BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

December 8, 1961

CONFIDENTIAL (FR)

To: Federal Open Market Committee

From: Mr. Young

For your information there are enclosed: (a) a collation of comments made by eleven Presidents on the draft standing rules and directives of the Federal Open Market Committee circulated under my memorandum of September 6, 1961; (b) a checklist of specific issues raised in response to the September 6 drafts; and (c) a version of the September 6 draft of standing rules incorporating editorial and minor substantive changes suggested by Committee members and others and considered by the Secretariat to be noncontroversial.

The organization of the checklist parallels that of the collation. The checklist is designed to aid in focusing consideration and discussion of the issues presented to the Committee on this matter. Parts I and II of the checklist and collation are concerned with the matters of basic importance for the December 19 meeting of the Committee, including the questions of what disposition the Committee should make of its present operating policies and what specific language should be employed if revised statements are to be adopted.

Parts III and IV of the collation and checklist relate to the issues concerning the Committee's current policy directive to the New York Bank. While it would be desirable to reach a Committee decision at the December 19 meeting concerning the desirability of splitting the directive between a continuing and a current policy directive, it would not be essential to resolve all of the issues raised in these two parts at this meeting.

No questions are included in the checklist on the subject of Part V of the collation, frequency of publication of the Policy Record, on the grounds that this matter is deferrable until a later meeting.

The checklist also omits questions on the specific language of a continuing authority directive. The comments made by the Presidents on the September 6 draft of this proposed directive appear amenable to incorporation in a revised version, which accordingly is being prepared and will be sent to you in a few days.

Ralph A. Young

Ralph A. Young, Secretary,
Federal Open Market Committee.

Enclosures 3.

CONFIDENTIAL (FR)

December 8, 1961

COLLATION OF SUGGESTIONS ON PROPOSED CHANGES IN OPEN MARKET COMMITTEE PROCEDURES

Prepared by
the Secretariat,
Federal Open Market Committee

CONFIDENTIAL (FR)

Collation of Suggestions on Proposed Changes
in Open Market Committee Procedures

At the Open Market Committee Meeting of September 12, 1961, the Chairman requested that members and Bank Presidents not currently serving on the Committee study a number of documents concerning possible changes in the Committee procedures and send their comments to the Secretary for distribution to other members in preparation for a later discussion by the Committee. Among the documents distributed was a memorandum by Mr. Young dated September 6, 1961, entitled "Discussion of changes in the Committee's procedures," with three attachments consisting of draft texts of (I) "Standing Rules Governing Open Market Practice of the Federal Open Market Committee," (II) "Federal Open Market Committee's Continuing Authority Directive to the Federal Reserve Bank of New York," and (III) "Current Economic Directive" (in four alternative forms).

The purpose of this memorandum is to collate the views expressed in the replies received to date. 1/ The memorandum is organized in terms of a number of issues which are interrelated in various ways but which, it is believed, are more or less separable.

1/ Replies have been received from the following, under the indicated dates: Mr. Allen, September 27; Mr. Bopp, November 22; Mr. Bryan, November 24; Mr. Clay, November 13; Mr. Deming, November 24; Mr. Ellis, October 9; Mr. Fulton, November 3; Mr. Hayes, November 3; Mr. Irons, November 1; Mr. Swan, November 10; and Mr. Wayne, October 11.

Not all of the replies expressed views on each of the issues distinguished, which were not posed as such in the materials distributed, but (with two exceptions) all of the views expressed can be classified under them and all substantive comments made in the replies are quoted here. The two statements on other issues are presented in a final section, headed "Other comments," which begins on page 55. The issues and their page references are as follows:

I. General issues relating to "Operating Policies" or "Standing Rules"

a. Should the Committee adopt and publish any "standing rules" regarding its general objectives and procedures at this time?

Six of the Presidents (Messrs. Allen, Bopp, Ellis, Deming, Fulton, and Hayes) believe the Committee should not.

Mr. Allen: "My suggestions . . . envision abandonment of existing operating procedures and policies. Because the Committee meets at three-week intervals I feel that there is no further need for formal agreement on such procedures or policies, however desirable that may have been at one time. Further, it seems needless to make pious pronouncements annually which represent either a paraphrase of statutes or policies which the Committee at least occasionally decides to disregard."

Mr. Bopp: "I am persuaded by the arguments that have been advanced to eliminate the Standing Rules. It seems to me undesirable to build any 'boxes' that might inhibit the Committee from doing whatever it considers appropriate at any meeting because of fear that it might violate a 'commitment' to the market.

"On the other hand, if most members of the Committee feel strongly that standing rules are necessary, I would feel that the rules should be used for internal purposes and not published. One disadvantage of published rules is that any departure would require a public announcement. Another is that the Committee might refrain from deviating from the rules in cases when it would be desirable but not urgent to do so."

Mr. Ellis: "The FOMC faces the difficult problems of adjusting its actions to changing circumstances and seeking better public understanding of its actions. In this process we must avoid oversimplification that results in distortion of understanding. Reliance upon any single set of rules or imposing limitation of Committee action through such rules in policy determination is dangerous and risks denial of needed flexibility in adjusting policy to constantly changing conditions, the elements of which combine in shifting proportions....

"I urge the Committee not to attempt at this time the development and adoption of a set of 'standing rules' to replace those suspended since February. The original purpose of the 'rules' has been stated as helping to improve the functioning of the market for U. S. Securities by leading to greater self-reliance. The 'rules' singled out certain Open Market Committee practices which had been characteristic of the pegged market and which in varied form had been continued during the early period after the Accord. Suspension of the 'rules' in late February 1961 recognized new forces and different conjunctures of forces which required new working procedures to accomplish the objectives of credit policy. Experience with the new procedures that followed suspension of the rules has not been long enough to establish beyond reasonable doubt that the new techniques make a positive contribution. Evidence is lacking that the mechanical functioning of the market has been damaged. Market reactions have probably been no greater than those which would normally occur during a period of change characteristic of the last six months. At the same time, certain positive accomplishments of credit policy can be cited.

"Under these circumstances it seems desirable that members of the Committee will wish to continue study of the new techniques against the framework of the market as it has now developed and changed relationship of economic forces as may have evolved in the last 10 years. Before any new set of 'rules' or policies is adopted, the Committee should come into closer agreement on the matters of principle in operations. This reasoning leads me to conclude that the Committee should not attempt at this time to develop and adopt a set of 'standing rules' to replace those in effect prior to February 20."

Mr. Deming: "After studying all of the suggestions concerning the standing rules and trying my own hand editorially, I come, somewhat reluctantly, to the same conclusion reached earlier by Messrs. Allen and Ellis that the rules should be eliminated. My reluctance has little to do with the substance of the question; in general, I concur in the position taken by Messrs. Allen and Ellis that the rules are unnecessary and can prove to be administratively embarrassing at times. Rather it reflects my feeling that we cannot take this action gracefully. I have become convinced, however, that neither maintenance of the rules, as is, nor rephrasing to make them more broad can be accomplished with any more grace.

"Along with others, I have tried to explain the background of the rules, have noted that the language itself makes plain that they can be changed or deviated from at any time the Committee chooses to do so, and have stressed the demonstrable fact that they have not been rigid in application. I have noted that they are mainly technical operating matters, that there are technical operating reasons for them and that short-term securities are the best instruments for most central banking open market operations. Progress toward outside understanding and acceptance of the rules seems to me to have been zero at best, and I am not at all sure that it has not been negative. Therefore, I believe that it is hopeless to try to live with the rules without change.

"It seems to me that there are two major disadvantages to amending the rules. First, unless they are written in very broad language they are subject to the same kind of attack as the present rules and, in fact, they may be limiting at times and thus force hard-to-explain deviations; if they are written so broadly as to escape these difficulties, they become almost meaningless as 'rules'. Second, the difficulties involved in explaining the substance of amended rules and the reasoning behind the changes would be at least as great, and perhaps more so, than just eliminating the rules completely.

"Therefore, I believe that we should abandon the rules and, at the proper time, say so publicly. I believe the action should be taken before the end of this year so that it can be covered in the Annual Report for 1961.

"My own preference as to form of announcement would be a tightly written article which would trace the background, rationale and record of the present operating rules, discuss the role of short-term securities in central banking open market operations, note that they have stirred up so much misunderstanding and controversy that they no longer serve any particularly useful purpose, and that the Committee, with its frequent meetings, no longer sees the need for such a body of rules. The article should be quite frank in approach but not apologetic. I see no reason why it should not appear, perhaps in somewhat longer form, in the Bulletin as well as in the Annual Report.

"In effect, the above comments apply to the first five 'rules' in Attachment I. If repurchases are covered in II, there should be no need for Point 6 in any set of 'rules' anyway. Point 7, designation of the New York Bank, can be covered, as now, by action at the organization meeting, and Point 8 should be left where it now is in the 'Rules on Organization'."

Mr. Fulton: "I am not clear about the desirability of publishing the Standing Rules of the Committee at this time. We should try to reach agreement on the Rules as soon as possible, and then test to see if we can live with them for a period of six months or so before they are published. It would be unfortunate to rush into print with a set of rules that might be violated soon after publication."

Mr. Hayes: "We are much attracted by Mr. Allen's suggestion that there is no further need for a formal statement of operating procedures. We agree with him that since the Committee meets at three-week intervals there is no need for a formal published statement on operating rules. The absence of a public statement would not, of course, involve any relinquishment by the Committee of control over the general conduct of open market operations. The Committee would still be free to give the Federal Reserve Bank of New York any kind of instructions it wishes. The absence of a public statement of procedures would leave the Committee's hands untied and permit it to take whatever actions future circumstances might indicate as desirable without setting off the magnified and exaggerated reactions in the market and in the press that would ensue if its action were an exception to a published statement of formal rules. In view of the continuing problem posed by the imbalance in our international accounts, it seems to us especially important for the Committee to retain the high degree of freedom to act that would result from giving up a published statement of operating procedures....

"In urging the adoption of Mr. Allen's suggestion that there be no formal statement of operating procedures, we are not attempting to evaluate the results of our operations outside the short-term area in recent months. Nor can we attempt to predict the extent to which, over the months and years ahead, the Committee will find it desirable to operate in intermediate- and longer term issues. Rather, we would emphasize that whether we like it or not, international considerations are going to be highly important for a long time to come, and they will require maximum flexibility on the part of the System. Thus it seems important to us to retain full freedom of action, preferably by having no published statement of formal rules, or at least by casting any statement of rules in terms broad enough to encompass whatever operations the Committee may wish to conduct, with whatever frequency the Committee may wish to conduct them."

Five of the Presidents (Messrs. Bryan, Clay, Irons, Swan and Wayne) imply that they take an affirmative position on this issue. Mr. Irons writes, "I would accept your draft statement (of Standing Rules) with the following reservations . . . ." His reservations concern language, and are noted at a later point. Messrs. Bryan, Clay and Swan similarly confine their comments to specific language. Mr. Wayne writes:

"Under this plan (for a division of statements into three parts) the Committee would state its basic goals and purposes once a year in the standing rules and then omit reference to them in the current policy directive. I believe that the inclusion of what President Allen calls 'pious pronouncements' in the current directive has done much to add to its complexity and obscurity."

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II. Language for Operating Policies, or Standing Rules

a. General coverage and nature

Suggestions for revisions of the draft standing rules circulated as Attachment I to Mr. Young's memorandum of September 6 are made by Presidents who feel there should be no standing rules (with the exceptions of Messrs. Allen and Deming)as well as by other Presidents, for use if a majority of the Committee favors publication of rules. The following general comments are offered:

Mr. Bopp: "If the Committee wishes to retain the standing rules, whether published or not, I would in general favor wording as broad as possible to accomplish the purpose at hand. As examples, I would stress the broader objective of open market operations rather than supplying and absorbing reserves; prefer to emphasize a wide latitude of operations in all maturities and then make the qualification that most transactions ordinarily would be in short terms; incline to have the Committee retain a free hand to engage in swaps and a free use of repurchase arrangements."

Mr. Bryan: "I find myself largely in agreement with the letter of Mr. Irons. The suggestions that Mr. Irons has made for changes in the draft proposal of standing rules all strike me as excellent, with one exception. (Note: The exception is cited below.) ....

