Statement of J. L. Robertson, Vice Chairman,

Board of Governors of the Federal Reserve System

before the

Senate Banking and Currency Committee

on

H. R. 14026

September 13, 1966

The Board of Governors of the Federal Reserve System endorses the legislative proposals placed before this Committee which would provide:

(a) flexible authority for all federal supervisory agencies to set maximum rates on deposit-type accounts;

(b) expansion of the permissible range of reserve requirements on time deposits in member banks; and

(c) authority for the Federal Reserve System to buy and sell obligations of all federal agencies.

All of these changes would be helpful in permitting actions that could (1) moderate the uneven impact of credit pressures upon different sectors of the economy, and (2) smooth adjustments to changing economic and financial conditions.

This Committee is already abundantly aware of the kinds of sharp changes in savings flows and credit market conditions that can develop. The Board of Governors is concerned about the heavy impact of these changes

(a) on housing;

(b) on the liquidity of financial institutions; and

(c) on the effectiveness of monetary policy in curbing the expansion of bank credit.

This proposed legislation would enable us to establish different ceiling rates of interest on the basis of size of deposit or otherwise. Although regulations that would permit higher rates on large deposits than on small are in many ways distasteful, it may be the best way of working out of a difficult - but, I hope, a temporary - situation.

However, it is important that regulatory actions to moderate extreme credit pressures be not only effective but also equitable as among the major financial sectors involved. This is why the Board of Governors has urged the provision of the same kind of interest rate regulation for thrift institutions as for commercial banks.

Our views with respect to this proposed legislation have not changed since my testimony before this Committee on August 4, 1966. However, the bill was amended in the House of Representatives in two respects:

(1) a "sense of Congress" provision with respect to reduction in interest rates was incorporated in section 1; and

(2) section 7 was added to limit the effectiveness of the new legislation to a one-year period beginning with the date of enactment, at the end

of which time the law would revert to its status immediately prior to the enactment of the bill.

Treating with these amendments in reverse order, let me say, on behalf of the Board of Governors, that we doubt the wisdom of limiting the effectiveness of this legislation to a one-year period. In our view, the expanded basis for setting reserve requirements on time deposits in member banks should be permanent, and this is likewise true with respect to the purchase and sale of "agency" issues. The limiting of the effective period of the legislation might thwart the effective use of the new authority. For example, the Board of Governors might be reluctant to raise reserve requirements on time deposits if it knew that those increases would automatically be reversed at the end of a year, when conditions might be such that a reduction in reserve requirements on time deposits would be undesirable.

It could also be that ceiling rates on certain time deposits, fixed under the authority of this proposed law, would automatically be altered or reversed, contrary to the current needs of the economy, simply by virtue of section 7 of the proposal rather than the prevailing economic conditions. In addition, the authority of the Federal

Reserve to purchase and sell all Agency issues - rather than just a selected few - is desirable as a permanent measure. I can think of no valid reason for limiting this expanded authority to one year.

Furthermore, we believe that the authority of the Federal Home Loan Bank Board and the Federal Deposit Insurance Corporation to set maximum rates of interest or dividends on deposit-type savings of thrift institutions should be permanent rather than temporary.

For these reasons, we urge that section 7 of H. R. 14026 be deleted.

With respect to the "sense of Congress" amendment, contained in section 1, the Board of Governors offers no comment other than that this is the only provision of the bill as to which a one-year limitation may be appropriate. It is doubtful that the Congress would wish to incorporate a "sense of Congress" provision of this nature in permanent legislation, since it is obviously aimed at present conditions in which the strength of credit demands has lifted interest rates to exceptionally high levels.