For release on delivery
Saturday, June 19, 1976
12:30 PM P.D.T.
(3:30 PM E.D.T.)

The Proper Limits of Openness in Government

Address by

Arthur F. Burns

Chairman, Board of Governors of the Federal Reserve System

at the

1976 International Monetary Conference

San Francisco, California

June 19, 1976

During the past decade we have witnessed profound changes in the attitudes of Congress, the courts, and the public generally toward "secrecy" in government. Since the passage of the Freedom of Information Act in 1966, the public has had broad access to government documents, and almost daily one reads of new legislative proposals or judicial decisions that would require agencies of government to make public some aspects of their business that previously had been kept confidential. The balance between the needs of government to carry on certain aspects of its business in confidentiality and the right of the public to know what is going on in government is nowadays more frequently being struck on the side of disclosure. At a time when anti-establishment feeling is running high, there seems to be little inclination to consider what limits the national interest should impose upon openness in government.

The acceleration of the trend toward greater disclosure is unquestionably part of our Nation's reaction to Vietnam and Watergate. By 1972, a large section of the American public, including many members of the Congress, already felt that information vital to understanding the Vietnam war and its proper financing had been withheld or distorted by the Executive branch. The shocking revelations that soon followed of the Watergate crimes and other excesses at the highest level of government diminished still more the credibility of government. The very fact that serious misconduct by high government officials had been so recently concealed under spurious claims of national interest has naturally resulted in widespread public skepticism about the need for confidentiality in any phase of government business.

It has now become a popular saying among articulate advocates of disclosure that the government's business is the people's business, and that the people's business should be carried on in public. But this is a slogan, not a reasoned argument. Moreover, it is a dangerous slogan, because it obscures the practical need to conduct some of the work of government in private. The efforts to dispel mistrust in government by exposing more of the process to contemporaneous public view are undoubtedly well-meaning, but they run a serious risk of impairing the ability of government to carry out certain of its necessary activities effectively.

The trend toward increased openness in government should be of special significance to the banking industry. Historically, banking and bank supervision have been subject to a high degree of confidentiality. The process of bank examination, in particular, has been surrounded with elaborate safeguards intended both to protect the privacy of bank customers and to preserve public confidence in individual banks and the banking system as a whole. Yet during the past ten years a number of laws have been enacted -- and a mass of regulations promulgated under Congressional mandates -- requiring banks to make greater disclosure to their customers and security holders, and in recent months there have been several significant attempts in Congress to breach the confidentiality of the supervisory process. These events mark a serious departure from tradition with respect to banking matters, and both bank regulators and bankers must come to terms with these changing attitudes.

At the Federal Reserve we have been deeply concerned about two disclosure issues that have confronted us recently. One of these involves the disclosure of examination reports in connection with a Congressionally ordered study of the bank supervisory process. The other involves disclosure of certain aspects of our decision-making process -- in particular, the application to the Federal Reserve of one or another of the "Government in the Sunshine" bills that may soon become law.

I would like to discuss each of these issues in some detail, because I believe that the positions we have taken indicate areas in which the public interest requires some limits on openness in government.

To be fully effective, the process of bank supervision -- and by this I mean the process by which the banking agencies detect problems or potential problems in banks and attempt to remedy or prevent them -- depends heavily upon an atmosphere of free communication between bank officials and examiners. While our laws have not yet recognized an enforceable privilege for such communications -- similar to that which attaches to the relation between a lawyer and client or a doctor and patient -- there are significant protections in this area. For example, an examiner or some other agency employee who makes an unauthorized disclosure of information obtained in the examination process may be subject to criminal penalties. Even the Freedom of Information Act expressly recognizes an exemption for documents relating to the bank examination process.

The banking agencies traditionally have gone to great lengths to protect the confidentiality of examination reports. They have done so for three principal reasons: First, public disclosure of problems surrounding a bank could threaten such swift erosion of public confidence in the bank that the ability of supervisors to remedy those problems might be destroyed. Since the main purpose of bank supervision is to prevent bank failures, public disclosure of the results of the examination process could run directly counter to the very objective that the supervisors are attempting to achieve. Second, bank examination reports typically will contain confidential information about bank customers that could damage the legitimate interests of those customers if it were disclosed publicly. We feel a very deep obligation to maintain confidentiality in this area. Finally, we believe that if examination reports were made public, bankers would be less candid in discussing their problems with the examiners, who in turn would be less candid in their appraisal of bank portfolios and bank managements. The effectiveness of the examination process itself would thus become impaired.