"Absent from Mr. Irons' letter are several suggestions that I regard as objectionable. He does not:

"(1) Eliminate from the statement on standing rules the reference to bank reserves as an objective of open market operations;

"(2) Eliminate the reference to the maturities in which operations of U. S. Government securities are to be conducted;

"(3) Weaken in any way the present prohibition against dealings in issues involved in a Treasury financing operation; or

"(4) Remove the present 15-month maturity limitation on U. S. Government securities held under repurchase agreements.

"I like two of Mr. Irons' suggestions: these are his support in Rule 2 of a statement that would define in terms of some precisely-stated number of months just what 'short-term issues' are, and his insertion in Rule 5 a statement that would permit swaps only upon the authorization of the Committee."

Mr. Ellis: "If . . . a substantially similar series of rules as outlined in your memorandum is to be continued, it would be preferable to have them as brief as possible and not involve taking positions to which exceptions may have to be made. Any statement of policies adopted by the Committee should be pointed to what we want open market operations to accomplish in terms of credit policy and using them to make such policy effective. Necessarily, such a statement will have to be broad and general.

"It would also seem to be logical that rules which may be adopted should be made a part of the Regulation Relating to Open Market Operations of Federal Reserve Banks, rather than appearing in portions of the minutes of Open Market Committee meetings which are published in the Annual Report of the Board of Governors. These rules seem in essence to be policies or working procedures and are thus generally similar to Regulation A which outlines the guiding principles or working procedures for carrying out the discount function. Placing the 'rules' in the 'Regulation' would cover open market operations in a suitable complement to Regulation A.

"Even though the Committee may decide not to publish its policies as suggested above, it will need to consider the relationship between its published Regulation and Rules on Organization and Information and Rules on Procedure (as amended June 22, 1955) and the policies to be spelled out in the committee minutes. For example, would the Committee intend through adoption of Rule #8 to modify its Sec. 2, Par. (c) published statement on 'Rules on Organization' as to frequency of meetings? This reasoning leads to the conclusion that the Committee might well adopt as a general practice an annual review of its entire set of rules and procedures to ensure their continued applicability and compatibility.

"Turning specifically to the language of Attachment I, I realize that the present formulation of the rules represents a compromise in wording as will any which may be developed in the future. For this reason, I am limiting my comments below to examples of the way in which the concepts should be broadened and generalized."

Mr. Hayes: "If, however, the Committee should wish to retain such a statement, we would urge that the language of the statement be sufficiently broad to avoid giving an impression to the Congress and the public that the Committee has tied its hands in any way regarding the broad objectives of open market operations and the procedures used to implement those objectives....

"The draft of operating procedures contained in Attachment I to your memorandum of September 6 seeks to introduce a greater degree of flexibility into our open market practices. But it seems to us that the draft does not go far enough in that direction to avoid the kind of Congressional and public misunderstanding and debate which, as the Chairman has pointed out, has often obscured a real understanding of the substance of System policies over the past few years. In fact it would still leave the System boxed in as it has been in the past."

Mr. Clay: "In formulating our views as to the appropriate content of these operating procedure rules and the directive, we also have reviewed the replies of Presidents Ellis, Hayes, Fulton, Wayne, Allen and Irons. Their recommendations adopted a broader, less limited approach to the formulation of the operating procedure rules than is contained in Attachment I. This broader approach we favor very strongly. At present, the need for such an approach appears most clearly on the ground that international considerations now and for the foreseeable future dictate it. Our reasons for favoring a flexible approach are not confined to the balance of payments problem, however, but rather reflect our conception of the role and scope of monetary policy for the domestic economy as well.

"While a draft of operating procedure rules modifying Attachment I might be worded in various ways, the draft included in Mr. Hayes' statement of November 3, 1961, accords quite well with our views with two exceptions . . . . (Note: The exceptions relate to paragraphs 3 and 4, and are cited in the next section below.)

"It is preferable to confine the specific details of how operations shall be conducted to (the continuing authority directive) rather than to include them in the standing rules of the Committee."

Mr. Swan: "We visualize the Standing Rules as being a statement of broad principles, subject to quite infrequent changes, and not incorporating operating procedures."

Mr. Wayne: "With the exception of paragraph 2, I agree with the draft of the standing rules as given in Attachment I."

A number of suggestions are made for deleting particular paragraphs in the draft standing rules, and for moving paragraphs to some other document. These are cited below together with suggestions for revisions of language.

* * * * *

b. Specific language for the standing rules

The paragraphs of the September 6 draft standing rules are quoted below (following the numbering and line spacing of Attachment I to the September 6 memorandum) together with the proposals for modification of each paragraph and supporting arguments for the proposed modifications. The statement that a President "concurs" in the draft wording of a particular paragraph may reflect either a positive assertion to that effect or the absence of a proposal for revision.

Preamble

As provided in section 12A of the Federal Reserve Act and in the Regulations of the Federal Open Market Committee, open market operations of the Federal Reserve Banks are conducted "with a view to accommodating commerce and business and with regard to their bearing upon the general credit situation of the country." To implement this governing principle as well as to help achieve and maintain a high level of economic activity and employment, sustainable growth, stability of the price level, and a strong position in the world economy, the Committee adopts the following standing rules regarding open market practice, subject to change by the Committee at any time:

Messrs. Clay, Hayes and Wayne concur in the draft wording.

Suggestions for revision:

Mr. Ellis: Redraft, broadening to include ideas from foreword to Regulation A.

Mr. Fulton: Lines 10-11: Delete phrase beginning "subject to..." and restate as new paragraph 9.

Mr. Irons: Lines 8-9: Replace phrase, "the price level" with phrase, "price levels."
Line 9: Replace phrase, "strong position in the world economy" with phrase, "sound international position of the dollar."

Mr. Bryan: Concurs in Mr. Irons' second suggestion, but not the first.

Mr. Swan: Lines 6-7: Replace phrase, "as well as to help," with phrase, "by helping to."
Line 9: Concurs in Mr. Irons' suggestion.

Supporting Arguments:

Mr. Ellis: "In its present form, the preamble in Attachment I must be considered as a formulation of basic objectives of the System. Taken in conjunction with Rule #1 as written, it is inconsistent with a statement of System objectives which appears as a foreword to Regulation A. Paragraphs (a) and (b) say in part: 'This (discount) function is administered in the light of the basic objective which underlies all Federal Reserve credit policy, i.e., the advancement of the public interest by contributing to the greatest extent possible to economic stability and growth. The Federal Reserve System promotes this objective largely by influencing the availability and cost of credit through action affecting the volume and cost of reserves available to the member banks. Through open market operations and through changes in reserve requirements of member banks, the Federal Reserve may release or absorb reserve funds in accordance with the credit and monetary needs of the economy as a whole.'

"A redrafting the preamble broadened to include some of the ideas in Paragraphs (a) and (b) of Regulation A or at least some reference to the fact that the Committee is interested in both availability and cost of credit in the markets seems essential. If changes along these lines are accepted, Rule #1 becomes unnecessary."

Mr. Fulton: "...the phrase 'subject to change by the Committee at any time' has been deleted, and restated as a separate item (item 9) to give this point added emphasis."

Mr. Irons: "It seems to me that the suggested statement with respect to the international position of the dollar, while certainly broad enough is not quite as broad in all of its implications as the statement in your draft, namely, 'a strong position in the world economy.'"

Mr. Swan: "'by helping' is inserted to make clear that the principle governing open market operations is consistent with our national economic objectives rather than apart from them."

Paragraph 1

Open market operations are conducted to supply or absorb bank reserves consistent with the credit and monetary needs of the United States, in the light of both the domestic economy and international developments.

Mr. Wayne concurs in the draft wording.

Suggestions for revision:

Mr. Bopp: Would stress the broader objective of open market operations, rather than supplying and absorbing reserves.

Mr. Ellis: Delete, if proposed redraft of preamble is accepted.
Line 1: Insert "primarily" after "conducted."

Mr. Fulton: Line 1: Insert "primarily" after "conducted."
Lines 2-4: Replace second part of sentence, beginning with phrase, "the credit and monetary....." with the following:

"...the monetary and credit needs of the United States, in order to foster the broad objectives of monetary policy described above."

Mr. Hayes: Replace whole paragraph by:

"Open market operations are conducted to promote appropriate monetary and credit policies in the light of both domestic and international developments."

Mr. Clay: Concurs in Mr. Hayes' suggestion.

Mr. Irons: Line 2: Insert after "reserves" the following:

"or for such other purposes as the Committee considers..."

Or adopt this whole alternative paragraph:

"Open market operations shall be conducted for the purpose of carrying out the domestic and international objectives of monetary and credit policy."

Mr. Bryan: Concurs in Mr. Irons' first suggestion.
Does not favor eliminating reference to bank reserves.

Mr. Swan: Line 1: Insert "primarily" after "conducted."
Lines 3-4: Replace the phrase, "both the domestic economy and international developments" with the phrase, "the above principle."

Supporting arguments:

Mr. Ellis: "Rule #1 as worded can be accepted as an accurate description of the Committee's policy only if we interpret it to mean that supplying 'reserves consistent with the credit and monetary needs . . .' also means supplying reserves in such a way as to affect interest rates consistent with credit and monetary needs. For example, the record of policy actions covering the Open Market Committee meeting of February 7, 1961, contains the following sentence: 'This policy called for providing reserves to the banking system to meet the needs of the current business situation, and also avoiding direct downward pressure on short-term interest rates, or even permitting them to rise, in view of the relationship of the short-term rate structure to the balance-of-payments problem.'

"This excerpt and others like it in other portions of the record substantiate the view that the System is concerned with something more than simply to supply or absorb bank reserves. We must continue to be interested in levels of interest rates as an explicit part of open market policy. This being so, the language suggested in Rule #1 is an insufficient statement of the basic reason for open market operations. As a minimum, the word 'primarily' should be inserted following the word 'conducted'. . . ."

Mr. Fulton: ". . . the word 'primarily' has been inserted. . . since we are now concerned, in part, with the effect of our operations on the bill rate. The end of the sentence has been rephrased to refer back to the broad objectives of monetary policy described in the preamble, in order to avoid re-emphasizing our concern with international developments. It might appear to some readers that we are giving the international situation too much weight, in the event that the Standing Rules are published."

Mr. Hayes: "...we suggest that the objectives of open market operations be phrased in broader terms than 'to supply or absorb reserves'....The proposed statement (in Attachment I) implies a considerably more narrow approach to operations than the Committee has actually been following, for the cost as well as the availability of credit has always been a matter of Committee concern; over the past year the Committee has been paying particular attention to short-term interest rates because of the balance of payments situation. We note that Mr. Ellis makes essentially this same point in his letter on these matters."

Mr. Irons: "There are times when Open Market operations may be conducted for purposes other than absorbing or supplying bank reserves. During the past several months, in our attempt to prevent too great a decline in short-term rates, we have engaged in operations which were not conducted for reserve reasons. I think it is a mistake to set up a rule as rigid as the statement in your Attachment."

Mr. Swan: "The change (on lines 3-4) would relate operations to the principle already stated."

Paragraph 2

Open market operations are transacted in United States Government securities and, as authorized, in prime bankers' acceptances. Although operations in Government securities are ordinarily conducted in short-term issues, the Committee may authorize transactions in all maturities when desirable because of economic or financial conditions.

Suggestions for revision:

Mr. Bopp: Would emphasize a wide latitude of operations in all maturities and then make qualification that most transactions ordinarily would be in short terms.

Mr. Ellis: Delete rule. Alternatively:
Line 2: Delete "as authorized."
Lines 3-6: Replace whole second sentence with:

"Most operations in Government securities are conducted in short-term issues."

Mr. Fulton: Delete second sentence.

Mr. Hayes: Replace whole paragraph by:

"Open market operations are conducted in United States Government securities and in prime bankers' acceptances; ordinarily the bulk of operations is conducted in short-term Government securities."

Alternatively, adopt Mr. Ellis's proposed paragraph.

Mr. Clay: Concurs in Mr. Hayes' proposed paragraph.

Mr. Wayne: Replace whole paragraph by:

"Open market operations may be conducted in United States Government securities of any maturity and, as authorized, in prime bankers' acceptances. Market conditions and practices, however, will usually require that the bulk of operations be confined to short-term securities."

Mr. Swan: Concurs in Mr. Wayne's proposed paragraph, with the further deletion of "as authorized" from the second line.

