past by offering a way out.

MR. WHITEFORD: You cannot sell it to anybody except an approved mortgagee.

MR. FLEMING: Has not the way out been that mortgage paper was given to the public?

MR. ROGERS: I admit your operation would be more limited. I think we are discussing how it could be made to work. My idea is that it cannot be made to work under the present debenture idea. But new business and old business on the present plan of Title II would make it work.

MR. WHITEFORD: Would you permit approved mortgages to be sold to the banks? If the original mortgagee services the loan, takes it to the bank and the bank makes the loan, it is an approved mortgagee. I am a customer in the bank and I want to buy an insured mortgage - I buy it from the bank with the understanding that the bank serviced it. You would let the public buy the insured note instead of the debenture?

MR. ROGERS: It is a question of what the public will do. The insurance does not follow the mortgage beyond the elibigle mortgagee. If there were any way of having the insurance follow the mortgage, it seems to me you would then solve the problem.

MR. WHITEFORD: You would not advocate that, if you were going to make Title III function?

MR. ROGERS: No. I am thinking that Title III will not function.

MR. WHITEFORD: I don't see any reason why an approved mortgagee cannot be permitted to sell that mortgage under the regulations of the Administrator, provided the Administrator says, "You can sell it, but you have to service it." Then the insurance will follow the mortgage. That is only possible if you are not going to have Title III.

MR. FLEMING: That comes to the question of changing the law.

MR. WHITEFORD: You don't have to.

MR. FLEMING: As I understand the law, the insurance follows the mortgagee. You cannot have the individual as a mortgagee. If a trust fund, the Administrator cannot approve the servicing.

MR. ARDREY: We have dressed it up for the National Mortgage Associations, creating safety, etc.

MR. FLEMING: I believe you can create a market for insured mortgages. I would never be agreeable to have the individual become the agent for collection.

MR. ROGERS: Is it possible to have the mortgage serviced?

MR. ARDREY: Mr. Whiteford is of the opinion that the law can be interpreted to where the proceeding can be followed. The best advice we had was to the effect that this could not be done. Mr. Whiteford thinks it can.

MR. ROGERS: If it can, it seems to me you have solved the situation, except as to the man who cannot buy the whole piece, but wants to buy a part.

MR. FERGUSON: Would the general public be interested?

MR. ROGERS: We are talking about trustees. They want to have some place to put their money. Should the $5,000,000. limitation be reduced?

MR. FLEMING: I think there is a grave danger in doing this. We can say that the capital should not be reduced, at least for two reasons; first, that with a lower capitalization there is grave doubt in our minds as to National Mortgage Associations being able to carry their overhead because of the restricted volume of business; second, because it would inevitably cause increased risk to the purchasers of the debentures, who would probably be of that class in the community on whom such risk should be most reluctantly placed.

We will now consider B (b) - "Should they (National Mortgage Associations) be allowed to issue obligations 15 times instead of 10 times their capital stock?"

MR. ARDREY: I think if you have a $5,000,000. Mortgage Association, you need not worry about the 10 or 15 times.

MR. MILLER: Might it not be practical in getting one set up, if we could give the trust companies power to subscribe to stock? They are very much interested in getting the problem solved. While I do not think there is any hope of doing it within the next few weeks, I think we might evade the 15 times, and if with $5,000,000. capital we might not object to the 15 times. With this volume it would give a little better chance for the mortgage company to keep out of the red, and make somthing for the stockholders.

MR. FLEMING: There is a need of further earning power.

(The opinion of the Committee was then asked. All were agreeable.)

MR. ROGERS: I think it is a pretty thin margin.

MR. PALMER: At the Executive Committee meeting it was asked that I announce before each Committee that it is desired to maintain any minority opinion, so it is not necessary that we get a unanimous vote.

MR. FLEMING: In regard to B (b) then, we believe it would be desirable for National Mortgage Associations to be allowed to issue obligations 15 times instead of 10 times their capital stock, in that it would make more effective the earning power of the organization.

We now come to B (c) - "Should the National Banking Act and the Federal Reserve Act be amended to permit member banks to invest in stock of National Mortgage Associations?" How do you feel on that subject, Mr. Miller?

MR. MILLER: I think it should be limited to a certain percentage of the capital. I feel pretty strongly that the National Mortgage Association that we are discussing today -- in future. I will say something about that later on. I would like to say much, but I don't know to what extent. Many trust companies would have considered going in if they had the power.

MR. FLEMING: They are allowed to subscribe to six per cent of the Stock and surplus of the Federal Reserve bank that is one half.

MR. ARDREY: Required to subscribe. I imagine that somewhere between that peak and some other peak you get that figure. Take a large bank with $150,000,000. capital and surplus, that would be $10,000,000.--would be more than ample. Take in our community here, unless we take Richmond and Baltimore into the picture, 10% would not do the trick. I think it is too much but they do permit National Banks to invest 15% of their capital in safe deposit companies, but that is a wholly-owner company.

MR. FLEMING: That is a different matter. That is the peak. I am starting at the peak. If you had the same Federal Reserve Requirement that would be six per cent of the capital.

MR. CANNON: It follows the pattern of the Federal Reserve System, in a way?

MR. FLEMING: There is some psychology, politically, if you are going to recommend it from that standpoint.

MR. CANNON: That is the picture that runs in my mind. We are in the Chicago district now. All those districts are pretty well knit together.

MR. FLEMING: Is there any regulation with respect to the form of the management of these banks as far as the corporate structure is concerned?

MR. ARDREY: No; no regulation.

MR. FLEMING: In other words, there is no set up contemplated on the stockholders.

MR. ARDREY: We have had no idea in the world of drawing any restrictions around the free management and control of it. We have not drawn any regulations; nothing in sight. Whiteford is a little contrary. He has come only recently, and we have been devoting our time almost exclusively to getting out our mortgage forms.

MR. FLEMING: No provision so far as you know against serving on the boards of its official organizations?

MR. WHITEFORD: No; I don't see why there should be. We don't want to put any limitation on them.

MR. ARDREY: What we have said publicly was that the formation of these institutions would be almost right down the line with National Banks.

MR. FLEMING: They will have a Federal charter?

MR. ARDREY: Yes; take the form of a national banking association; rub out "banking" and put "mortgage" and you have the forms all there.

MR. WHITEFORD: We have the forms and charter for each. All that has been prepared; but we haven't written any regulations because we feel that the less regulations the better for the present, so far as personnel is concerned.