The Federal Reserve has recently had its commitment to the principle of non-disclosure of examination reports tested.

You may recall that in January of this year two of the country's largest newspapers published highly confidential information from examination reports and internal supervisory memoranda relating to so-called "problem" banks -- that is, institutions which had received or were receiving special supervisory attention. These disclosures set off a number of inquiries in Congress. In January, the late Congressman Wright Patman proposed that the General Accounting Office conduct a far-reaching study of the bank supervisory process -- a request that was subsequently supported by Mr. Reuss, the Chairman of the House Banking Committee, and by Mr. St Germain, an influential subcommittee chairman. At about the same time, Mr. Proxmire, the Chairman of the Senate Banking Committee, proposed a similar study by GAO, to be conducted under the general direction of the Committee staff. In each case the focal point of the study was to be on the bank examination process, so that disclosure of examination reports would be required. A subcommittee of the House Government Operations Committee similarly indicated its intention to conduct such a study through its own staff, again focusing on the examination process. It sought authority in this connection to subpoena the Comptroller of the Currency to produce examination reports of more than 60 national banks.

In response to these Congressional initiatives, we at the Federal Reserve informed the two Banking Committees that we would welcome a meaningful inquiry into the performance of our bank supervisory responsibilities, but that we strongly opposed disclosure of bank examination reports. In order to permit such a study to go forward, we proposed a means by which GAO could look into the performance of our bank supervisory functions without the need for disclosure of the identities of individual banks or bank customers. We further offered to work with the Committees in developing a procedure by which information on the bank supervisory process and the health of the banking system could be supplied on a regular basis to assist the Committees in performing their oversight responsibilities.

Our staff negotiated at length with GAO, both on the issue of disclosure of examination reports and on the scope of the study itself. We explored a number of possible ways of providing information from examination reports without disclosing the identities of banks or their customers, but GAO would not accept any such limitations. The negotiations finally resulted in an agreement under which GAO will have access to examination reports of a sampling of state member banks on a carefully controlled basis. The security of these materials will be closely guarded. GAO will not be permitted to remove from our premises either the examination reports, copies or extracts of reports, or notes or other work papers generated by GAO itself during the study, and all such materials will be kept under lock at the Board. When GAO completes its study it will prepare a report to the Congress, but that report may not identify any bank, bank official, or customer, and it may not be framed in such a way as to permit such identification. Furthermore, GAO must give us an opportunity to review its report in draft form, so that we will be able to insure that no improper disclosure of examination report information is made.

I am pleased to say that both Mr. Reuss and Mr. St Germain of the House Banking Committee have accepted our agreement with GAO. More important, they have assured the Comptroller General that no attempt will be made to compromise the agreement by requiring disclosure of confidential information. An important precedent has been established, therefore, in support of our position that bank examination reports should not be a subject of Congressional staff study. Indeed, the fact that the Comptroller of the Currency and the FDIC had previously agreed to a GAO study, and that we too were involved in negotiations with GAO, finally persuaded the House Government Operations Committee not to issue a subpoena to the Comptroller for the production of bank examination reports in connection with the study being conducted by its staff.

We have by no means satisfied all demands for access to examination reports. With increasing frequency other agencies of government with investigative or law enforcement responsibilities are looking to the bank examination process as a means of obtaining information to carry out their responsibilities. It has been our practice in the past, when access to examination reports has been sought by other agencies in connection with specific allegations of wrongdoing, to allow carefully limited access under conditions intended to protect both banks and their customers from unwarranted invasions of privacy. Furthermore, when our examiners uncover evidence of crime in the course of their examinations, they regularly refer such matters to the proper authorities. However, we do not believe it appropriate for other agencies to use the examination process as a means of prospecting for evidence of possible wrongdoing in areas beyond our jurisdiction. I say this not because we want to protect bankers or bank customers from lawful investigation into possible misconduct, but because we firmly believe that the principal objective of the examination process, namely, maintenance of a safe and sound banking system, would be injured by burdening that process heavily with other tasks.

I would now like to turn to the question of disclosure of the Federal Reserve's internal decision-making process. This question has received considerable public attention recently because of a decision by a Federal district judge in Washington ordering the Federal Open Market Committee to make available to the public, immediately after each meeting of the FOMC, the guidelines agreed upon at that meeting for market operations by our New York bank during the succeeding month. In addition, the Court ordered that segregable factual portions of the minutes of two FOMC meetings be made promptly available to the plaintiff in that judicial proceeding.