Mr. Irons: Possibly define "short-term" in the rule.

Mr. Bryan: Concurs in Mr. Irons' suggestion.
Would not eliminate the reference to the maturities in which operations are to be conducted.

Supporting arguments:

Mr. Ellis: "The Committee presently seems to believe that operations in maturities other than short-term serve a constructive purpose. Under these circumstances it can adopt the proposed wording of Rule #2 only by simultaneously acknowledging that the rule does not apply at present by virtue of special circumstances. Why not solve this issue by not adopting any new rule on this subject until we can operate under it straightforwardly? Alternatively, it might be worded ...." (Note: proposed wording cited above.)

Mr. Fulton: "...the reference to short-term securities has been removed, since it may be misunderstood by the public as a carry-over from our earlier 'bills-only' philosophy. If this change is made, however, the Committee would presumably wish to direct the account manager at each meeting as to the Committee's broad preferences with respect to maturities."

Mr. Hayes: "For reasons well stated by Messrs. Ellis and Wayne we suggest a recasting of the second paragraph.... The wording ... suggested by Mr. Ellis would also be acceptable to us."

Mr. Wayne: "With regard to paragraph 2, I feel strongly that a change is in order, as I indicated in my letter to you of March 20, 1961. As the draft is now worded, it would not substantially change the present situation. The words 'may authorize' mean that the Desk could not conduct operations outside the short-term field except on special authorization. If that authorization is not permanent, the making and rescinding of it would almost certainly involve extended debate. Further, the changes might well excite undue concern and speculation in the market when they become known either through rumors or from open market operations. In my judgment, the situation should be reversed; the authorization to deal in longer-term securities should be permanent and any limitation on it should be by special action. In addition, as I said in my letter of March 20, the statement as it now stands in the draft would almost certainly lead critics of the System to charge, with justification, that the System still clings to 'bills usually.'"

Mr. Irons: "The only suggestion I have with respect to your statement of Rule 2 is that 'short-term issues' should be defined in the Rule. I have no fixed number of months in mind, but I would be agreeable to a continuation of the 15 months or less that we have used, or, on the other hand, I would be willing to lengthen the period to, perhaps, 18 to 20 months. In any event, it would avoid confusion and contribute to clarity if the definition were included."

Paragraph 3

Open market operations are not for the purpose of fixing or pegging the price of any issue of government securities. If conditions in the market for Government securities should become disorderly, the Committee will take appropriate corrective action.

Messrs. Bryan and Ellis concur in the draft wording.

Suggestions for revision:

Mr. Fulton: Delete first sentence. (Note: Second sentence becomes paragraph 4 in his proposed list.)

Mr. Irons: Line 3: Possibly insert at end of first sentence:

"although such operations may tend to influence rates of interest."

Mr. Bryan: Does not concur in Mr. Irons' suggestion.

Mr. Hayes: Line 5: Replace with: "such action as it deems appropriate."

Mr. Swan: Concurs in Mr. Hayes' suggestion.

Mr. Clay: Line 3: Insert at end of first sentence:

"although such operations influence rates."

Line 5: Concurs in Mr. Hayes' suggestion.

Mr. Wayne: Line 3: Insert "United States" before "Government."

Supporting arguments:

Mr. Fulton: "The first sentence of your item 3, which states that open market operations are not for the purpose of fixing or pegging the price of any issue of government securities has been deleted; we are now in effect substantially influencing the rate on Treasury bills."

Mr. Irons: "I have no criticism with respect to (rules 3 and 4). Rule 3 does introduce the question, perhaps obliquely, of the effect of Open Market operations on interest rates. I don't object to your statement of the Rule, but I wonder whether it might be desirable to insert between the first and second sentences of the Rule, something to the effect — (Note: The suggestion is quoted above). I do not feel strongly on this point, but thought it might be considered."

Mr. Hayes: "The declaration against 'pegging' in paragraph 3 . . . is an essential operating policy. We consider it important for the Committee to reiterate this policy in its minutes if the Committee is not to continue a published statement of operating procedures. If the Committee is to have a published statement, we believe it should not contain a fixed commitment to 'correct' disorderly conditions (which the market might interpret to mean that the System would necessarily buy heavily, possibly to an extent equivalent to pegging), since the best course might conceivably be to let the market correct itself with little or no help from the System. The language we suggest leaves the door open for any kind of role--major or minor or none at all--that the System may wish to play in the case of disorderly conditions."

Mr. Swan: "We would agree with Mr. Hayes that 'such action as it deems appropriate' is preferable to 'appropriate corrective action.'"

Mr. Clay: "...we favor the inclusion of a phrase, somewhat along the lines suggested by Mr. Irons....." (Note: The suggestion is quoted above.)

"We also agree with....the modification of the statement on disorderly market conditions so as to remove any fixed commitment as to the specific action to be taken...."

Mr. Wayne: "I have one general but minor comment which applies to all three documents. The first time a reference is made to Government securities the words used are 'United States Government securities'. In formal documents of this type it might be well to use the term 'United States Government securities' in all instances."

Paragraph 4

Lines

During Treasury financings, open market operations are conducted in such a manner as to change as little as possible the conditions prevailing in the money markets. Consequently, open market operations are not conducted in (a) maturing issues, (b) when-issued securities, or (c) comparable issues available in the market.

Messrs. Bryan, Irons and Wayne concur in the draft wording. Mr. Bryan would not "weaken in any way the present prohibition against dealings in issues involved in a Treasury financing operation."

Suggestions for revision:

Mr. Ellis: Line 4: Insert "generally" after "operations."

Mr. Swan: Concurs in Mr. Ellis's suggestion.

Mr. Fulton: Line 4: Insert "usually" before "not conducted."
Line 6: Replace with "issues of comparable maturity outstanding in the market."
(Note: Paragraph is numbered 5 in his proposed list.)

Mr. Hayes: Lines 2-3: Replace "the conditions prevailing in the money markets" with "prevailing market conditions."
Line 4: Replace "consequently" with "generally."
Insert after "operations": ", except those involving repurchase agreements,".

Mr. Clay: Line 4: Insert "generally."
Line 6: Replace with "issues available in the market comparable in maturity to the new securities offered."

Supporting arguments:

Mr. Ellis: "This rule, as written, may require exceptions from time to time and this may justify inclusion of a qualification from the outset. Insertion of the word 'generally' after open market operations in line 4 will permit departure from usual practice when necessary. The justification for this is that the Committee should be in a position to consider jointly with the Treasury the market impact of its issues and the aspects of market performance that involve credit policy as well as debt management. The course of action should be determined by the Committee in particular instances rather than freezing its position and requiring the formality of amendment."

Mr. Fulton: "Section 5 (in his list) refers to the 'even keel' policy. I have inserted the word 'usually' before listing the things we will not do, since it may be necessary under certain circumstances, now that we are dealing in other than bills, to operate in maturity ranges comparable to those designated in the new Treasury financing."

Mr. Hayes: "We believe that insertion of the word 'generally' in the second sentence of paragraph 4 of Attachment I, as suggested by Mr. Ellis, would provide a desirable degree of flexibility in the Committee's approach to Treasury financing operations without weakening the principle that such operations must stand the full test of the market. The limitation contained in paragraph (b) of the operating procedures adopted in the past, regarding transactions in issues involved in a Treasury financing operation, has consistently been construed as not applicable to repurchase agreements with respect to such issues. We think that this exception should be explicit in the second sentence of paragraph 4."

Mr. Clay: "...we assume that the intended meaning of item (c) in paragraph 4 would be more correctly reflected in some such wording as...." (Note: Suggestion quoted above.)

Paragraph 5

Open market operations involving concurrent purchases and sales of securities of different maturity for the primary purpose of altering the maturity composition of the System's portfolio are ordinarily not undertaken.

Messrs. Ellis and Wayne concur in the draft wording.

Suggestions for revision:

Mr. Bopp: Would incline to have the Committee retain a free hand to engage in swaps.

Mr. Hayes: Delete whole paragraph.

Mr. Clay: Delete paragraph from standing rules.

Mr. Fulton: Replace paragraph with:

> "The Committee avoids 'swap' transactions with others undertaken off the open market."
>
> (Note: This would be the final sentence of a proposed new paragraph 3, quoted below.)

Mr. Irons: Line 4: Replace with, "portfolio, or for other reasons, are undertaken only upon the authorization of the Committee."

Move paragraph to continuing authority directive.

Mr. Bryan: Concurs in Mr. Irons' suggestions.

Mr. Swan: Eliminate paragraph from standing rules. Possibly include it in continuing authority directive.

Supporting arguments:

Mr. Hayes: "We note that the limitation of paragraph 5 . . . would not apply to transactions which are not for the primary purpose of altering the maturity composition of the System's portfolio. Thus the paragraph would not apply to transactions for the purpose of influencing short-term interest rates (such as those under the special authorization). This distinction, however, may be too sophisticated to convey clear meaning to the general public; we would prefer to see this paragraph deleted from the standing rules. This would not in any way reduce the Committee's control over swap transactions; yet it would avoid tying the Committee's hands. For example, in view of the opinions expressed by several members of the Committee, and by the Manager, that an increase in the proportion of Treasury bills in the System portfolio would be desirable, it would be useful for the Committee to have complete freedom to act if there should be future opportunities to switch some part of the System's large holdings of short-dated coupon securities into Treasury bills."

Mr. Clay: "We also agree...with the deletion of the 'swaps' paragraph from the standing rules."

Mr. Fulton: (See below, "New Paragraphs Suggested by Mr. Fulton.")

Mr. Irons: "This Rule, as stated, applies only to one purpose for which 'swaps' might be undertaken. We believe that your statement of Rule 5 should be broadened by making the last line of the Rule read as follows: (Note: Suggestion quoted above).

"...we would remove your Rule 5 and Rule 6 from the Standing Rules and include the two Rules as stated in the Continuing Authority Directive....This change would shorten the Standing Rules and we believe would place the substance of Rules 5 and 6 in proper position in the Directive to the New York Bank."

Mr. Swan: "We would eliminate the entire item from the Standing Rules since it seems to us to be a matter of procedure....

"While we suggest that item 5....should more appropriately be incorporated in the Continuing Directive, we have some question even here unless 'concurrently' is further defined, since we are in fact in the position of altering the maturity composition of the System's portfolio on occasion, not for its own sake, but in connection with efforts to prevent short-term rates from declining."

Paragraph 6

Repurchase arrangements may be entered into with nonbank dealers from time to time to supply temporary reserve funds to the market. To this end, Government securities having remaining maturities of 15 months or less and prime bankers' acceptances may be purchased from nonbank dealers subject to agreement for their resale within 15 calendar days. The repurchase rate is normally the discount rate at the Federal Reserve Bank of New York, but may be as low as the average issuing rate on the most recent issue of three-months Treasury bills.

Suggestions for revision:

Mr. Bopp: Would combine with draft paragraph 3 of continuing authority directive.

Mr. Deming: Not needed; repurchases should be covered in continuing authority directive.

Mr. Ellis: Move up to follow paragraph 2, or alternatively, move to "standing authorities" (continuing authority?) and publish in Regulation.

Mr. Fulton: Line 1: Replace "arrangements" with "agreements."
Line 2: Delete "from time to time."
Lines 2 and 5: Replace "may be" by "are."

Lines 7-10: Replace last sentence by:

"The repurchase rate is determined on the basis of conditions prevailing in the money markets, but is not less than the average auction rate on the most recent issue of three-month Treasury bills."

Mr. Hayes: Replace paragraph with:

"Repurchase agreements in Government securities and prime bankers' acceptances may be entered into with nonbank dealers from time to time to supply reserves to the market on a temporary basis."

Mr. Clay: Concurs in Mr. Hayes' proposed language.

Mr. Swan: Concurs in Mr. Hayes' proposed language, except for the further deletions of "from time to time" and "to the market."

Mr. Irons: Line 2: Delete "from time to time."
Move paragraph to continuing authority directive.

Mr. Bryan: Concurs in Mr. Irons' suggestions.

Mr. Wayne: Line 3: Insert "United States" before "Government."

Supporting arguments:

Mr. Ellis: "Rule #6 dealing with repurchase agreements concerns the release of reserve funds at a price and, if the first two rules are to be preserved, should be placed as Rule #3 which will associate it with other operations affecting availability and cost of reserve funds. An alternative would be to consider repurchases as part of the standing authorities and together these materials would be carried in an appropriate place in the 'Regulation.'"