MR. ARDREY: My own suspicion has been from the beginning that if you had National Mortgage Associations, unless you had a stock identified with high class institutions and personnel on the board and personnel on the management and banking stability, you would never sell the debentures.

(4330) MR. FLEMING: As an illustration, a bank having $10,000,000. capital

and surplus find, would have $600,000.

MR. WHITEFORD: What was that?

MR. FLEMING: Figuring Federal Reserve six per cent.

MR. ARDREY: What is the capital of the smallest Federal Reserve Bank?

MR. FLEMING: I cannot answer that; I rather imagine that Atlanta is the smallest.

MR. McDONALD: No reason why we would have to stick to our regional districts regarding the organization, such as National Mortgage Associations, for instance.

MR. ARDREY: The law authorizes National Mortgage Associations to do business anywhere, any State.

MR. WHITEFORD: It is not likely to get a bank in New York to subscribe to a Mortgage Association in an area somewhere else.

MR. McDONALD: But on the contrary you could get the Richmond bank to subscribe to New York mortgages.

MR. MILLER: If you have the adequate capitalization for it a year or so, you will pretty well show the money-making capacity of the institution, and then instead of going around drumming up capital for the bank you will find the very people wanting to put in money. The mortgage companies start in a small way until they could make money; and then as they showed that they could make money, they grew. I cannot believe with my knowledge of the mortgage market of the country that even with the competition occurring among them, they have ceased to show any intelligence whatever in the time loans they have made and the risks they took. This is a feature which takes it out of debentures, it seems, to a great extent. We reached 80% with one bank, with a total mortgage loss of less than 1/10 of one per cent. I do believe the important thing is to get one of these associations started if we can, and see what it will do. If I guess right, I am reasonably sure that it can become profitable to the stockholder.

MR. FLEMING: As I understand, any mortgage that is not insured can be bought with the approval of the Administrator.

MR. McDONALD: That is only as far as the capital funds go.

MR. MILLER: I don't like it; it is in the Act.

MR. FLEMING: I think there is your one danger.

MR. McDONALD: They cannot issue debentures.

MR. ARDREY: There is a point in that. I don't know whether it was discussed in the meetings, but there is quite a business the National Mortgage Associations can do, in buying round amounts of mortgages here and there that are insurable but not insured--that are eligible for insurance--and they can buy them and revamp them and insure them and issue debentures against them.

MR. MILLER: They can buy only insured loans.

MR. FLEMING: Amortized mortgages.

MR. McDONALD: The idea was that when the people subscribed to five million, they could immediately invest it and earn an income.

MR. ARDREY: Did I hear some one say that the National Mortgage Association could not insure a mortgage?

MR. MILLER: They can buy an insured mortgage, but as I see the law they cannot become an approved mortgagee.

MR. ARDREY: We have approved them as a mortgagee.

MR. WHITEFORD: They are not approved in the Act.

MR. ARDREY: I think the distinction there is, and the Council can put us right on it, that they can purchase and sell mortgages. The restriction was to keep these National Mortgage Associations from going out and competing with Building and Loan Associations but it says: (quoting from the Act) they may "purchase and sell first mortgages and such other first liens as are commonly given to secure advances on real estate held in fee". It was with this concept we had that these institutions would buy mortgages which are eligible for insurance upon revamping or rewriting and, with the cooperation of the borrower, they would insure these mortgages which they might purchase.

MR. MILLER: With that construction it is all to the good.

MR. FLEMING: The smallest reserve bank is Minneapolis, $3,132,00. paid in capital and surplus. That answers the question raised a little while ago.

MR. ARDREY: They have to have four million subscribed.

MR. McDONALD: Would you make this five million subscribed?

MR. ARDREY: The law says five million in cash.

MR. REINBRECHT: The law requires it paid in.

MR. McDONALD: We are thinking of changing the law.

MR. FLEMING: We voted on B (b). That still brings us back to the question "Is it desirable for national banks and Federal Reserve members to be allowed to invest in stock of the corporation, and if so what percentage of the capital?" Suppose we put the first question to see if it is desirable that they subscribe.

MR. ROGERS: It is a question for the banks themselves to settle. I am not a banker, and if I were I think I would think a little bit about the history of National banks had I been asked to subscribe to Federal Land Bank stock. The banks would be in an awkward position if they subscribe to the Stock. In spite of the fact that we have had as many foreclosures on amortized loans as on straight payment loans, my own belief is the banks would find themselves in an awkward position by reason of the fact that they have backed mortgage institutions. If history repeats itself the banks will be very

sorry that they have ever mixed up in a business they didn' know much about. The banks know little about the mortgage business. I think if they studied history they would think twice before investing in National Mortgage Associations. On this particular subject I vote "No." I shall go along with the Committee if it wants to. As a committee member I will save it against itself.

MR. CANNON: I think Mr. Rogers has stated a matter of policy there. I think this is the only way we can get the machinery started and I think it is possible to work it out. It can be done with probably better supervision through that sort of an organization plan by permitting the banks and trust companies, etc., to subscribe to the stock rather than what might otherwise be accomplished if left to others with less definite motives to handle the situation. From that point of view I am agreeable with the plan, that is, that it would be desirable for national banks to have that privilege or members of Federal Reserve banks to have the right to subscribe to this association. Personally I would feel much safer if they had management interest.

MR. MILLER: It seems to me one of the great troubles that we had before the bank holiday that is not cured as yet was the freezing up of the assets of the country banks. This does not apply to the big banks or to the large cities, unless it is in Detroit. With freezing up in mortgage loans and while they have been recapitalized through RFC, they are still going on and have still got this back-log of tremendous unliquid loans which, with an ordinary real estate market, they would eventually be able to liquidate. I have just been over the portfolio of one institution to divide it up into three classes--all the loans that were now under 60%; all the loans that were between 60% and 80%, and all the loans that were over 80%. That was a portfolio of nineteen million, and there were between six and seven million dollars of loans that ranged between 60% and 30%. I put the 80% because of this law. Between six and seven million of these loans that ranged between 70% and 80%, on these there was not a single default of interest, or ranged up very much closer to the 80% average than the other. In other words, that bank will come out all right when normal conditions are restored in the mortgage market, and it is about the worst that I have seen in the mortgage business. It will not have a loss of any considerable amount. There was some reason for having a marginal loss. It seems to me that after all, we do hope that this whole Act will tend to bring back money into the mortgage market and the old channels be used again and new channels created. In order to do so we have to create some channel through which they can flow, and to do that is ultimately for the salvation of the banks themselves, outside of the big cities, to determine whether we can do that job successfully. It should be a rather minimum amount. For the sake of trying to do this big job in a big way it is probably advisable. I have my doubts as to whether banks should have mortgage loans--I know one large bank that has 60%, and it is not a savings bank; all of its deposits are in mortgage loans that can be liquidated today, and I saw a lot more in about that shape. Why let them stand aside and let somebody else do the job that is perfectly their job? That is the only argument I could make for it. Take the trust companies, they have been getting many mortgage loans in the big cities, but they have an enormous amount of mortgage loans. It is also true that they owe at least the effort to bring this thing out of chaos and set us on our feet again, and if I were running one of these trust companies with one hundred million or something like that in trust funds invested in guaranteed mortgages, I should feel it was my duty to risk a certain

percentage of my capital in an effort to bring this thing out, provided I had something to say about the management. I have no hesitation in voting in favor of permitting the use of it.