We have appealed certain aspects of the Court's order, and I am therefore limited in the extent to which I may comment upon the case. But I can say that even if the district court's interpretation of the Freedom of Information Act is upheld, I believe the public interest would not be served by immediate disclosure of FOMC strategy. Our open market activities are watched closely by some of the sophisticated money market specialists. Based upon their observations they make judgments about the current direction of monetary policy, and they shape their strategies in the securities market on the basis of these judgments. While their guesses are often astute, there is sufficient uncertainty to cause them to temper their aggressiveness.

If FOMC plans were disclosed immediately, however, market professionals would know at once the key determinants of our open market operations over the next four or five weeks. Sophisticated and experienced market participants, equipped with financial resources to act quickly, would be far better situated to interpret and trade on this information than members of the general public. Needless to say, the Federal Reserve has not the slightest interest in assuring profits for speculators in stocks or bonds -- the ones who would inevitably be the chief beneficiaries of immediate disclosure. And there is still another difficulty with premature publicity. Not only would the large speculators gain trading advantages, but -- being armed with these new insights -- they would be apt to engage in more aggressive market behavior. As the response of market rates to Federal Reserve actions was accentuated by such behavior, the result could well be greater short-run volatility in interest rates. Exaggerated shifts in market expectations and interest rates caused by premature disclosure of FOMC strategy may in turn require adjustments of policy simply to maintain orderly conditions in financial markets. Our ability to control bank reserves and to make effective use of open market operations might therefore be weakened.

While the case just discussed raises questions about the timing of the release of FOMC market strategy, I am even more deeply concerned about the prospect that Board deliberations prior to decision may be opened to public scrutiny. One of the principal legacies of Watergate is a deep public cynicism about the process of government decision-making. Many people seem willing to assume that confidentiality in the decision-making process promotes improperly motivated or even corrupt decisions. The response to that attitude has been a drive to force government agencies to conduct their deliberations in public sessions. This movement has rallied under the banner of "Government in the Sunshine."

There are several versions of "Sunshine" bills presently pending in Congress, and I am continually amazed at how little public attention these bills have received. The basic structure of these bills is similar: they would require multi-member Federal agencies to conduct their deliberations concerning agency business in an open forum, accessible to the public. While the bills all recognize certain exemptions from open meetings, they require that if a meeting is to be closed pursuant to an exemption, notice must be given of the subject matter of the meeting and a verbatim transcript must be made and retained. Following each closed meeting, the agency would be required to release to the public those portions of the transcript not covered by an exemption. Any member of the public could bring a court challenge to the validity of the agency's action in closing a meeting, and the court could order the entire transcript to be disclosed. This provision alone offers frightening potential for innumerable lawsuits, each of which would require individual defense.

The obstructionist dangers in this legislation do not stop there: they extend to the greater part of the substantive business of the Federal Reserve. Our deliberations on monetary policy issues involve highly sensitive questions of great national concern. The close scrutiny that is given our statements and actions in this area is itself an indication of the sensitivity of the matters with which we deal. We are keenly aware that financial markets may react dramatically, based solely upon nuances or shades of meaning in our decisions; and our public statements are drafted with great care because of this.

Similar observations apply to our bank supervisory and regulatory functions. We very often have before us detailed information about the financial and managerial condition of bank holding companies or about individual banks and their customers. Sometimes we must deal with crisis situations that may call for emergency action. It is unthinkable to me that the national interest would be served by discussion of these issues in public. Indeed, the Congress has thus far concurred in this judgment by delineating various exemptions from the requirement for open meetings. But it is no answer that certain meetings may be closed, for as long as we must keep a verbatim transcript of such meetings the threat exists that the substance of these meetings may be made public.

The underlying premise of the "Sunshine" legislation is that if the public is permitted to observe the decision-making process in action, the integrity of decision-making will be assured and public confidence in government will be enhanced. This, however, is a vastly oversimplified view of the manner in which the government works, and I believe it is a simplistic view of the way in which government should work. The advocates of this view ignore the fact that debate conducted on a stage is different in tone and quality from debate conducted in private. The simple fact is -- and I think that even the supporters of "Sunshine" legislation ought to concede this -- that debate carried on before a public audience tends to take on some characteristics of the theater, rather than serve as a search for truth and wisdom, and that the debaters themselves tend to become performers pronouncing predetermined positions, rather than participants in a deliberative process seeking to develop their own ideas and persuade their colleagues.