Mr. Fulton: "Item 6...is placed in the present tense to conform with the other Standing Rules, and the phrase 'from time to time' in your draft is eliminated to avoid the implication that we engage in repurchase agreements only occasionally.

"The reference to the discount rate at the Federal Reserve Bank of New York as 'normally' the repurchase rate seems to me to be false and misleading, at least over considerable periods of time. I have tinkered with the idea of using the discount rate at New York as the upper limit for the repurchase rate and the bill rate as the lower limit, but that, too, is misleading since the repurchase rate has seldom, if ever, been set above the discount rate. That is, if the Desk tries to set a repurchase rate above the discount rate, the dealers' clearing bank would presumably carry the dealers and obtain the needed reserves at the discount window. I conclude that the best we can do is state that the rate is determined on the basis of conditions prevailing in the market, but that in no case is it below the rate prevailing at the last auction of three-month Treasury bills."

Mr. Hayes: "...we would prefer to see the details on repurchase agreements omitted from the standing rules and left to the proposed continuing authority directive."

Mr. Swan: "eliminate the rest of item 6 (i.e., sentences 2 and 3) since it appears more appropriately in Attachment II."

Paragraph 7

The Federal Reserve Bank of New York is selected as the Federal Reserve Bank to execute transactions in the open market pursuant to directions issued by the Committee from time to time.

Messrs. Bryan, Fulton, Irons, Swan and Wayne concur in the draft wording.

Suggestions for revision:

Mr. Bopp: Lines 3-4: Replace phrase beginning, "directions issued..." with "authorizations and directions issued by the Federal Open Market Committee." Use revised language as new paragraph 1 of continuing authority directive.

Mr. Clay: Delete from standing rules and include elsewhere.

Mr. Deming: Not needed; point can be covered by action at the organization meeting.

Mr. Ellis: Delete from standing rules and include in Rules on Organization and Information and Rules on Procedure.

Mr. Hayes: Delete from standing rules and combine with continuing authority directive.

Paragraph 8

The Committee will meet at least once a month, but other meetings may be held at the call of the Chairman.

Messrs. Fulton, Swan and Wayne concur in the draft wording.

Suggestions for revision:

Mr. Clay: Delete from standing rules and include elsewhere.

Mr. Deming: Not needed; point should be left in Rules on Organization.

Mr. Ellis: Delete from standing rules and include in Rules on Organization and Information and Rules on Procedure.

Mr. Hayes: Delete from standing rules; covered by Rules of Organization and Information and by Committee's By-Laws.

Mr. Irons: Delete from standing rules.

Mr. Bryan: Concurs in Mr. Irons' suggestion.

Supporting arguments for paragraphs 7 and 8:

Mr. Ellis: "Both of these statements seem out of context in relation to the preamble and the content of the other 'rules.' They seem more adapted for presentation in the presently published Rules on Organization and Information and Rules on Procedure. In fact, as mentioned above, Rule #8 seems to modify a parallel statement in the published Rules on Organization."

Mr. Hayes: "We agree with Mr. Ellis that paragraphs 7 and 8 of Attachment I seem out of context in the standing rules, and should be provided for elsewhere. Paragraph 7, for example, might be combined with the continuing authority directive. The subject matter of paragraph 8 is covered by section 2(c) of the Committee's Rules on Organization and Information, and by Section 5 of Article I of the By-Laws."

Mr. Irons: "We would not include in the Standing Rules a statement regarding Committee meetings."

Mr. Swan: "We have included (paragraphs 7 and 8) as written, as we believe they are less appropriate in the standing directive than in the Standing Rules."

New Paragraphs Suggested by Mr. Fulton

3. All transactions in United States government securities, except certain exempt transactions indicated below, are conducted in the open market and at prices and yields prevailing in the market at the time purchases and sales are made. Exempt transactions include exchanges of maturing United States Treasury securities with the United States Treasury incident upon exchange offerings, and transactions with or for the account of foreign central banks. The Committee avoids 'swap' transactions with others undertaken off the open market.

9. These rules may be changed or revoked at any regular or called meeting of the Federal Open Market Committee.

Supporting argument for new paragraph 3:

"Item 3 in the attached draft grows out of an earlier suggestion by Mr. Wayne. In effect, it rules out 'off-the-market swaps', and restricts transactions to purchases and sales in the open market at going market rates. There remains the problem of how to handle exchanges for maturing Treasury obligations and transactions with foreign central banks. Perhaps you can suggest how these exceptions should be phrased."

* * * * * *

III. Procedural issues relating to policy directives

a. Should the Committee's directives to the Account Management be divided into a "continuing authority directive" and a "current policy directive?"

Five presidents expressed and five implied approval of this proposal.

Mr. Deming: "I am in agreement with those who believe that the present directive should be split into two parts...."

Mr. Ellis: "Separation of the continuing authority directive from the current economic directive would be a major step toward improvement of the general framework of our working procedures. It should lead to a better public understanding of Committee actions. It also clears the way for improved expression of the Committee's current economic directive....

"The policy record clearly reveals the two reasons that have moved the Committee to change clause (b)--changes in recognition of different economic conditions and changes to accompany monetary policy moves. The record also shows, however, that because only a single phrase was to be changed, reluctance to signify any change in policy sometimes delayed explicit recognition of changed economic conditions.

"An explicit two-part directive should permit the Committee to recognize the course of economic activity over the cycle. It would also facilitate expression of the Committee's objective in terms of change in the relative degree of ease or restraint. Such an improvement seems possible. As stated in the Broida memorandum, 'If the nature of the consensus can be succinctly summarized in the record it is not clear why it cannot also be reflected in the directive.'"

Mr. Hayes: "We are in accord with the proposal for separating the directive into a continuing authority directive and a current policy directive. This separation, it seems to us, would be preferable from a procedural standpoint."

Mr. Swan: "We believe a separate continuing Directive (Attachment II) is desirable since there are certain items which change so infrequently as to be inappropriate to incorporate each meeting into a current directive, but which should not be in the Standing Rules as they are, for the most part, limitations on operations."

Mr. Wayne: "I prefer dividing the statement of procedures and authorities into three parts: . . . . (B) The second part would be the continuing authority directive to the New York Bank. (C) The third part would be the current policy directive to the New York Bank."

Messrs. Bopp, Bryan, Clay, Fulton and Irons imply approval of this split by confining their comments on the draft proposals to matters of content. On the other hand, Mr. Allen offers a proposed form of a directive which incorporates into one document, of a type to be adopted at each meeting, material which is divided between the continuing and current directives in the drafts distributed.

* * * * *

b. What specific language should be employed in the continuing authority directive?

Messrs. Clay and Irons concur in the draft of this directive, except that each would add material from the draft standing rules, as noted above. Mr. Allen proposes a single directive, the first (unnumbered) paragraph of which includes material of a type included in the draft current economic directive, and the next two paragraphs of which (numbered 1 and 2) correspond approximately to the paragraphs with those numbers in the draft continuing authority directive.

Mr. Ellis offers this comment:

"Here again, I urge consideration of placing these continuing authorities in the 'Regulation' with annual review of all such regulations rather than publication through the Annual Report of portions of the minutes of our March meetings.

"Incidentally, I prefer Mr. Allen's proposed wording to that in Attachment II and believe that the section dealing with repurchase agreements should be included as part of this material."

Mr. Bopp favors a four-section continuing authority directive. He writes:

"If the standing rules and the directive were to be eliminated, a certain number of technical matters would remain. It would seem appropriate that all authorizations and instructions of a continuing nature be incorporated in the equivalent of Attachment II. It might be well for these authorizations to be reviewed annually, probably at the March meeting. With these purposes in mind, I suggest the following changes in Attachment II:

"Section 1 would be similar to No. 7 under Attachment I, namely....(Note: Proposed language is quoted above.)

"Sections 2 and 3 would be similar to the present Sections 1 and 2 of Attachment II; however, in the interest of clarity, I prefer Mr. Allen's wording.

"Section 4 would cover authority to execute repurchase agreements similar to that included in Section 6 under Attachment I and Section 3 under Attachment II. A combined authorization covering repurchase agreements might be stated as follows:" (Note: Proposed language is quoted below.)

Other Presidents make suggestions for specific language changes and modifications of coverage. The paragraphs of the draft are cited below (following the format of Attachment II) with the proposals for change in each and the supporting arguments.

Preamble

During periods between meetings of the Committee, the Federal Open Market Committee, with a view to implementing its current economic policy directive instructs the Federal Reserve Bank of New York:

No suggestions for revision in this language are made. The paragraph is omitted from Mr. Allen's proposal and is not referred to in the proposal Mr. Bopp describes.

Paragraph 1

To make such purchases, sales, or exchanges of Government securities and, as authorized, prime bankers' acceptances (including replacing of Government securities that mature, or allowing such securities to run off without replacement) for the System Open Market Account in the open market or, in the case of maturing securities, by direct exchange with the Treasury, as may be necessary to carry out the Committee's current policy directive. The authority of the Bank to increase or decrease the aggregate amount of Government securities (including forward commitments) held in the System Account, other than such special short-term certificates of indebtedness as may be purchased for the temporary accommodation of the Treasury under the provisions of (2) below, is limited to $1 billion during any period between meetings of the Committee, except as otherwise authorized. Government securities shall be purchased and sold at prices determined in the market and bankers' acceptances at market discount rates.

Messrs. Clay, Deming and Irons concur in the draft wording.

Suggestions for revision:

Mr. Allen: Replace whole paragraph with the following:

"To make (a) such purchases and sales of prime bankers' acceptances and (b) such purchases, sales or exchanges of United States Government securities (including replacement of maturing securities, and allowing maturities to run off without replacement) for the System Open Market Account in the open market or, in the case of maturing securities, by direct exchange with the Treasury, as may appear necessary to effect the aforementioned judgment, provided (a) that the aggregate amount of bankers' acceptances held at any one time by the Federal Reserve Bank of New York shall not exceed $75 million, and provided further that such holdings shall not be more than 10 per cent of the total of bankers' acceptances outstanding as shown in the most recent acceptance survey conducted by the Federal Reserve Bank of New York and (b) that the aggregate amount of securities held in the System Account (including commitments for the purchase or sale of securities for the Account) at the close of this date, other than special short-term certificates of indebtedness purchased from time to time for the temporary accommodation of the Treasury, shall not be increased or decreased by more than $1 billion;".

Messrs. Bopp and Ellis: Concur in Mr. Allen's proposal.

Mr. Fulton: Replace whole paragraph with the following:

"To engage in open market operations in United States government securities and, as authorized, in prime bankers' acceptances, as provided in Sections 2 and 3 of the Standing Rules Governing Open Market Practices of the Federal Open Market Committee. The authority of the Bank to increase or decrease the aggregate amount of United States government securities held in the System Open Market Account (including forward commitments), other than special short-term United States government certificates of indebtedness identified in Section 2 below, is limited to $1 billion during any period between meetings of the Committee, except as otherwise authorized."

Mr. Swan: Line 2: Omit "as authorized."
Line 3: Omit "of"
Lines 18-21: Omit final sentence.
Line 21: Insert: "Holdings of bankers' acceptances are not to exceed $75 million, or 10 per cent of total bankers' acceptances outstanding."

Mr. Wayne: Lines 1-10: Replace first sentence with the following:

"To buy, sell, or exchange United States Government securities and, as authorized, prime bankers' acceptances in the open market for the System Open Market Account to the extent necessary to carry out the Committee's current policy directive. This includes replacing United States Government securities which mature by direct exchange with the Treasury or allowing such securities to run off without replacement."

Lines 18-21: Replace last sentence with the following:

"United States Government securities and bankers' acceptances shall be purchased and sold at prices prevailing in the market at the time purchases and sales are made."

Mr. Hayes: Concurs in Mr. Wayne's proposal, with these modifications:

Replace "and, as authorized, prime bankers' acceptances" with "and of prime bankers' acceptances in amounts as authorized,".

Make clear that transactions in bankers' acceptances are for the account of the New York Bank.

Supporting arguments:

Mr. Allen: "It will be noted that the suggested directive Exhibit A, does not restrict the maturities of United States Government securities which the Federal Reserve Bank of New York would be authorized to buy and sell. Thus it would eliminate the need for the special authorization which a Committee majority has approved at each meeting since February.