MR. FLEMING: Permissive power. I rather think that those subscribing would be only those of the the type of institutions that you mention. It is not a nontaxable proposition.

MR. MILLER: You wouldn't have it unless the thing turned out to be really profitable, and then you will find them small country institutions. They may go out to buy up. I would see it limited to five years, to be out in that time.

MR. FLEMING: That is a good thought.

MR. ROGERS: Mr. Miller's talk runs along the line of expediency. But after all is said, the Act runs a long time in the future.

MR. FLEMING: This 5-year period is agreeable to me.

MR. ROGERS: I agree with Mr. Miller as to the matter of expediency.

MR. FLEMING: We are not going to get individuals to start to put their money into these Mortgage Associations. There might be somebody like Mr. Ardrey spoke of, in the building trades or construction field, who might put some in. There is no question but what the great portfolios of banks should never have been frozen up with mortgage paper.

MR. ROGERS: What objection do you have to the building trades going into this?

MR. ARDREY: None in the world.

MR. ROGERS: The man who takes the greatest risk is the man who buys on a 20% shoestring, and the next one is the one who takes the mortgage. It does seem that the material man must get into this proposition where he was taking a risk in the sense of lending some of his money.

MR. WHITEFORD: How will it sell the debenture? It does not give character enough to the company. The first question they ask when they come down is, "will you arrange with the R.F.C. that they will lend a certain amount of money on the debentures"? Then, "Where will we sell these debentures"? This is the story you get. You cannot start this off with the RFC. This is a reclamation proposition anyhow.

MR. ROGERS: It seems that if the national concerns in the heavy industrial trades finance this thing, the big concerns, I know no reason why their paper would not go on the market on a comparable basis with General Motors. Automobile companies have found their paper acceptable.

MR. ARDREY: The answer is that the finance companies on automobiles are doing it on 12 or 18 months, whereas you have 20 years. They find a market principally in the banks as commercial paper--almost the same as commercial paper. With the General Motors Acceptance Corporation its debentures sell

among banks, with tremendous capital behind it, and sponsorship behind it, short maturity, and their experience has been good, but it is all short paper. It is not 20-year paper. you can sell a debenture.

MR. ROGERS: It is an argument against the formation of debenture associations.

MR. ARDREY: There is this difference. Mr. Whiteford had some friends down here, and we spent one whole morning talking with them about it. We did not say we wouldn't give them a charter to organize, but when talking about the rate the paper would bear, a basic rate of five per cent, they didn't see where they could function. They believed that debentures issued by a corporation of that kind would sell at a higher rate; they could not make a living out of it. I don't know at what they will sell the debentures.

MR. WHITEFORD: These debentures are not tax-free and long-term. A man was talking about it Saturday morning. He said, "We do not see how we can sell them". And he said that when you compare these securities with a lot of tax-exempt securities there are, we have to have a longer term. I talked to him about the short-term idea. He said that is so, and he spoke of moratorium laws right away. He said: "You have moratorium laws in 13 States. You sell these debentures to parallel these maturities. You cannot foreclose; you don't get the property; the Administrator cannot issue his debentures; you just cannot do it; we cannot recommend them; the people wouldn't buy them".

MR. ROGERS: He was correct. National Mortgage Associations would be faced with the fact that when there is a social feeling against foreclosures you cannot foreclose, irrespective of the moratorium.

MR. WHITEFORD: Banks would not touch them.

MR. MILLER: Go to the people who bought mortgage certificates before and to the people who would like the mortgages. It would be sold in some cases to the interior savings banks. There has never been a time in the history of the State where the safest banks could not get money they needed to keep up the percentage of mortgages. We had to depend on what we thought was the interest of the mortgage in getting a good loan. To get the money flowing back is absolutely essential to the recovery of the United States in my judgment. I am here to contribute what little I can in that direction, because it is the most important thing we have to do. They will lose their status as approved mortgages as soon as they begin to let it drift and taxes accumulate. As to your moratoria, in the first place some of the States have had those laws only as to mortgages written before the panic. In other States you are already asking State legislators to make changes.

MR. FLEMING: Automobile paper has been sold because there has been education about it, for example, Ford Motor Company.

MR. MILLER: These must be sold differently. You have to educate the public. You have features you never had before--guarantee, insurance fund, protection to the principal sum involved, moratorium.

MR. FLEMING: The question before us is whether this permissive power should be given - whether we would recommend this power be granted. Are you gentlemen in favor of granting that permissive power? (B-c)
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MR. MILLER: Yes.

MR. CANNON: Yes.

MR. ROGERS: No.

MR. FLEMING: I vote "YES".

The next question would be the amount that they would be limited to subscribe to. It seems to me you get a good figure on six per cent of capital and surplus.

MR. MILLER: I think it should be three per cent. I think six per cent is too high.

MR. FLEMING: As you get into smaller institutions that affects them more. That ten per cent loan may be all right in larger institutions, but not in the smaller institutions. Do you think three per cent will be a sufficient amount?

MR. MILLER: In New York it would take care of it.

MR. ARDREY: I don't think you are going to have Mortgage Associations in every Reserve District.

MR. FLEMING: You would have less resistance from bankers if it were small.

MR. MILLER: If the New York bank should show a handsome profit, the public will take care of it, and the bankers would not have to put their money in it.

MR. McDONALD: Just because you are allowing banks to subscribe to it, you would not prohibit fire insurance companies or individuals from subscribing, would you?

MR. FLEMING : No.

MR. ARDREY: The more you make it sound like a Federal Reserve Bank, the easier it would be.

