



BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON 25, D. C.

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

September 24, 1946.

PERSONAL AND CONFIDENTIAL

Dear Chairman Eccles:

In response to the request that you made before you left for the West, members of the Staff have drafted for your consideration a statement which might be adopted by the Executive Committee of the Federal Open Market Committee for the purpose of making it clear that the Manager of the System Open Market Account should not express personal opinions or recommendations to the Treasury with respect to Treasury financing policies and related matters. We believe this statement is a logical interpretation of the procedure set out in the Committee's letters of March 25 and April 25, 1944, to the Secretary of the Treasury which, in effect, made the Chairman and the Vice Chairman of the Committee the spokesmen for the System in this field.

The Staff members who worked on this statement feel that it would be preferable, if possible, to avoid the ruffled feelings that a discussion of the matter at a meeting of the Federal Open Market Committee or the Executive Committee might cause. It is, therefore, suggested, if you find the statement to be in satisfactory form, that you talk it over with Mr. Sproul before the meeting and, if you and he agree, the understanding could be confirmed by correspondence between you and him without unnecessary discussion.

In addition, you asked that the Staff prepare for your information, in case such a statement is not agreed upon, a memorandum showing how the operation of the System account could be brought more completely under the direct control of the Committee. Such a memorandum showing three possible plans, designated A, B and C, is attached. We believe that, if the point should be reached where some such plan must be considered, it would be plan A, because that plan provides for a complete divorce of the Manager and his staff from the control of any Reserve Bank. However, any such plan would raise the question what should be done about fiscal agency operations in the market, as distinguished from those for the System Open Market Account, and this question is commented upon in the last paragraph of the attached memorandum.

I am sending you this letter with the thought that you

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Chairman Eccles

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might find time to read the enclosed material before you reach Washington, so that you can think it over before you see Mr. Sproul.

Sincerely yours,

A handwritten signature in cursive script, appearing to read 'Cm', written in black ink.

Chester Morrill,
Special Adviser.

Enclosure

Chairman Marriner S. Eccles,
Hotel Ben Lomond,
Ogden, Utah.

Confidential memorandum for
Chairman Eccles regarding possible
plans for change in official rela-
tionship of Manager of System Open
Market Account to the Committee.

In the circumstances which brought up the question of a change in status, the major objective would be a clarification to everyone concerned of the Manager's relation and responsibility solely to the Committee. At the same time it must be borne in mind that, under the present arrangement, Mr. Rouse not only acts as Manager of the account but also handles the fiscal agency operations of the Federal Reserve Bank of New York in Government securities. It seems therefore that, while it would be possible to adopt one of the attached plans, the immediate purpose could be accomplished much more simply by an agreement that the Manager is bound by the policy adopted by the Committee in 1944 with respect to the procedure for communicating Federal Reserve System views to the Treasury.

Attached hereto are drafts of three possible plans (Plans A, B and C), all of which are designed to bring the Manager directly under the Open Market Committee and its Executive Committee. Plans B and C are presented solely for the purpose of showing possible variations, but, if any of the three plans were to be adopted, it is believed that Plan A is the only one that should be considered.

Under Plan A, the Manager, Deputy Manager, and the entire staff engaged in the operation of the account (except for purely ministerial functions) would be officers or employees of the Committee. They would, on behalf of the Reserve Banks, make all purchases and sales of securities for the System account, the Federal Reserve Bank of New York acting merely as custodian for the account. The existing dual responsibilities of the Manager would be wholly eliminated. Requiring the complete separation of this organization from the Reserve Bank, this plan would involve a major departure from the procedure heretofore followed.

In this connection, it is a well settled principle of law that a statutory grant of power carries with it the incidental power to do whatever is necessary to exercise what the power expressly granted. Therefore, if the Committee should find that it is necessary to employ and compensate a Manager, Deputy Manager, and staff required to operate the System account in order for the Committee to carry out effectively the powers expressly granted to it, the Committee would have the incidental power to do so and to require that the Reserve Banks pay the salaries and expenses of the necessary personnel.

If there should be any objection to this particular procedure for paying the expenses, it could be met by placing the Manager and his staff on the Board's pay roll where they could be paid out of the proceeds of the Board's assessments on the Reserve Banks.