"It will be noted also that I have included in the suggested directive authorization for the Federal Reserve Bank of New York to buy and sell bankers' acceptances. The inclusion of such authority in the directive seems more appropriate than the current annual authorization, for the reason that we presumably operate in acceptances as a part of open market operations authorized by Section 14 of the Federal Reserve Act."

Mr. Fulton: "(a) The preamble states that the Federal Reserve Bank of New York is to conduct open market operations with a view to implementing the Committee's 'Current Economic Policy Directive'. It, therefore, seems unnecessary to repeat this proviso in subsequent sections of the directive, and accordingly this has been omitted.

"(b) The attached draft of Section 1 of the Continuing Authority Directive attempts to simplify the phraseology by referring back to the appropriate Standing Rules. If we can agree upon those, there seems to be no good reason to repeat them here."

Mr. Swan: "While we do not feel strongly about this, we question whether this sentence (that is, the last sentence of the draft paragraph 1) is necessary in view of item 3 of the Standing Rules. In any case, it is on a somewhat different level than is the rest of the material in the Continuing Directive."

(With respect to the proposed added sentence on the dollar limit for bankers' acceptances:) "This limitation it seems should be in this directive along with other dollar limitations prescribed."

Mr. Wayne: "The first two sentences of this section seem unnecessarily complex and obscure, while the last sentence appears to be vague and ambiguous. I prefer the following statement of the paragraph (Note: the statement is quoted above) which, to me, seems clearer and more direct without changing the substance:"

Mr. Hayes: "...we have some preference for Mr. Wayne's rewording of paragraph 1...except that it should be made clear that transactions in bankers' acceptances are conducted for the account of the Federal Reserve Bank of New York. We would suggest..." (the language change noted above.)

Paragraph 2

Line

To purchase directly from the Treasury for the account of the Federal Reserve Bank of New York (with discretion, in cases where it seems desirable, to issue participations to one or more Federal Reserve Banks) such amounts of special short-term certificates of indebtedness as may be necessary from time to time for the temporary accommodation of the Treasury; provided that the total amount of such certificates held at any one time by the Federal Reserve Banks shall not exceed in the aggregate $500 million, except as otherwise authorized.

Messrs. Clay, Deming, Hayes, Irons, Swan and Wayne concur in the draft wording.

Suggestions for revision:

Mr. Allen: Line 10: Delete "except as otherwise authorized."

Mr. Fulton: Line 1: Replace "purchase" with "acquire."

Paragraph 3

To supply reserves to the money market on a temporary basis, when consistent with the current policy directive, by purchasing for the account of the Federal Reserve Bank of New York from nonbank dealers Government securities having a remaining maturity of 15 months or less or prime bankers' acceptances, under resale agreements maturing in up to 15 calendar days. The rate on such agreements will normally be the discount rate of the Federal Reserve Bank of New York, but in no event shall it be a rate below (1) this discount rate or (2) the average issuing rate on the most recent issue of three-month Treasury bills, whichever is the lower.

Messrs. Clay, Deming, Swan concur in the draft wording. Mr. Bryan would not remove the present 15-month maturity limitation on securities held under repurchase agreements.

Suggestions for revision:

Mr. Allen: Delete the paragraph.

Mr. Bopp: Replace paragraph with the following:

"Repurchase arrangements in Government securities and prime bankers' acceptances may be entered into with nonbank dealers in order to help carry out the Committee's policy directive. Purchases made under this authorization shall be (a) limited to Government securities and bankers' acceptances having remaining maturities of X months or less, and (b) under resale agreements maturing in up to 15 calendar days. The rate on such agreements will normally be the discount rate of the Federal Reserve Bank of New York, but in no event shall the rate be below this discount rate or the average issuing rate on the most recent issue of 3-month Treasury bills, whichever is the lower."

Mr. Fulton: Line 2: Insert "Committee's" before "current," and "economic" after "current."
Line 4: Insert "United States" after "dealers."
Line 7: Replace period with comma
Lines 8-14: Replace with the following:

"subject to the restrictions set forth in Section 6 of the Standing Rules Governing Open Market Practices of the Federal Open Market Committee."

Mr. Hayes: Lines 5-6: Remove reference to maturity or increase limit to 24 months.

Mr. Wayne: Line 5: Insert "United States" before "Government."

Note: Mr. Irons' and Mr. Ellis's suggestion that paragraph 6 of the standing rules be moved to the continuing authority directive might imply some modification of the draft of this paragraph.

Supporting arguments:

Mr. Allen: "...I have not included in the suggested directive authority for repurchase agreements in bankers' acceptances and securities; these could continue subject to annual authorization."

Mr. Fulton: "In your version of Section 3, Attachment II, certain restrictions are placed on the determination of the repurchase rate that differ from Rule 6 of the Standing Rules as stated in Attachment I. The revised draft simply refers back to the appropriate section of the Standing Rules."

Mr. Hayes: ". . . we would suggest that the limitation on repurchase agreements to securities maturing in 15 months be broadened by removing reference to maturity or at least by increasing the maturity limit to 24 months. While repurchase agreements under almost any set of circumstances would be limited to short-term securities, the 15-month dividing line is perhaps too narrow."

Possible additional paragraphs

Additional paragraphs or other language revisions for the continuing authority directive are implied by the suggestions, noted earlier, for moving certain material from the standing rules. These are Mr. Irons' suggestion to include in the continuing authority directive the draft paragraph on "swaps," a suggestion also made by Mr. Swan but with some questions, as noted; Mr. Hayes' suggestion to include here the substance of paragraph 7 of the draft rules; and, perhaps, Mr. Clay's suggestion to include "elsewhere" paragraphs 7 and 8 of the draft rules.

* * * * * * *

c. Should a "statement of general policy position" be regularly prepared as a supplement to the current policy directive?

Mr. Hayes recommends supplementing the directive with a "Statement of General Policy Position," a proposal to which Mr. Deming sees no objection. Mr. Allen also proposes supplementary language.

Mr. Hayes: "While we thus favor the elimination of clause (b) as used in the existing directive, we believe that it would be desirable for the Committee to formulate and to vote upon a statement of policy broader and more general in scope than the instruction to the New York Bank as to the relative degree of ease or tightness which we believe should constitute the directive. We thus suggest that the Committee experiment with a procedure similar to that suggested by Mr. Irons in his letter to you of February 28, 1961. Under our proposal, the Secretary of the Committee and the Manager of the Account would draft, immediately after each meeting, a statement of the general economic policy position of the Committee as it developed out of the discussion. This statement, which would be as brief as is consistent with accuracy and clarity, would be reviewed by the Chairman (or by whoever may have presided in his absence) and then distributed that same day to each member of the Committee (by wire in the case of the Reserve Bank Presidents). The Committee members could then, within a day or two, indicate their approval of the statement, offer suggested changes, or register dissents. A statement of the Committee's policy position would appear, along with the current policy directive, in the policy record for each meeting. We envision that a draft of the policy record would be prepared and circulated at the same time as the draft of the minutes. The Committee would thus have before it a few days after each meeting a draft of the minutes and a draft of the policy record entry, with the latter containing not only the current policy directive but also the general statement of policy position revised in accordance with suggestions made by members on the initial draft of the statement which would have been dispatched (by wire in the case of the Presidents) on the afternoon of the meeting. At the following meeting the Committee, having reviewed and commented upon the above material, would formally vote on the general statement of policy position and would approve the minutes. Any dissents or supplemental statements a member may wish to record with respect to the statement of policy position could readily be presented in the subsequent text of the policy record. The entire procedure outlined above, it should be added, could be explained in the general introduction to the policy record for each year.

"The general policy statement we have in mind might at times be as short as a single sentence. More often it would take three or four sentences to express the main points integral to current policy. We believe that a statement of this kind would provide a much more flexible format than clause (b) has been for communicating to the Congress and the public a summary statement of what policy is and how it has developed. As an example of what we have in mind, we include as Enclosure B a re-write of how the first part of the policy record entries for the meetings of June 6 and June 20 might have looked had our proposal then been in effect."

His enclosure B consists of the two illustrative directives, quoted later, plus the following illustrative policy statements:

"Statement of General Policy Position

(for the meeting of June 6, 1961)

"It is the policy of the Committee to encourage further expansion in bank credit and the money supply as a means of giving additional stimulus to the economic recovery which is clearly underway but which is not fully assured. This policy recognizes that despite the gains in activity that already have been achieved since the recession low, there remains a large volume of unused labor and other resources and there is no evidence of upward pressure on prices. At the same time, the Committee recognizes that in view of the persisting problem of the balance of payments, it is necessary to continue to pay close attention to international financial developments."

(for the meeting of June 20, 1961)

"It is the policy of the Committee to stimulate the developing, but incomplete, business recovery through the encouragement of further expansion in bank credit and the money supply. The Committee believes that further expansion in current levels of liquidity is desirable in view of the persistence of a large volume of unemployment and excess capacity, and that in view of these unused resources and the related absence of upward pressure on prices, such expansion poses no present inflationary danger. At the same time, the Committee recognizes the importance of giving continued attention to the balance of payments problem of the United States."

These illustrative statements are accompanied by the note:

"To be followed by the usual summary review of economic and financial developments."

Exhibit B attached to Mr. Allen's letter is an illustrative policy record for the meeting of September 12, 1961. It consists of the illustrative directive (including the numbered paragraphs quoted above) followed by these three paragraphs:

"In determining that it would be appropriate for essentially the same degree of ease in the money and credit markets which had prevailed since the last meeting of the Committee to continue for a further period, the Committee was influenced primarily by the state of the domestic economy, the Treasury's financing program, and the international situation.

"The over-all expansion in economic activity had continued, but without acceleration, and there was as yet no evidence that consumer spending or expressed intentions to spend would dramatically increase. Unemployment remained at 6.9 per cent of the labor force. Business loans, which normally increase in August and early September, had thus far risen in no more than seasonal proportions. Note was taken of the increased liquidity in various sectors of the economy, financial institutions in particular, and of the need to be alert to market developments on the expansionary side which, if they developed, might require prompt re-evaluation of monetary policy.

"The Treasury's financing program, which called for the raising of $5 billion in cash between the date of the meeting and mid-October, and the serious state of international problems, were also factors in the Committee's decision that no change in the existing degree of monetary and credit ease was in order pending further developments."

Mr. Deming: "Should this form be adopted (that is, a simple directive along the lines of Mr. Allen's suggestion, without use of quantitative guides) I would see no objection to having a 'general policy position' stated and voted upon also, as outlined by Mr. Hayes. As a matter of fact, the 'general policy positions' might be used for the complete policy record in the Annual Report, if a published explanation of policy, as noted below, were to be done....

"This (that is, avoidance of quantitative guides in the directive) does not mean that the policy explanation need avoid using these (and other) indicators. In fact, I think that the policy explanation should use such indicators but should put them in better perspective and should make clear that no one indicator (or several) can serve as an absolute guide to or explanation for policy at all times. The essence of my argument is that a full, authoritative, current and readable policy explanation would go a long way in dispelling the kind of criticisms now being made of the directives and the policy record. Mr. Swan makes this same point in his letter and I agree with him almost completely."

* * * * *

d. What procedures should the Committee establish for the preparation of its current policy directives?

Messrs. Ellis, Wayne and Fulton suggest having alternative possible policy directives prepared in advance of the meeting, whereas Messrs. Irons, Bryan, Deming and Hayes recommend preparation of a draft directive after the meeting, subject to the approval of the full Committee.

Mr. Ellis: "At the present time, when it appears to the Chairman at the outset of a meeting that it might be appropriate to consider some change in the language of the directive, he has suggested phraseology that has been referred to him by the Secretary. This has proved to be an advantage to those who wish to discuss changes in language during the go-around. It seems possible that this technique might be elaborated to the Committee's advantage.

"Thus the Committee may wish to consider the advisability of inviting the Secretary, perhaps in collaboration with the Manager, to prepare in advance of the meeting a suggested statement of the main directive and one or two alternatives of the second part of the economic directive. These statements could be mailed to the members of the Committee in time to reach their offices on the Friday preceding the meetings. They could serve as a basis for discussion within staff groups in the various banks in their preparation for the meeting.