MR. MILLER: Would you make it possible to allow this three per cent limit to have it cover capital and surplus? I don't think a fellow would like to have a mortgage company started and immediately go into the red. Make the three per cent cover the contribution of capital and surplus.

MR. ARDREY: The Comptroller recommends a paid-in surplus.

MR. FLEMING: Three per cent of capital and paid-in surplus would make it pretty small. I think it should be three per cent of capital and surplus.

MR. MILLER: If you limit it to three per cent of the capital, they cannot put in any of the surplus.

MR. WHITEFORD: The question under the law is, if $5,000,000. capital, the Administrator could require surplus.

MR. ARDREY: You cannot require it, but the Comptroller recommends paid-in surplus.

MR. WHITEFORD: I think the Act ought to give the Administrator that authority.

MR. ROGERS: If a man said he was ready, would you let him start the National Mortgage Association? I don't think you have to put it in the Act.

MR. FLEMING: In regard to the permissive power of the member banks to subscribe - if you said three per cent of the capital only, they would be tied to the capital.

MR. ROGERS: I think it should be capital and surplus.

MR. FLEMING: You can get it started better with a small percentage.

MR. MILLER: There is more chance of getting it through Congress with the small percentage.

MR. FLEMING: I don't think in the New York District you would have any trouble, or in our District, or the Boston District or Philadelphia District.

MR. ARDREY: The average surplus of many national banks is sixty per cent, so I would make it either six per cent of the capital or three per cent of the capital and surplus. This would be adequate in New York. I don't expect these things to spring up in all the Districts. I think we would be better off if we had six or eight National Mortgage Associations in the larger centers than if scattered around. There is nothing in the Act that makes the purchase of insured mortgages mandatory. A New York Association might insure a sound mortgage outside of New York, but because of the small number of mortgages in that particular community they would not want to go down to look after one mortgage. They will buy the mortgages in densely populated sections. They would pick the place. I think a New York Association with five million dollars, if run well, and if it increased its capital as the business grows, would function. We don't want to keep the capital limited.

MR. FLEMING: If you subscribe to the Federal Reserve stock, you subscribe according to capital. You cannot have two sets of stockholders, and I don't think you will get other people to come into the proposition if the banks buy preferred stock and the other people could buy both preferred and common. I think this would mess it up. What would be the recommendation about allowing the bank to subscribe from surplus?

MR. ARDREY: I don't think there is anything to prohibit that. I think a National Mortgage Association in New York, with five million dollars, would sell its stock at one hundred and twenty.

MR. FLEMING: Are you going to be restricted under the law? If you set the limit with a par of one hundred, and not to exceed a price of one hundred and twenty a share, a five million dollar proposition would give you a one million dollar surplus. If they said you must have a two million dollar surplus you would be blocked.

MR. ROGERS: If the amendment reads that these Federal Reserve Banks were authorized to buy capital stock of the National Mortgage Associations, that does not govern the price. They could pay one hundred and twenty a share. You are not saying that they would be authorized to buy it only at par. It might be they would want to come in later when the stock would be worth one hundred and fifty.

MR. ARDREY: What does a non-member state bank now have to do when it comes in?

MR. FLEMING: They have to subscribe to an amount of stock equal to six per cent of their capital and surplus, but they only pay in half of that. New stock is issued. In the Federal Reserve, in case of liquidation, the surplus goes to the Government. The stock is limited to six per cent dividend.

MR. ROGERS: With what sort of an amendment would you be satisfied?

MR. ARDREY: An amendment which merely says to amend Section 5136, providing that they may subscribe to stock of National Mortgage Associations up to, and not to exceed, six per cent of their capital, and leave the surplus out.

MR. FLEMING: You will be getting a little better than three per cent of capital and surplus.

MR. MILLER: I am thinking about the National Mortgage Association. If the first annual report shows a loss, everybody will be scared. Some sort of a reserve must be set up to take care of it.

MR. ARDREY: Would that not be in the by-laws of the National Mortgage Association?

MR. MILLER: Yes. You can subscribe to the stock at par, but you cannot subscribe to the surplus. I want to get away from the legal mind that says it cannot be done.

MR. WHITEFORD: If you say "subscribe" that is the meaning, but you should say "purchase and become the holder of".

MR. FLEMING: Taking Mr. Ardrey's suggestion, shall we recommend that we amend the National Banking Act, paragraph 5, Section 5136, Revised Statutes; also amend the Banking Act of 1933, member banks, Section 9, Federal Reserve Act - to provide that member banks be allowed to invest in, and purchase stock of, National Mortgage Associations to an amount not to exceed six per cent of their capital stock? I think this has a very much better chance of going through. How do you gentlemen vote?

MR. ROGERS: I am not voting on account of my previous vote.

MR. MILLER: Yes.

MR. CANNON: Yes.

MR. FLEMING: I vote Yes.

The question has also been discussed as to whether it is advisable to limit the period that this power may be given to member banks. It appears to the Committee that this is a question which the Federal Housing Administration, if the recommendation is adopted, would have to work out with Congress.

MR. ARDREY: If we are right, then the banks already in ought to have a right to continue to subscribe to this stock. A New York National Mortgage Association, with five million dollar capital, will have ten million dollar capital in two or three years.

MR. FLEMING: The only danger is if we get into a boom. I don't think the big (?) banks are going to be hurt on six per cent of the capital. I am afraid about the small banks. I think the banks have a job to do here to help save themselves.

MR. FERGUSON: Is not this idea broad enough to permit them to purchase new stock?

MR. FLEMING: Yes, but all we are doing is giving out the suggestion that it may seem desirable.

MR. ARDREY: As a practical matter you might limit it to July 1, 1937.

MR. WHITEFORD: That would have quite an influence.

MR. FLEMING: Six per cent capital would not change it much. Once they get going the other capital will come into it. This is a primer.
Gentlemen, it is 12:50, Shall we adjourn for lunch?

(It was the opinion of the Committee that sandwiches should be served at the table, as the Committee wanted to adjourn about 3:00 P.M. Lunch was then served.)

MR. FLEMING: Question B (d), 2 sections: We will take up the first section, "Is it desirable that a mortgage discount bank be established?"