Plan B would be a less drastic plan. It is presented at this point because it is similar to one which was discussed in 1944. It differs from Plan A in that only the Manager and Deputy Manager (and not the entire staff) would be employed by the Committee. The Manager and Deputy Manager would control transactions for the account through the issuance of instructions to the Federal Reserve Bank of New York pursuant to the directions of the Executive Committee, but the actual purchase and sale of securities and other services incident to the operation of the account would continue to be performed by the Reserve Bank as at present. This plan would make the Manager and Deputy Manager responsible directly to the Executive Committee and not to the Reserve Bank of New York. It would therefore eliminate dual responsibility. However, the services that would be performed by the employees of the Reserve Bank necessarily would require the exercise of some judgment and there would also be the danger of administrative difficulties because of the fact that the Reserve Bank employees would continue to be on the pay roll of the Reserve Bank and therefore would not technically be members of the Manager's staff.

Plan C would be still less of a departure from the existing arrangement because it would provide only that, except with the permission of the Committee, the Manager of the System account would perform no duties and have no responsibilities other than as Manager of the account and he would be responsible directly and solely to the Committee and its Executive Committee. This would not accomplish quite as much as either of the other two plans but it would be designed within the framework of the existing organization, to separate the responsibility for System account operations from other operations of the Reserve Bank of New York, and to make more clear the authority of the Committee over the Manager. Under this plan, the Manager's position might be regarded as somewhat analogous to that of Assistant Federal Reserve Agent.

None of these plans provides expressly for coordination of System Open Market operations and those of the Treasury in the Government securities market. Under Plan C, however, and perhaps under Plans A and B, although that seems doubtful, arrangements might be made for the Manager of the System account to continue to handle Treasury affairs. Obviously, however, the result would be the same as under the present arrangement and it is questionable whether anything would be gained that could not be accomplished by specific instructions to the Manager of the account to refrain from expressing personal opinions and recommendations.

September 24, 1946.

PLAN A

SEPARATE MANAGER OF SYSTEM OPEN MARKET ACCOUNT

1. The Manager of the System account and a Deputy Manager would be selected and their salaries fixed by the Federal Open Market Committee. Members of the Manager's staff would be selected and their salaries fixed in such manner as the Committee might determine. The salaries of the Manager, Deputy Manager, and the staff, and all other expenses of the office, would be paid by the Federal Reserve Bank of New York on a reimbursable basis, or by the Board of Governors.
2. The Manager, Deputy Manager, and the staff would not be officers or employees of the Board or any Federal Reserve Bank but would be officers and employees of the Committee and responsible solely to it and its executive committee acting pursuant to directives of the full Committee.
3. Under the direction of the Committee or its executive committee all purchases and sales of securities for the System account would be made by the Manager on behalf of the Federal Reserve Banks.
4. The Federal Reserve Bank of New York would serve as custodian for the account, having custody of the securities held in the account and paying for securities, delivering and collecting for securities pursuant to instructions given by the Manager or the Deputy Manager, and allocating securities held in the account to the various Federal Reserve Banks.
5. The Committee would make provision for office space and all other necessary facilities for the Manager's office, and consideration could be given to the location of the offices at some place other than the Federal Reserve Bank of New York.

September 24, 1946.

Confidential

PLAN B

SEPARATE MANAGER OF SYSTEM OPEN MARKET ACCOUNT

1. The Manager and the Deputy Manager of the System account would be selected and their salaries fixed by the Federal Open Market Committee. Their salaries and authorized expenses would be paid by the Federal Reserve Bank of New York on a reimbursable basis or by the Board of Governors.

2. While the Manager and Deputy Manager would be responsible solely to the Committee and its Executive Committee, and they would control all transactions in the account, they would perform their functions through the issuance of instructions to the Federal Reserve Bank of New York which would continue to carry them out through the existing staff as at present.

3. The Federal Reserve Bank of New York would continue to serve as custodian for the account, having custody of the securities held in the account, and paying for securities, delivering and collecting for securities, pursuant to instructions given by the Manager or the Deputy Manager, and allocating securities held in the account to the various Federal Reserve Banks.

September 24, 1946.

PLAN C

SEPARATE MANAGER OF SYSTEM OPEN MARKET ACCOUNT

Continue the existing arrangement under which the Manager of the System Open Market Account is an officer of the Federal Reserve Bank of New York but provide --

1. That the Manager shall perform no duties and have no responsibilities other than as Manager of the Account; and
2. That the Manager shall be responsible directly and solely to the Federal Open Market Committee and to its Executive Committee acting pursuant to directives of the full Committee.

September 24-1946.