"One advantage of this approach is that each participant in the meeting would have before him a suggested wording of the directive upon which he could base his comments. He could seek either to make it more specific or less specific. He could suggest modification of relevant magnitudes cited in the directive. This approach could provide a focus for discussion which would add definiteness to the consensus at the termination of the meeting. It would leave with the Committee the responsibility for determining the directive.

"It seems that no more than three alternative wordings would be sufficient to cover the range of views that the Committee might wish to express at various times. By having the alternatives carefully worded in advance, the Committee would not be forfeiting its right to decide the course of policy, but would have before it some materials which would sharpen debate."

Mr. Wayne: "To facilitate action by the Committee in deciding on a directive, it might be well to have the staff submit draft copies of several versions of possible current policy directives along with its memorandum on economic conditions and which would be consistent with the analysis in that memorandum."

Mr. Fulton: "In general, I like Mr. Wayne's suggestion that the staff submit draft copies of several versions of the current directive along with its economic report for consideration by the Committee. If the Committee is to give more complete directions to the Federal Reserve Bank of New York, which I favor, the Board staff will necessarily play a more important role."

Mr. Irons: "Such a directive (that is, of the type he proposes) would be written following the Open Market Committee meetings by the Secretary of the Committee and the Manager of the Account. These officials would be guided by their observations as to what had been said in the meeting, together with a summarization of the consensus as presented orally at the meeting by the Chairman. Such a written directive could be approved the afternoon of the meeting by the Chairman of the Committee and forwarded to the members."

Mr. Bryan: "Let me ... indicate general agreement with Mr. Irons' suggestion that the directive be written after each meeting by the Secretary of the Committee and the Manager of the Account, and after approval or amendment by the Chairman, forwarded to the members of the Committee. I believe there is nothing more futile than nineteen men trying to edit a directive around a table at a meeting. Incidentally, if we ever attain clear, quantitative directions to the Desk, the present hairsplitting shifts of linguistic emphasis in the directive will be reduced to a lesser and more proper importance, and we shall have a better guide to when a change of language is called for."

Mr. Deming: "I do not favor the suggestion that two or three alternative directives be prepared by staff prior to a Committee meeting. I do favor Mr. Irons' suggestion that the secretary and manager be charged with drawing up the formal directive, and, if it is to be used, the 'general policy position', after the meeting. I should think this work could be done quickly and probably could be made available on the afternoon of a meeting. In fact, it should not be too difficult to arrange affairs so that the Committee reconvened briefly after lunch to pass formally on the statement or statements at the time. It seems clear that a formal vote should be taken on the directive, and perhaps on the policy position, and I think this could be done more easily and efficiently at a meeting than by mail."

Mr. Hayes' comment is made in conjunction with his recommendation for material to supplement the directive, and is quoted above.

* * * * *

IV. Form of the current policy directive.

Attachment III to Mr. Young's September 6 memorandum, on the current policy directive, was headed "Alternative Suggestions as to Formulation," and carried the note: "Other suggestions will, of course, occur to members of the Committee." No Presidents express a preference for Alternatives A or B of Attachment III. Messrs. Fulton and Wayne lean toward Alternative C, Messrs. Bryan, Clay and Ellis toward Alternative D, and Mr. Swan prefers "some combination" of C and D. Messrs. Allen, Bopp, Hayes, Irons and Swan offer suggested forms other than those included in the draft, with Mr. Deming concurring in Mr. Allen's suggestion. These proposals are cited below following quotation of the comments made on this issue.

Mr. Allen: "In an effort to suggest procedures which might meet with the approval of a majority of the Committee I enclose two exhibits, both based on the Committee meeting held September 12, 1961. Exhibit A is a suggested directive to the Federal Reserve Bank of New York which I believe could have been issued at the conclusion of that meeting....

"Let me repeat that I have prepared the enclosures in an effort, among other things, to meet what I construe to be the present attitude and conviction of a majority of the Committee, and at the same time to offer forms of directive and policy record which would be understandable to the layman."

Mr. Bopp: "The record of policy actions, in addition to meeting the statutory requirements, affords the best opportunity for informing the public about the Committee's policies and the conduct of open market operations. The record of each meeting should give a clear, concise analysis of business and financial developments considered in reaching a policy decision. In case of significant differences of opinion as to policy, the differing views should be explained briefly.

"Instead of a 'directive' to the Manager of the Account, I suggest that the record give a concise statement of the consensus agreed upon at each meeting. The consensus should include a brief appraisal of the economic situation together with the Committee's intention as to policy for the interval before the next meeting, similar to alternative (c) under Attachment III. Using alternative (c) as an illustration, the consensus might be stated as follows: (Note: Suggested language is quoted below). To meet the requirement of a recorded vote and to afford an opportunity for recording dissenting views, a vote could be taken on policy as stated in the consensus.

"This method of handling the consensus and the recorded vote would avoid the danger of leaving the reader of the Annual Report with the impression that such a brief published directive covers the Committee's instructions to the Manager of the Account. The discussions and the minutes of the meetings serve as a much better 'directive' than one or two sentences which necessarily must be in very general terms."

Mr. Clay: "As to the form and content of Attachment III -- the Current Economic Directive -- several considerations are involved. Some of the ambiguity in past directives probably arose from a lack of agreement among the Committee members, and efforts to be completely explicit may make it more difficult to arrive at a consensus. But a lack of specific directions shifts the responsibility of interpretation to the Trading Desk and may subject the Desk to criticism which it should not bear. Attempts to be specific also are hampered by the fact that individual members of the Committee differ in the measures through which they express their choices -- using free reserves, interest rates, credit expansion, and other terms that cannot be interchanged.

"Despite these difficulties, the Committee should strive to develop methods of expressing their objectives in as unequivocal a form as possible. More progress toward this end would be made if further directives followed the general pattern of Alternative D in Attachment III. The type of detail that could be incorporated in the subordinate directive would have to be learned by experimentation over time and indeed might vary from time to time according to the circumstances prevailing. By reason of the unforeseeable developments that repeatedly occur, the details of the subordinate directive would need to be viewed as targets for the manager to pursue rather than as inflexible goals."

Mr. Deming: "My comments with respect to the form of the current economic directive should be taken against the background of the following points:

"(a) I agree with Mr. Broida that the problem is not one of communicating instructions to the Desk, but of communicating to the public, and that the form and content of the directive and the policy record should be aimed at this end.

"(b) I do not agree that the language or the form of the (b) clause, as used at present, is as meaningless or as absurd as some critics contend. I have given apparently well received and understood talks on Federal Reserve policy using the (b) clauses as a framework on which to hang discussion of policy. It is true, of course, that the clauses were given more meaning by being explained against the background of economic and financial developments and credit policy actions than if they had been presented standing alone, but the significant point to me has been that no one has raised questions about language. Until the recent comments on the Open Market policy record appeared I had heard no adverse comment on (b) clause wording outside the Committee (or the System) itself.

"(c) The above should not be taken to mean that I think the current economic directive is perfect. Of course, I think its language can be improved. I believe, however, that the key to better understanding lies in more full explanation of policy, either in the policy record or in special articles, or both, rather than in the directive.

"My feeling then is that the directive should be simple, general, and brief. I rather like the form suggested by Mr. Allen. That form would imply more frequent changes in directive than have occurred in the past, but I see no objection to that. I think it would offer the advantage of presenting a somewhat more definitive policy on which to vote than does the present form....

"What I particularly want to avoid is a directive couched in terms of a guide or guides such as free reserves, money supply, total reserves, federal fund or bill rates, or the like. I simply do not believe that any one indicator is going to be good enough to use all of the time and I fear that should we attempt to use one (or more) in the directive itself, we will spend a great deal of time subsequently trying to explain why we did not get quite the precise results that these apparently precise indicators would imply we sought. I also feel that an attempt to write directives in specifics would push us uncomfortably close to mechanistic policy-making."

Mr. Ellis: "The four alternatives presented ... all have one thing in common. Each one has a phrase, sentence or paragraph describing the economic situation, followed by a statement of the direction policy is to take. Whichever alternative is accepted will be a constructive move. However, alternative 'D' offers the best opportunity to improve on the clarity of instructions to the Account Manager. Unless the consensus can be stated more explicitly, 'The entire burden of determining how much and what reflects more ease or more restraint is placed on the Manager,' as stated by Karl Bopp in his March 1st memorandum."

Mr. Fulton: "Of the four, I rather like Alternative C, since it is short, flexible, and easily understood, without going into quantitative detail. I would, however, add a sentence about bill rates or the maturity preferences of the Committee, although somewhat more general in nature than that contained in Alternative D. For example, at the last meeting, the Committee might have expressed a preference for a bill rate somewhat higher than the average level prevailing since the last meeting of the Committee. Since we are providing reserves on balance during the current period, this would imply a maturity preference, namely, that open market operations be conducted in other than bills, to the extent possible.

"I am hesitant about stating precise targets for free reserves, the level of bill rates, etc., in the Economic Policy Directive. We talk about these targets freely among ourselves, which is all to the good, since we know the limitations of these figures and mentally attach ranges of error to them. On the other hand, we might be leaving ourselves open to criticism by those who may not understand the fragile nature of our targets and estimating procedures if quantitative goals were compared, upon publication, with the results actually achieved. For this reason, among others, I prefer Alternative C to Alternative D, since the former states the directive in general qualitative terms ('about the same degree of ease as obtained since the last meeting,' 'slightly easier,' and so on). The same would apply to statements about the bill rate ('about the same,' 'slightly higher,' etc.). Also, this form of directive gives the Account Manager more room to maneuver on a day-to-day basis towards the common objective."

Mr. Hayes: "As far as the current policy directive is concerned, we believe that it should contain the instruction that is most useful to the New York Bank in the day-to-day conduct of operations--the instruction as to the relative degree of ease or tightness that the Committee wishes to have maintained in the market during the period until the next meeting. We note that Mr. Allen's suggested directive consists of this kind of instruction. At the same time, we believe that the Committee should not seek to include in the directive a statement as broad and as tightly compressed as clause (b) of the existing directive. Clause (b) has typically consisted of a statement so general in scope and so abbreviated in form that, as Messrs. Broida and Knipe have demonstrated, the Committee has had difficulty in making the statement an effective vehicle for conveying to the public a record of changes in policy over time. This difficulty was also pointed up recently by the criticism of the Record of Policy Actions for 1960 made by the Joint Economic Committee and its staff."

Mr. Irons: "We believe that if a change is made from the present type clause (b) directive and statement, an attempt should be made to spell out a current economic directive in some detail to the Manager of the Account. We continue to believe that a directive of the type included in our memorandum of February 28, 1961 may have possibilities ... I am not sure how much improvement we can effect in making our directive concise, nor am I confident of being able to reduce a directive to some sort of precise formula. If there is to be any change, I lean to the side of appreciably more detail rather than less."

Mr. Bryan: "Turning to the current economic directive, I again find myself in complete agreement with Mr. Irons' view that an attempt should be made to spell out such a directive in more detail. Of the four alternative formulations found in Attachment III, I like best of all alternative 'D.' It is the only formulation, among the four illustrations, containing quantitative instructions.

"As I see it, the need for stating instructions in quantitative terms, within a range of latitude suitable to the practical administration of the Account is now, and has been for a long time, one of the most important problems confronting the Committee. I regard the successful solution of this problem as imperative; I believe that, unless the problem is successfully resolved, the survival of the Committee in its present form, and with its present power, is gravely and needlessly endangered.

"It is clear that the relationship of the Agent Bank and of the Manager to the Committee is a fiduciary relationship, and it is subject to the general canons governing a fiduciary and his principal.

Among the responsibilities of a principal in such a situation is not only that of making his instructions to his agent reasonably clear, but also that of giving instructions within the limit of the means available to the agent. If the instructions are not clear, or if they lie beyond the means at the agent's disposal, then the agent has an adequate defense against misadventure, all to the discomfiture of the principal. The agent, quite aside from the requirement that he faithfully discharge his fiduciary responsibilities, has an even greater responsibility: the responsibility of being able to demonstrate that he has done so, and this responsibility is the more demanding in a public trust than in a private trust. Implicit in this is the responsibility, discharged every day in private fiduciary relationships, of refusing instructions that are excessively vague, meaningless, or beyond the means at the disposal of the fiduciary.