MR. ROGERS: This subject has been agitated a great many years, and I think it grows largely out of the desire to create a Government-sponsored Mortgage Discount Bank. However, in National Mortgage Associations there obviously is room for the establishment of the National Discount Bank, and it will come in strong competition with it. On the economic side, I would say it would be disadvantageous to all concerned, would be subject to political control, and it would get into trouble in the end. And in the end, in order to make it work it would have to be given Government guarantees anyhow and tax exemptions. If the Mortgage Discount Bank is to be by private capital, there would be no objection to it. If Government sponsored, which means, in the end, tax exemption, my vote would be "No."

MR. CANNON: Mr. Rogers has summarized it, as I see it.

MR. MILLER: I have been thinking what could be done if the National Mortgage Associations could not be formed. I believe that private capitalization might then be the only solution. I would not want to definitely condemn it until I know that National Mortgage Associations will or will not work. If they won't work then we will have to go back and consider what can be done. There are two problems. One is the problem of the selling of the mortgage which can be taken care of by the Mortgage Associations and in a sort of revolving fund to insure and sell part of their present holdings and use the money for new construction, if necessary to bring the thing out, and be helpful, but there is also the question of liquidity. Now that, at times, has been very acute. Under the laws of New York State we are allowed to have 70% of our assets in savings banks in mortgage loans. If they lifted up to that it would reduce liquidity of the savings banks to about thirty per cent unless some way was found to take care of it. Temporarily at least that situation has been pretty well handled with the aid of the RFC, so that if they are where a liquidity problem arises, it could probably be taken care of entirely in that community. It did arise a year ago last January quite severely, and the liquidity corporation there made some twenty millions of loans--purchases of the prior interest in mortgages. That is one trouble of establishing a bank with private capital. If things go right, it will have nothing to do a great part of the time, and then have to be able to take up the load when the load is needed. The nearest approach with us is the savings and loan banks in New York State, which is not a liquidity proposition. When they get out of funds so that they cannot make any loans at all, they are allowed to borrow on their credit and deposit mortgages of good standing as collateral in the building and loan bank. That bank in turn from time to time as it needs money issues its bonds, which it secures primarily, in the first instance, by depositing mortgages as collateral and, in the second place, by the credit of the building and loan banks in order to get the money out of the fund. That is not liquidity, except for purchasing new loans. If there should be a demand, they could not borrow in the building and loan bank to meet that demand; they can only borrow for the purpose of making new loans. The new issue is at four per cent. The bank bringing out the issue told me it was well over-subscribed before it was announced and they have always been able to sell at five per cent, and during the panic had sold at five per cent and the bonds have never gone below par, so that in a very small way the thing worked out to a success. In liquidity functions if you have not the power, it is a question as to how far you can go. It would vastly aid safety of mortgage loans and tend to reduce mortgage interest, if there was a way out for the institutions who are loaded with mortgage loans.

MR. ROGERS: If that is the purpose of the bank, I think it would be very desirable. Most can be taken care of by private institutions. My understanding of the mortgage discount bank is the same as has been proposed for a number of years on the theory that a great deal of good has come to the real estate interests.

MR. FLEMING: It comes down to the central bank. Commercial banks would have to have power to issue paper.

MR. ROGERS: The reduction of interest rates would do more harm.

MR. FLEMING: It would fall by its own weight.

MR. ROGERS: It certainly would.

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MR. FLEMING: The thing to aim at then is to try to make Title III work. If it won't work, then what?

MR. ROGERS: I am inclined to think Title III will work, if you will carry the insurance clear back to the ultimate investor, and I think it can be done under the Act.

MR. FLEMING: I think there is something in that, too.

MR. MCDONALD: If anybody wants the money, there it is.

MR. MILLER: In my experience of forty years, real estate security is very well thought of. They want to know if it is going to be handled as a straight proposition.

MR. ARDREY: All the building and loan associations in the country are against this mortgage discount. You will get between two fires, between the mortgage companies, who want it, and the others.

MR. FLEMING: I would cast my vote on this to say that we feel that every effort should be made to develop Title III rather than to go into other unexplored fields, such as the mortgage discount bank.

MR. ROGERS: The time is not opportune to discuss mortgage discount banks in view of the fact that efforts should be directed toward finding a way of making Title III work.

MR. FLEMING: Do the ideas expressed meet your views?

All replied in the affirmative.

MR. MILLER: If Title III does not work I should like to see this body take up consideration of a better proposition. A man set up a mortgage bank in Colombia and Peru, and it is working satisfactorily.

MR. FLEMING: Could we get him to give us a memorandum?

MR. MILLER: I think so; he is a useful citizen. I hope we will not entirely close the door on that question.

MR. ROGERS: We simply say it is not opportune at the moment.

MR. FLEMING: I think what we should do is to make a note of it.

MR. ROGERS: I will write Professor Kemmerer of Princeton.

MR. FLEMING: In regard to B (d), "Is it desirable to make insured mortgages eligible for rediscount with the Federal Reserve Banks?", if Title III works there is no need of bringing this up at all, because then the mortgages will be sold to these banks.

MR. ROGERS: If you limit Federal Reserve banks to take for rediscount construction mortgages with a definite time set for completion -

MR. FLEMING: That is eligible now.

MR. ROGERS: I vote "No" on the second section.

MR. MILLER: I am opposed to anything that will freeze up the Federal Reserve System. I vote "No."

MR. FLEMING: We do not feel that it is desirable to make insured mortgages eligible for rediscount in Federal Reserve banks. I vote "No" on the second section. We will now take up C (a), "What measures, if any, should be adopted if the National Mortgage Association does not materialize, to import liquidity to funds impounded in mortgage loans?" Shouldn't we say on that, that this is a subject which the committee is exploring and will be glad to report on at a later meeting?

MR. ROGERS: I will write Professor Kemmerer; it will take two weeks before reporting.

MR. MILLER: I will write Mr. Howard M. Jefferson tomorrow morning.

(This name was submitted by Mr. Reinbrecht.)

MR. FLEMING: I do not think the committee would want to bring any recommendations without a solid meeting on that one question.

MR. MILLER: What we are hoping for is that the Mortgage Association can function if we get that legislation through.

MR. ROGERS: Wouldn't the answer to that be to emphasize as far as possible the further working of Title II in the hope that Title II will eventually be made to work. Going back to our discussion, it does seem to me that Title II could be made to work very much better if the insurance followed either the debenture or the mortgage, irrespective of the hands it got into. If the small saver did not have to depend on the solvency of the Mortgage Association to get his money back, but could rely on at least getting a Government debenture, he would invest his money.