The advocates of "Sunshine" also overlook the fact that many actions of the Federal Reserve are quasi-judicial in nature. At almost every meeting we are called upon to adjudicate the rights of private parties seeking to engage in certain new activities or to extend the scope of their existing authority. In such matters we conduct ourselves much as judges would. It is a firm rule, for example, that Board members will not discuss the merits of an application with interested parties prior to Board action on the application. Historically, the deliberations of appellate courts on cases coming before them have not been conducted in open session. I see no convincing rationale for treating our adjudicatory deliberations differently. Of course, once decisions on applications before us have been reached, they are promptly announced and reasons for approval or denial are set forth.

There is a serious danger, I believe, that a "Sunshine" law may have the unintended effect of diminishing the quality of decision-making in an agency such as the Federal Reserve Board. The Board has a long tradition of free discussion. We have important decisions to make, and we have been extremely fortunate to have

Board members and staff of high intellectual competence. Our deliberations are characterized by deep respect for one another's opinions, and by an atmosphere that welcomes completely free expression by both Board members and staff. A fundamental precondition to the free exchange of ideas is an atmosphere in which new or unpopular ideas -- or even wrong ideas -- can be put forth for discussion without fear of embarrassment or recrimination.

As we attempt to decide difficult issues, many things are said in our Board meetings that might well not be said if we were in public session or if each word spoken were subject to later public disclosure. This is not to say that "evil" views are being expressed; it simply means that the goal of fully informed decision-making can only be achieved if the participants are free to bring to light all considerations that may bear upon their actions. Were we forced to conduct our deliberations under circumstances where highly sensitive matters could not be discussed in private, the quality of our decision-making would unquestionably deteriorate and the public interest would ultimately be disserved.

Although the Board has at times been accused of being overly secretive in performing its responsibilities, I believe that charge is not based upon fact. We make far more information available to the public about our activities than any other central bank. Very few of the world's central banks regularly inform their national legislature of their plans for the future course of monetary policy, and none does this as often as the Federal Reserve. Not only do we appear frequently before committees of Congress -- Board members have testified 25 times already during 1976 -- but we deal constantly with inquiries from Congress and the public about the substance of our work. In our responses we strive to be as forthcoming and helpful as we can. In the bank regulatory area, unlike many other agencies, we have for many years published written decisions explaining our actions in application proceedings, such as those involving bank holding company and merger actions.

I believe we must face the problem presented by the "Sunshine" legislation realistically. Certain of the "Sunshine" bills and associated Congressional reports define the term "meeting" so broadly that a bare quorum of the Board -- four members -- literally could not converse informally about any aspect of the Board's business without being required first to issue notice to the public and thereafter to conduct a public discussion or hold a closed discussion with the tape recorder running. In certain instances, these requirements would apply even to discussions between only two Board members.

In conclusion, I fail to see how the national interest would be served by circumscribing actions of the Board in an endless array of recording requirements. In such circumstances we could not be expected to maintain the quality of thorough analysis and thoughtful care that has marked our work over the years. If the Board were exempted from the verbatim transcript requirement, our difficulties with the "Sunshine" legislation would be substantially reduced. However, if any of the "Sunshine" bills as now written becomes law, an agency such as ours would be in an almost impossible position. On the one hand, we could operate under the law as enacted with the virtual certainty that some of the destructive consequences I have indicated -- and I have not even mentioned international complications -- will occur. On the other hand, we could go through the motions of adhering to the law's requirements but, as a practical matter, resort to "underground" procedures that would effectively circumvent the law. That would be a cruel dilemma, but I would have no hesitation about the choice. I must and do reject circumvention as a suitable course for the Federal Reserve. We will have no part in any such dubious exercises.

In sharing with you my views on some of the disclosure issues that have come before the Board recently, it has been my purpose to question the premise that disclosure is a desirable end in and of itself. I particularly question the premise that disclosure is the cure for bad government. To be sure, it is more difficult for corruption and malfeasance to occur when the public has easier access to the inner workings of government. But there are legitimate and important reasons for permitting certain processes of government to operate in reasonable confidentiality. In striving to renew the public's trust in government, we should recognize that such trust ultimately will depend not upon the public's observation of the process of government decision-making, but upon their perception that their government is comprised of men and women of intelligence and integrity making reasonable decisions in the public interest.

* * * * * *