"I thus believe that the Committee, as principal, owes it to itself and to its Agent Bank and Manager to make its instructions not only clear but also within the means disposed by the Bank and the Manager. I also believe the Agent Bank and the Manager have the responsibility--inadequately realized, I think--to accept no instructions that are unnecessarily vague, meaningless, or beyond the means disposed by the Bank and the Manager.

"The Committee, I strongly feel, has tended to avoid clear, quantitative instructions because it has failed to draw a distinction between means and ends. Although most of the things that we wish ultimately to influence, our ultimate purposes or ends, can be stated in quantitative terms, many of them cannot be so stated. Even when they can be stated in quantitative terms, the combinations and permutations of such items as price levels, employment, interest rates, and so on through a long list, are so many as to make an instruction, weighing all items, impossible. More than that, many of our purposes or ends are qualitative, not quantitative: ease, tightness, and so on through a long list, which I spare you. These things, despite an element of reality, defy adequate and meaningful definition, and they are unreasonably vague, sometimes meaningless, and not always proportionately responsive to the means governed by the Committee and at the disposal of the Agent Bank and Manager.

"What the Committee has failed to remember is that the Committee has control over but one means, whatever its ultimate purposes; that is, it controls bank reserves. Unless it gives its instructions in terms of a quantitative reserve concept, from time to time modifying the instructions in accordance with its view of the attainment or nonattainment of the final purposes or ends it has in mind, then in my judgment the Committee cannot decently hold the Agent Bank and the Manager responsible for the fulfillment or non-fulfillment of the Committee's instructions. What is equally important, the Agent Bank and the Manager, while they may have an adequate defense in the ineptitude of the instructions given by the Committee, are deprived of the positive proof to the Committee and the Congress, when such instructions are given in vague and qualitative terms, that they have followed the Committee's intent. This will ultimately be a disaster, I feel sure.

"I lay the chief responsibility for this situation on the Committee, where the authority and power vests, but I believe some responsibility lies with the Agent Bank and, to a much lesser extent, with the Manager. They should have the keenest awareness of the canons of fiduciary responsibility; they should give the Committee the greatest aid and assistance in developing a basis for clear, quantitative instructions within the means that are disposed by the open market operation; they should cease their eternal yowling for greater discretion.

"As I have said, I regard this matter of quantitative instructions, and a clear distinction between means and purposes or ends, as imperative. Unless we solve it, we shall one day be confronted with an explanation to the Congress of what we intended, all without being able to say what we did in fact intend; the Agent Bank and the Manager, after our retreat into vague generality, will one day be confronted with the task of explaining whether it fulfilled as the fiduciary the wishes of the Committee, without being able to explain."

Mr. Swan: "Turning to the current directive (Attachment III), we would strongly prefer some combination of alternatives 'C' and 'D'. For example, to the first sentence of 'C' we would add a sentence as shown in our Attachment III relating to the comparative degree of ease or tightness, and would then go on to specify what particular quantitative variables appear to fit. These variables would not, of course, necessarily remain the same from one meeting to the next. Despite their limitations, however, free reserves have been more generally mentioned as a quantitative policy guide than have any other one measure.

"Similarly, in view of the concern over international flows of funds, the 91-day bill rate has received much attention in recent months.

"There are, of course, other important quantitative variables, such as the Federal funds rate, the rate of growth of the money supply, required and nonborrowed reserves, and the level of member bank borrowings. However, we would prefer to avoid trying to specify too many quantitative guides, especially in view of our imperfect knowledge of how they are related.

"Nevertheless, we believe it would ordinarily be desirable to specify at least two quantities in the directive so as to give explicit recognition to reference points which are to some degree now available to the Manager in the consensus."

Mr. Wayne: "I strongly favor abandoning the present system with its cumbersome and ambiguous clause (b)....

"I favor a current policy directive which is short and clear and with a format allowing a brief statement of the reasons underlying the directive. Perhaps alternative 'C' ... would meet these requirements."

The newly suggested forms for directives are as follows:

Mr. Allen:

(Illustration for meeting of September 12, 1961)

"It is the Committee's judgment that essentially the same degree of ease which has prevailed in the money and credit markets since the last meeting of the Committee should continue until the next meeting or until the Committee determines otherwise, and the Committee directs the Federal Reserve Bank of New York until otherwise directed by the Committee:" (This is followed by paragraphs 1 and 2, quoted earlier.)

Mr. Bopp: "In view of the fact that there is still substantial unemployment and under-utilization of resources, it was the consensus of the Committee that open market operations should be directed toward maintaining about the same degree of ease."

Mr. Hayes:

(Illustration for meeting of June 6, 1961)

"Until the Committee otherwise directs, operations should be designed to maintain approximately the same degree of ease as has prevailed recently, resolving any doubts on the side of further ease and clearly avoiding any lessening of the availability of reserves."

(Illustration for meeting of June 20, 1961)

"Until the Committee otherwise directs, operations should be designed to maintain substantially the same degree of ease in the market as has prevailed recently, with the understanding that any doubts arising in the operation of the System Open Market Account would continue to be resolved on the side of ease."

Mr. Irons:

(Excerpted, together with an explanatory note, from his letter of February 28, 1961, to which he refers in his recent letter quoted above.)

"Policy Directive

"(Note: As is explained in the accompanying letter, the substitute policy directive set forth below attempts to establish a more logical form for the directive, while at the same time preserving the basic form of earlier policy directives. Thus Clause (a) sets forth what might be viewed as the basic objectives of monetary and credit policy, regardless of the phase of the business cycle. Clause (b) sets forth the current translation of the long-run objectives in terms of the existing economic situation; that is, the current phase of the business cycle (an economic recession) is reflected in the statement. It is contemplated that Clause (a) would seldom, if ever, be changed, but that Clause (b) would be changed several times throughout a business cycle. Clause (b) would be followed by a fairly specific 'instruction' to the New York Bank, which would be designed to translate the broader policy objective in Clause (b) into specific terms for guidance of the Account. The final paragraph would contain any special authorizations for the succeeding period until the next meeting of the Committee. In this example, the special authorization to deal in securities of more than 15 months maturity is included.)

"The Federal Open Market Committee directs the Federal Reserve Bank of New York to make such purchases, sales, or exchanges of securities, as authorized in the operating policies and standing directives of the Committee adopted on March ____, 1961, as may be necessary with a view:

"(a) to relating the supply of funds in the market to the needs of commerce and business in order to promote the highest sustainable rate of economic growth, continuity of employment opportunities, and reasonable stability in price levels, and

"(b) to encouraging monetary expansion for the purpose of fostering recovery in economic activity and employment, while taking into consideration current and prospective international developments.

"In furthering these objectives, the Federal Reserve Bank of New York is instructed, until the next meeting of the Committee, to maintain approximately the same degree of ease in the money market as has prevailed since the last meeting of the Committee, as reflected in the availability of bank reserves, short-term interest rates, and the general tone and feel of the market. Such degree of ease would in general be reflected in net free reserves averaging approximately $400 to $500 million; member bank borrowing from Reserve Banks in the range of $50 to $150 million; rates on 3-month Treasury bills fluctuating between 2.40 and 2.60 per cent; and a

Federal funds rate ranging between 2 per cent and the existing discount rate. These instructions contemplate that the Federal Reserve Bank of New York will assume sufficient leeway to meet day-to-day situations of unanticipated tightness or ease, when necessary, as reflected by the tone and the feel of the market.

"During the period until the next meeting of the Committee, the Federal Reserve Bank of New York is authorized to purchase, sell, or exchange for securities of more than 15 months maturity, and up to 10 years maturity, in effectuating the goals of monetary and credit policy; provided that the net amount of purchases, sales, or exchanges for such securities is not to exceed $500 million."

Mr. Swan: "In view of the fact that there is still substantial underutilization of resources, despite the healthy upward movement of the economy, the Committee directs that open market operations be undertaken to encourage bank credit expansion. Over the next three weeks, operations should be designed to maintain a degree of ease about the same as that prevailing since the last meeting. This implies a range of $500 to $550 million of free reserves and a money market condition producing a 91-day bill rate of between 2.25 and 2.50 per cent."

* * * * * * *

V. Frequency and lag of publication of the Policy Record

Messrs. Wayne, Fulton and Bopp favor quarterly publication of the Policy Record, with a lag of one quarter, but Mr. Swan takes a contrary view. Their comments, and Mr. Deming's, are as follows:

Mr. Wayne: "I have two suggestions concerning reports on policy actions.

"(1) The draft of the policy record should be written by staff members as soon as feasible after the close of the period. This should be a succinct and clear statement of the reasons for adoption of the directive and, in line with President Allen's suggestion, might well include the directive, either verbatim or in substance. The Committee should then approve the draft, with such modifications as it prefers, so that it could be entered into the policy record.

"(2) I favor publication of the policy record each quarter, with a lag of one quarter. There are several possibilities for publication but I would favor a quarterly paper in the Federal Reserve Bulletin. This would be a comprehensive and authoritative but compact summary of national monetary and credit developments, into which would be woven the account of the policy changes. If this method should be chosen, every effort should be made to maintain the highest possible level of competence and lucidity in the preparation of this paper. The staff member charged with preparing it should maintain a running account during the quarter to be covered. Shortly after the end of the quarter he should put it into shape for a thorough review and appraisal by all members of the Committee and all presidents of Federal Reserve Banks who are not members.

"I see no valid reason for the present long delay in publishing parts of the policy record. Publication along the lines described above would not only end one of the persistent and potent criticisms of the System but would also provide all parties with a useful and authoritative account of monetary and credit developments as well as a rational account of policy action while it is still pertinent, yet not current to the extent that it might defeat the purposes of the Committee."

Mr. Fulton: "As for publication, I favor the suggestions of Messrs. Wayne and Allen that a description of the policy record be written by a staff member promptly after each meeting, and that this be submitted to the Committee for amendment and approval, and then entered into the policy record. These statements could then be brought together at the end of each quarter, reviewed by the Committee, and published in the Federal Reserve Bulletin with a lag of one quarter."

Mr. Bopp: "The suggestion that the record of policy actions be prepared and sent to members of the Committee for their consideration and suggestions as promptly as possible after each meeting is a good one. As a means of keeping the public as well informed as feasible, I also favor publishing the record of policy actions quarterly with a lag of one quarter instead of annually."

Mr. Swan: "Finally, turning to the question of public understanding of Federal Open Market Committee determinations, we do not believe this can be accomplished through publication on a quarterly basis of the policy record including a more detailed directive, and such publication would in all probability encourage more frequent Congressional inquiry.

"We still believe, as we indicated earlier, that what is needed is a separate publication of System policy positions and accomplishments (and failures). This should involve a more explicit review of both policy decisions and of the changes in the economy which occurred either in response to, or in spite of, such decisions than could or should be provided in the formal policy record of the Federal Open Market Committee. This would be a considered statement of what the System is trying to do, how it tried to do it, and what seems to have been accomplished. In other words, we need some economic analysis of policy on a fairly current basis, done within the System, and presented regularly to the public. We would recommend that a quarterly presentation in the Federal Reserve Bulletin be prepared along these lines but we believe it should not be an official statement of the Committee itself. Perhaps, to insure that such a statement is authoritative but something less than official, it might be entrusted to the Economist and Associate Economists of the Committee. To test the practicability of this suggestion, the Committee could direct this group to prepare such a study covering the second quarter of 1961."

Mr. Deming: "If such a policy explanation were done quarterly for Bulletin publication, I see no reason why it should be lagged a quarter. Given the normal delays of writing and publication, it would be lagged 45 to 60 days anyway. I agree with Mr. Swan that such a quarterly article should not be an official Committee statement, but I assume that it would quote the Committee directives and policy actions as a framework on which to hang the discussion. Were this approach to be used, the official policy record in the Annual Report could be confined to a 'bare bones' story, perhaps using the 'general policy position' form as the only explanation of the policy action."

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Other Comments

Mr. Bopp: "...I should like to endorse with enthusiasm the decision to commission competent, uninvolved observers to review critically what we have done. I am persuaded that this innovation has very great promise for a viable Federal Reserve System. Of course, I disagree here and there with the Knipe and Broida memoranda; of course, they annoy me on occasion; but such disagreements and annoyances are relatively unimportant. What is important as we enter the future is a willingness to take the risks involved in authorizing and circulating among ourselves such memoranda. There are no experts in this field and we can profit immeasurably from uninhibited internal criticism."