MR. ARDREY: Mr. Whiteford is of the opinion that we might draw a regulation under Section 201(b) of the Act, which says:

> "The term 'mortgagee' includes the original lender under a mortgage, and his successors and assigns approved by the Administrator; and the term 'mortgagor' includes the original borrower under a mortgage and his successor and assigns". --

The original lender of the mortgage is approved by the Administrator. As a practical question it is impossible for the Administrator to approve successor mortgagees where the mortgage passes from hand to hand. Without attempting to lay down any controversial opinion about it, my opinion also is that the individual would not be interested in buying amortized monthly payment 20-year mortgages at all. But I think the thing we hear quoted around is that amortization means liquidity to institutional investors and dissipation of principal to individual investors. Mr. Callaway, who is a member of this Committee, is a lawyer and Vice President in charge of the Trust Department of the Guaranty Trust Company. He failed to come to the

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last meeting, but was down Friday afterward. I asked him if he would not assume responsibility for your Committee and for us to prepare such an amendment to our regulations that would set up a range whereby we could qualify mortgage companies, or trust companies rather, both in their corporate capacity and in their fiduciary capacity. I tried to get him on the 'phone yesterday. We have very definitely in mind in this office that we do not have National Mortgage Associations. If we do not have National Mortgage Associations, we can broaden the regulations. We have written these regulations here having in mind Titles II and III. Of course, if Title III does not function, the whole frame-work would be modified. Whiteford thinks that, as it is, we can set up something here and call it a service or something under this Title II. It doesn't read that way to me. Mr. Ferguson might know what Mr. Whiteford has in mind.

MR. FERGUSON: What I have thought about Section (b) is, that we would be safe if we would, by regulation, some way or other, say that we would approve any holder of the mortgage so long as the original mortgagee retained the obligation to service the loan. In other words, the original mortgagee could sell the mortgage to whomsoever he pleased, but he still retained the obligation to service it, to collect the payments, and to apply them.

MR. FLEMING: Suppose he says he doesn't want to do this?

MR. FERGUSON: Then he cannot sell it. Some people say they can service them for one-half of one per cent.

MR. ROGERS: No question about that. It would be a very helpful step. Companies have already said they can handle it.

MR. FLEMING: It might grow. In the hands of the individual himself, he is going to dissipate it.

MR. ROGERS: There is tremendous money that can be drawn out of hiding. Say an executor of an estate that is worth $50,000 wants to put the money somewhere. As to the individual himself, I am not impressed with the thought of dissipation.

MR. ARDREY: I think it is a pretty substantial loss of interest, however. It will take him ten months.

MR. ROGERS: The average individual is more impressed with safety than he is with the return of five per cent or six per cent, and I think if he was getting back five per cent or six per cent I am not afraid of the dissipation of it.

MR. MILLER: What worries me is that the banks would sell participations in those mortgages. They would have a $10,000. mortgage and sell $1,000. to one man, and another $1,000. to somebody else, and all the time the mortgage would be scattered among ten participants, and probably do it without any trust debenture; probably do it without more than an undivided interest in that mortgage. How would you go to work to foreclose your lien on the part that you sold for participation, as the bank has no interest in the mortgage except to service it? I think that would have to be worked out by regulations, or you would get the whole Federal Housing Administration in wrong

again in reaping some of the errors of the banks that sold for participation in the old days. I don't think it is impossible to work it out, but I am glad I am not on the Committee.

MR. ARDREY: We spent a lot of time, days and nights, to make this Act as flexible as we could, to give it all the spread, at the same time recognizing the safeguards. These mortgages have stamped on the back of them "Insured". We tried to throw around them all safeguards. We have had some criticisms. We want to consider whether or not we would amend the regulations in order to create trust powers. It is perfectly obvious that you could not let a bootlegger buy an insured mortgage and have the borrower pay all the taxes. Somewhere you have to have some responsible person. We considered whether or not we could not set up an intermediary, but we hesitated about going any further than the plain purport of the Act. We were approving these mortgagees with quite a responsibility as it was. We have set up a service intermediary. Suppose the only fellow who wanted to be approved as mortgagee wanted to service twenty-four millions--that is a pretty big responsibility.

MR. ROGERS: You are up against that contingency anyhow.

MR. ARDREY: Certainly, except under the terms of the deed of trust, through holders of the notes, there is an offset.

MR. MILLER: There would be an offset if the assignee misappropriated. It would only be if the thing ran along until complete.

MR. ROGERS: You take the risk in either event. The question you are discussing is whether or not the insurance feature could be carried further back, particularly the eligible mortgagee of service origin.

MR. FLEMING: I do not see any reason why we could not broaden it. It seems to me that is the key to the situation. It would broaden Title II.

MR. ARDREY: It seems to me that by not imposing on the purchaser of the debenture the risk of the solvency of the National Mortgage Association which gives him the benefit of the insurance, that you could drag this money out at a very cheap rate. There is no present provision in the Act for that. We have had more complaints on our low-cost housing program as well as very serious complaint from people who would operate as approved mortgagee because of the lapse of time between the issuance of the debenture and the foreclosure.

MR. FERGUSON: Do you know why that was changed in the Act? The Act as it was originally drawn provided that he should get his debentures upon foreclosure and transfer or title or in the discretion of the Administrator, upon the assignment of the mortgage.

MR. MILLER: It was changed in the House.

MR. ROGERS: Is there any possible way any debenture of the National Mortgage Association can have the benefit of the insurance?

MR. ARDREY: No present way.

MR. FLEMING: Going back to the question - What do you think the situation is? Should we recommend that there be some loosening up in the regulations to the end that an insured mortgage would remain insured if sold to an individual, provided the mortgagee who sells the mortgage agrees to continue to service it? How do you vote? All we can do is to suggest that we make the mortgage more liquid by making it more salable. Does that meet your views?

(The Committee agreed.)

MR. ARDREY: What is the feeling of the members of this Committee about the restriction we put in the regulations about who may be a mortgagee?

MR. FLEMING: We have not discussed that.

MR. ARDREY: It is part of the same thing, because so far we have not approved small banks as mortgagees, but we are considering doing so. Generally speaking, we have not approved any mortgage companies, largely because they were not under supervision, and because the trust relationship did not seem to us to be properly provided for.

MR. FLEMING: Gentlemen, we will take up the last question, C-Insured Loans, (b) "Should the limitations on interest rates that may be charged by mortgagees (5% to 6%) be altered?" My observation is that it is rather expensive on old mortgages, and not so expensive on new mortgages, when the cost of the house is taken into consideration. Unless someone wants an eighty per cent mortgage on a piece of property constructed prior to this Act, an insured mortgage at six per cent for twelve years is very much better.

MR. ROGERS: What is the purpose of this question?

MR. ARDREY: There are just as many people talking one way as the other.

MR. FLEMING: Suppose we ask Mr. Palmer to read Pages 45 and 46 of the Minutes of the Housing Advisory Council Meeting, December 17 and 18, 1934.

(Mr. Palmer then read Pages 45 and 46 from the Minutes.)

MR. PALMER: I will also read the following from a letter from Mr. Lewis H. Brown, which just came in this morning, pertaining to the same subject.

> "3-The President's ruling on the 5% interest rate threatens the success of the National Housing Act. What can be done to have this ruling changed?"

MR. ROGERS: I think he must be thinking of changing it downward.

MR. MILLER: They sent Mr. Moffett a letter last night. Mr. Brown's idea was that the President handicapped the Federal Housing Administration by saying he wanted a uniform five per cent interest rate, and Mr. Brown's thought was it should be left as it was in the Act, with discretionary powers in the Administrator to increase it to get the best results.

MR. FLEMING: I think Mr. Brown is correct. I don't think it was wise to pin it to a five per cent proposition.

MR. ROGERS: I don't see that you could change these rates very much. In the case of five per cent it comes to seven per cent. You cannot put the rates up. From an economic standpoint you must put them down.

MR. MILLER: I am not sure you cannot put them up where people are accustomed to paying higher rates. In some parts of the country the people are paying eight and ten per cent. We want to induce money back into the mortgage market. There is no other business into which you can induce money by putting the rate for money below what you have had it before. In New York six per cent has been the prevailing rate for years. If you bring it from six per cent down to five per cent, no matter what the demand is for the loan, it handicaps your style. I think it will slow it up in certain parts of the country.

MR. FLEMING: Take a new mortgage - the purchaser gets a distinct advantage and saving. He knows the contract runs for twenty years, and if he keeps the reserve up that is all he has to worry about. I think he is getting protection that way by lower cost, and I think it is pretty cheap financing.

MR. ROGERS: This changes the situation - if he sells the house as soon as he builds it. When we talk about selling a piece of property ----

MR. FLEMING: Sometimes they want to step right into this thing. So, to those people you will have one mortgage on the property, and it is a tremendous argument.

MR. ROGERS: I don't think you could raise the rate.

MR. FLEMING: No. But when it comes to an old piece of property, unless that fellow wants to roll the first and second trust into one, it is far better for him to get a mortgage from an insurance company. There is no objection this, so far as the Federal Housing Administration is concerned, because you only have two billion dollars.

MR. ARDREY: The Act provides for two billion dollars, but the President may increase it. We compared our rates with the insurance premium, and it compares favorably. The lowest rate is five per cent plus the service charge. The insurance premium figured on flat five per cent all the way through amounts to 5.88%. The interest figured on an amortized basis is 1.76%, 5% and 1% service charge figures 7.76%. The interest rate and service charge is only six per cent actual cost. We have had criticisms from both directions from the fact that we had the service charge and the flat rate was 5%. A great many friends of this Act in Congress have been critical about the rate of 5%. The President did not take exception to Mr. Moffett and permitted it to stand. This Act was passed in the atmosphere of the Home Owners' Loan Corporation legislation and operation, and the people who voted for it had in mind that the Federal Housing Administration would function here, and private capital would come along and take the place of the Home Owners' Loan Corporation, which was making loans at 5%, plus actual appraisal cost. Mr. Moffett took the report made by the President's Committee in 1931 and made a survey as to the rate on dwelling mortgage loans from commercial banks, savings

banks, trust companies, building and loan associations and life insurance companies. When we were ready to announce our rates, we sent a telegram to our offices and asked for the rates, and they did not change. The average rate thrown into a pot was 6.69%.

MR. FLEMING: Your average is considerably lower than that.

MR. ARDREY: Yes, taking the insurance rate out. That was the rate in the mortgage itself, and had nothing to do with service charges, etc. Congress expected that these loans would not be made through brokers or agents, but would be loans made directly from the portfolios of institutions in the country that held the thrift funds of the country, and roughly speaking, of course, these were commercial banks, savings banks, trust companies, building and loan associations and life insurance companies. Of the 21 billion dollars worth of loans, 3 to 4 billions were held by individuals (many of them bought outright through mortgage companies), 3½ billions by mutual savings banks, 2½ billions in commercial banks, 2 billions in insurance companies, 3 billions in trust companies, and 6½ billions in building and loan associations - total of 21½ billions. It was expected that these loans would be made direct. We were supposed to take the place of the Home Owners' Loan Corporation. When Mr. Moffett made up his first schedule of charges, he made a rate of 5% in the area by States where the minimum mortgage rates existed - Connecticut, New Jersey, the northeastern sections of the country. He had the 5½% rate in the zone where they were higher, and the 6% rate out in the Pacific Coast and in the Southwest. Having in mind the National Mortgage Associations, and servicing them at home, he figured you had one-quarter of one percent service charge and 3% commission. The President asked him to come up and talk about it, and the understanding was that the President wanted a 5½% rate on new construction where there was acquisition of property. Mr. Moffett did not quote a rate on refunding, but in his letter to the President he said that he would make a basic rate of 5%, but the rate would be somewhat higher on refunding operations. The President had no fault to find with the service charge and the initial commission, but he did not want it called that, and he said: "You find some other way to put it in so it does not sound like that". This was on November first, with the election on November sixth. We wrote it up that it would be one-half of one percent without commission, and as we figured it we found it was about 1% lower than the charge that the President had approved. The Act calls for initial service charges. What they meant I don't know, but it looks like they meant all of these charges. Section 203 (b) says, "To be eligible for insurance under this section a mortgage shall - (2) involve a principal obligation (including such initial service charges and appraisal and other fees as the Administrator shall approve) in an amount not to exceed $16,000 * * * *." Congress apparently, from what Mr. Watson tells me, wanted to take the cost of the mortgage and give the borrower the right to borrow that, as well as the principal of the loan.

MR. FLEMING: There is nothing in the Act prohibiting the lending agency charging what it wants to, is there?

MR. ARDREY: There is nothing, except the 5% interest provision. The Act says the Administrator must approve the charges - such charges as approved by the Administrator. We have not drawn up any schedule of charges for application all over the country because you cannot do it for the reason that in many places the mortgage companies and other lenders have agreements as to

fees, etc. We do not require that they have a title policy. We say it shall be a first lien. The reason we do not bother about it is because under the foreclosure provision it says the title shall be conveyed satisfactorily to the Administrator. We have even had appraisal fees criticized.