Mr. Bryan: "...I wish to express the hope that we do not strive for complete unanimity in the document we are struggling over. There are evident great differences of philosophy in the Committee, and great differences in evaluating what is important and what is unimportant. If we struggle for unanimity, we shall produce an amorphous and witless document, satisfying to no one and resolutely defensible by no one."

CONFIDENTIAL (FR)

December 8, 1961

Checklist on Issues Concerning Committee Procedures

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Part I - General Issues Relating to "Operating Policies" or "Standing Rules"

1. At its March 7, 1961 meeting the Committee tabled consideration of changes in its existing operating policies, which consequently remain in effect. Should the Committee at this time:

   (a) Reaffirm the existing operating policies

   (b) Adopt revised operating policies or standing rules

   (c) Terminate existing operating policies

   (d) Take no action concerning operating policies

2. If a majority of the Committee favors taking no action at this time with regard to operating policies (alternative (d) under Question 1), should the Committee plan to consider such policies:

   (a) At the March 1962 organization meeting

   (b) After more experience is gained with the results of the special authorization

   (c) In conjunction with a thorough-going revision of the Regulation Relating to Open Market Operations of the Federal Reserve Banks, Rules on Procedure, and Rules on Organization and Information

3. If a majority of the Committee favors either revision or termination of operating policies (alternatives (b) or (c) under Question 1), should the published explanation appear:

   (a) Only in the Policy Record

   (b) Also in the <u>Federal Reserve Bulletin</u>, perhaps in extended form

Part II - Language for Operating Policies or Standing Rules

1. Should the suggestion be adopted that the preamble to the draft of standing rules be broadened to include reference to both the availability and cost of credit and possibly other ideas from paragraphs (a) and (b) of Regulation A?

2. If a majority of the Committee approves the modification of the preamble proposed in Question 1, should paragraph 1 of the standing rules be deleted?

3. If a majority of the Committee favors retention of paragraph 1, should the word "primarily" be inserted after "conducted"?

4. Which, if any, of the following versions of paragraph 1 should be adopted?

   (a) The September 6 draft wording:
   "Open market operations are conducted (primarily) to supply or absorb bank reserves consistent with the credit and monetary needs of the United States, in the light of both the domestic economy and international developments."

   (b) The September 6 draft wording, with the phrase "or for such other purposes as the Committee considers" inserted in line 2 after the word "reserves".

   (c) "Open market operations are conducted (primarily) to supply or absorb bank reserves consistent with the monetary and credit needs of the United States, in order to foster the broad objectives of monetary policy described above."

   (d) "Open market operations are conducted (primarily) to supply or absorb bank reserves consistent with the credit and monetary needs of the United States, in light of the above principle."

   (e) "Open market operations are conducted to promote appropriate monetary and credit policies in the light of both domestic and international developments."

   (f) "Open market operations shall be conducted for the purpose of carrying out the domestic and international objectives of monetary and credit policy."

5. Should paragraph 2 be deleted?

6. If a majority of the Committee favors retention of a paragraph along the lines of draft paragraph 2, should a definition of "short-term" be included in the paragraph?

7. Should the phrase "of any maturity" be inserted after "Government securities" in the first sentence of paragraph 2?

8. With respect to the second sentence of draft paragraph 2, which of the following alternatives should be chosen:

   (a) Complete deletion

   (b) Adoption of the September 6 draft wording, as amended: "Although operations in United States Government securities are ordinarily conducted in short-term issues, the Committee may authorize transactions in all maturities when desirable because of economic or financial conditions."

   (c) Replacement by the following:

   "Most operations in Government securities are conducted in short-term issues."

   (d) Replacement by the following:

   "; ordinarily the bulk of operations is conducted in short-term Government securities."

   (e) Replacement by the following:

   "Market conditions and practices, however, will usually require that the bulk of operations be confined to short-term securities."

9. Should the first sentence of draft paragraph 3 be deleted?

10. Should there be added to the first sentence of draft paragraph 3:

    (a) "although such operations may tend to influence rates of interest."

    (b) "although such operations influence interest rates."

11. Should the phrase, "appropriate corrective action" in draft paragraph 3 be replaced by the phrase, "such action as it deems appropriate"?

12. With respect to the second sentence of draft paragraph 4, should the word "generally" or "usually" be inserted before the phrase, "are not conducted"?

13. Should draft paragraph 5 be eliminated from the standing rules?

14. If a majority of the Committee favors elimination of draft paragraph 5 from the standing rules should the paragraph or its substance be included in the continuing authority directive?

15. If a majority of the Committee favors inclusion of a paragraph along the lines of draft paragraph 5 in either the standing rules or the continuing authority directive, which of the following courses should be chosen:

(a) Adoption of September 6 draft wording:
"Open market operations involving concurrent purchases and sales of securities of different maturity for the primary purpose of altering the maturity composition of the System's portfolio are ordinarily not undertaken."

(b) Replacement of the phrase, "are ordinarily not undertaken" by the phrase, "or for other reasons, are undertaken only upon the authorization of the Committee."

(c) Replacement of the whole paragraph by the following:

"The Committee avoids 'swap' transactions with others undertaken off the open market."

16. Should reference to repurchase agreements be omitted from the standing rules, in light of draft paragraph 3 of the continuing authority directive?

17. If a majority of the Committee favors inclusion of a paragraph along the lines of draft paragraph 6 in the standing rules, which of the follwing courses should be chosen:

(a) Adoption of the September 6 draft wording, as amended:
"Repurchase agreements in United States Government securities and prime bankers' acceptances are entered into with nonbank dealers to supply temporary reserve funds to the market. To this end, United States Government securities having remaining maturities of 15 months or less and prime bankers' acceptances are purchased from nonbank dealers subject to agreement for their resale within 15 calendar days. The repurchase rate is normally the discount rate at the Federal Reserve Bank of New York, but may be as low as the average issuing rate on the most recent issue of three-months Treasury bills."

(b) Replacement of the draft paragraph by one along the following lines, with the "details" left to the continuing authority directive:

"Repurchase agreements in Government securities and prime bankers' acceptances may be entered into with nonbank dealers to supply reserves on a temporary basis."

(c) Adoption of the amended draft paragraph, with replacement of the final sentence by:

"The repurchase rate is determined on the basis of conditions prevailing in the money markets, but is not less than the average auction rate on the most recent issue of three-month Treasury bills."

18. Should the maturity limit on securities acquired under repurchase agreements be:

(a) Retained at 15 months

(b) Increased to 24 months

(c) Removed completely

19. Should the substance of draft paragraph 7 be included in the standing rules?

20. If a majority of the Committee does not favor including the substance of draft paragraph 7 in the standing rules, which of the following courses should be chosen:

(a) Inclusion in Rules on Organization and Information or Rules on Procedure

(b) Inclusion in the continuing authority directive

(c) Inclusion in minutes of organization meeting

21. Should the following language be adopted as an additional rule:

"All transactions in United States Government securities, except certain exempt transactions indicated below, are conducted in the open market and at prices and yields prevailing in the market at the time purchases and sales are made. Exempt transactions include exchanges of maturing United States Treasury securities with the United States Treasury incident upon exchange offerings, and transactions with or for the account of foreign central banks. The Committee avoids 'swap' transactions with others undertaken off the open market."

Part III - Procedural Issues Relating to the Current Policy Directive

1. Should the Committee's directive to the Account Management be divided into a "continuing authority directive" and a "current policy directive"?

2. Should a "statement of general policy position" be regularly prepared as a supplement to the current policy directive?

3. Which of the following procedures should the Committee adopt for the preparation of the current policy directive (and policy statement, if any):

   (a) Have the Committee develop the directive in the course of its deliberations, without advance distribution of alternative possible directives

   (b) Have alternative possible directives distributed to the Committee several days in advance of the meeting, with agreement on the final directive to be reached in the course of deliberations

   (c) Have a draft directive (and policy statement, if any) prepared immediately after the meeting by the Secretary and the Account Manager on the basis of their understanding of the consensus, and, after approval by the Chairman, distributed to the Committee for approval or dissent

   (d) Have alternative possible directives distributed in advance of the meeting to facilitate deliberations, but follow the procedure indicated under (c) above for the preparation of the final directive (and policy statement, if any)

4. If a majority of the Committee favors having the directive completed after the meeting (alternative (c) or (d) under Question 3), which of the following procedures should be adopted:

   (a) Have the Committee reconvene briefly after lunch to pass formally on a directive drafted following the morning session

   (b) Have the directive drafted and distributed after adjournment, by wire to Presidents

Part IV - Form of the Current Policy Directive

1. Should the current policy directive include a summary statement on the cyclical phase of the economy?

2. Should the current policy directive include:

   (a) A qualitative guide, written in terms of relative degrees of ease or restraint, but without reference to specific variables such as total reserves, free reserves, money supply, bill rates, Federal funds rates, etc.

   (b) A qualitative guide, written in terms of one or more specific variables, e.g., calling for "somewhat higher (or lower) levels of ________"

   (c) A quantitative guide, written in terms of target ranges for one or more specific variables

   (d) None of these

3. If a majority of the Committee favors a reference to one or more specific variables in the current policy directive (alternatives (b) or (c) under Question 2) which variable(s) should be cited?

CONFIDENTIAL (FR) December 8, 1961

Standing Rules Governing Open Market Practice
Federal Open Market Committee
(Revision of draft of September 6, 1961)

As provided in section 12A of the Federal Reserve Act and in the Regulations of the Federal Open Market Committee, open market operations of the Federal Reserve Banks are conducted "with a view of accommodating commerce and business and with regard to their bearing upon the general credit situation of the country." To implement this governing principle as well as to help achieve and maintain a high level of economic activity and employment, sustainable growth, stability of the price level, and a ~~strong-position-in-the-world-economy,~~ SOUND INTERNATIONAL POSITION OF THE DOLLAR, the Committee adopts the following standing rules regarding open market practice: ~~subject-to-change-by-the-Committee-at-any-time.~~

1. Open market operations are conducted to supply or absorb bank reserves consistent with the credit and monetary needs of the United States, in the light of both the domestic economy and international developments.

2. Open market operations are transacted in United States Government securities and~~,-as-authorized,~~ in prime bankers' acceptances. Although operations in UNITED STATES Government securities are ordinarily conducted in short-term issues, the Committee may authorize transactions in all maturities when desirable because of economic or financial conditions.

3. Open market operations are not for the purpose of fixing or pegging the price of any issue of government securities. If conditions in the market for UNITED STATES Government securities should become disorderly, the Committee will take appropriate corrective action.

4. During Treasury financings, open market operations are conducted in such a manner as to change as little as possible ~~the conditions~~ prevailing ~~in the~~ money ~~markets.~~ MARKET CONDITIONS. Consequently, open market operations, EXCEPT THOSE INVOLVING REPURCHASE AGREEMENTS, are not conducted in (a) maturing issues, (b) when-issued securities, or (c) ~~comparable issues available in the market.~~ OUTSTANDING ISSUES COMPARABLE TO THOSE INVOLVED IN THE FINANCING.

5. Open market operations involving concurrent purchases and sales of securities of different maturity for the primary purpose of altering the maturity composition of the System's portfolio are ordinarily not undertaken.

6. Repurchase ~~arrangements~~ AGREEMENTS IN UNITED STATES GOVERNMENT SECURITIES AND PRIME BANKERS' ACCEPTANCES ARE ~~may be~~ entered into with nonbank dealers ~~from time to time~~ to supply temporary reserve funds to the market. To this end, UNITED STATES Government securities having remaining maturities of 15 months or less and prime bankers' acceptances ~~may be~~ ARE purchased from nonbank dealers subject to agreement for their resale within 15 calendar days. The repurchase rate is normally the discount rate at the Federal Reserve Bank of New York, but may be as low as the average issuing rate on the most recent issue of three-months Treasury bills.

7. The Federal Reserve Bank of New York is selected as the Federal Reserve Bank to execute transactions in the open market pursuant to AUTHORIZATIONS AND directions issued by the FEDERAL OPEN MARKET Committee. ~~from-time-to-time.~~

~~8.--The-Committee-will-meet-at-least-once-a-month,-but-other meetings-may-be-held-at-the-call-of-the-chairman.~~

8. THESE RULES MAY BE CHANGED OR REVOKED AT ANY MEETING OF THE FEDERAL OPEN MARKET COMMITTEE.