About Lewis Brown's memorandum - the rates are very low. Our thought was that before very long we might find political comment arising, and instead of the President giving the man in Utah the same advantage as the man in New York, he might be depriving the fellow in Utah, because no one would let him have the money. As a practical thing I do not believe people will lend money so cheaply in some areas as in others.

MR. FLEMING: We can answer C-(b) "Should the limitations on interest rates that may be charged by mortgagees (5% to 6%) be altered?" as follows - In reply to the inquiry we believe that the rates established by the Administrator should be given a trial before there should be any consideration of a change.

(This was agreed to by the Committee.)

MR. ARDREY: What is Mr. Miller's opinion as to how far we ought to go in trying to create a market for the insured mortgage itself, and how far we ought to go in approving, as a mortgagee, every member of the Federal Reserve System, every member of the Federal Home Loan Bank, etc., after application and examination of their statement?

MR. MILLER: When you first started, it was my own thought that many things would be delegated to the approved mortgagee that have not been delegated to the approved mortgagee because they would have an interest in the property. We did not think it was feasible for the Federal Housing Administration to set up such an organization as could appraise all over the United States. I thought they should be carefully selected. Now about all that is delegated to the mortgagee is the collection of the monthly payments, and watching the fire insurance, and this could be done by a bank with small capital, and each one of those would know enough, I presume, to foreclose. I cannot say how the banks are going to feel, but I think you should be allowed to let the property go to the member banks.

MR. ARDREY: I know it is perfectly legal in a great many States. In our Mortgagors' Application for Loan, these payments made in advance are set up as trust funds. In many States you can enforce that against the receiver of a bank.

MR. MILLER: I think probably you could, so far as the bank had ordinary trust powers. I doubt that you could enforce it if the bank had retaining trust powers, except as an offset against the mortgage.

MR. ARDREY: During the time so many banks were closing up, in March, 1933, a great many of these nationally operating concerns adopted a new system of collection of taxes, and they were collecting them by creating trust powers when they got the money. They were advised that they could do that.

MR. ROGERS: We did not do this. This would not work unless all banks had the trust capacity. Practically all of the loans we had were in that trust position and given the benefit of it.

MR. MILLER: I would like to get the advice of the Administration and of the Committee on this proposition. Savings bank clients in New York have a certain number of their mortgages that would probably run to at least 50% of their mortgage loans that now, under present conservative appraisals that we will make, will show that these loans, while in good standing, are still between 60% and 80% of the present appraisal of the property. They are therefore overloans at the present time and are illegal. I think there is a good deal that can be done with the cooperation of the examining authorities, and with cooperation of the Savings Banks Association. With the advisory powers they now have, if it were desirable and worth while, a good deal could be done to persuade savings banks to insure all the insurable loans that they have and make them legal loans. As soon as they are insured they become a legal loan up to 80%. Would the Administration welcome endeavors in that direction, or is the Administration interested primarily only in new loans at this time and would not welcome any particular concerted action to bring about that sort of thing? I talked with the Department about the banking problem, and I would expect to get cooperation there if it is desirable to have the thing done. However, if the Administration would prefer to wait, I don't want to butt in and create a campaign that the Housing Administration would not approve of.

MR. ARDREY: I can answer that without any hesitation for myself and Mr. Moffett. We have not put any emphasis ourselves on any one of the groups of loans that we have under our schedule. We believe that you do not get anywhere with new loans until you get in better condition the portfolios under the old. You know the New York law better than I do. It prohibits the making of a loan of over 60%, but does not penalize anybody for making one. Therefore, the savings banks in New York are smart enough to be quite willing to have an open loan running on demand, rather than rewrite it, because that is making a loan. We have made our lowest rate (a rate where a mortgage company has foreclosed on a piece of property and is selling it to a buyer who is a borrower and taken back the mortgage which he wants to insure) 5% with no service charge. Even though it is old property, it is classified and the mortgage hazard there pays 20% in cash, so then the bank welcomed the premium of one half of 1%, partly as a sales talk and partly as something else. The lowest rate we make is in cleaning up distressed properties; the next lowest rate we make is on new construction, 5%, ½% service charge, and ½% insurance premium. Where Jones sells to Smith and Smith wants to borrow the money and goes to a bank, and that bank makes a loan on that class we allow ½% service charge. Both parties are putting fresh money into the mortgage market. We make five reconditioning loans to one new one. In Ohio someone got crossed up with these loans, and they are damning us for giving preference to reconditioning loans. This is inconsistent. Mr. Van S - has set up six rehabilitation companies, taking capital out of the trust he is administering and putting in new capital without any liabilities. These institutions do not technically qualify, but, with certain agreements and certain understandings we had, four of them have been approved as mortgagees. Their thought was that they would want to insure all the mortgages that they had, with a view to selling them to approved mortgagees, and particularly hoping that they would have National Mortgage Associations. We do want to have this thing used as widely as it will be in rehabilitation of the mortgage structure market. A good deal can be accomplished in the next six months or a year.

MR. MILLER: A great deal can be done along that line.

MR. FLEMING: Have we overlooked anything?

MR. PALMER: No.

MR. FLEMING: Mr. Ardrey, do you feel at liberty to tell us in regard to Mr. Brown's memorandum?

MR. ARDREY: From my telephone conversation with him yesterday in New York, he does not expect this thing to be so quick in operation as a lot of people expect it to be. As much as he is in the durable goods market, he is only interested, apparently, in having an even flow of mortgage funds into the market, consumption of materials, and employment of labor. He thinks that the tendency down here is toward imposing, in these rules and regulations and amendments to the Act, conditions on lenders that are going to defeat their own purpose. He believed that this thing should be liberalized enough with rates, etc., so that lenders would lend from business reasons alone rather than to do it pro bono publico. That is what we have in mind. You can get a lot of people coming along and applying to the mortgagees who never make a loan, just to cooperate. When business begins to pick up, these rates are not going to do any harm.

MR. MILLER: You cannot cut them any further.

MR. ARDREY: We have been damned because of the 1% service charge.

MR. FLEMING: Will it be agreeable with you gentlemen for me to ask Mr. Palmer to take the notes, confer with me and draft the final report?

(All agreed:)

MR. FLEMING: We will now adjourn.

The Meeting adjourned at 3:10 P. M.

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