

February 14, 1951.

Governor Eccles:

Pursuant to your suggestion that I look into the legislative history of the Banking Act of 1935 in connection with the functions of the Open Market Committee, I have now prepared the attached memorandum regarding the relationships between the Federal Reserve System and those of the Treasury on this subject.

GBV

February 14, 1951.

(CONFIDENTIAL)

RELATIONSHIPS BETWEEN RESPONSIBILITIES OF THE
FEDERAL RESERVE SYSTEM AND THOSE OF THE SECRETARY
OF THE TREASURY

The purpose of this memorandum is to consider the relationship of the functions and responsibilities of the Secretary of the Treasury with respect to the Government debt and those of the Federal Reserve System with respect to open market operations and credit conditions.

Statutory Functions

Federal Reserve. - Section 12A of the Federal Reserve Act, which creates the Federal Open Market Committee, provides that the time, character, and volume of all purchases and sales by Federal Reserve Banks in the open market "shall be governed with a view to accommodating commerce and business and with regard to their bearing upon the general credit situation of the country." No Federal Reserve Bank may engage or decline to engage in open market operations "except in accordance with the direction of and regulations adopted by the Committee."

This is the principal provision of statute which gives direction to the Federal Reserve authorities as to open market operations. There are, however, other related statutes. Thus the Federal Reserve Act provides that each Federal Reserve Bank, subject to the law and the orders of the Board of Governors of the Federal Reserve System, may extend credit with due regard for "the maintenance of sound credit conditions, and the accommodation of commerce, industry, and agriculture." The Board is authorized to change reserve requirements for member banks "in order

to prevent injurious credit expansion or contraction". Also, discount rates of the Federal Reserve Banks are to be fixed by them, subject to review and determination by the Board, "with a view of accommodating commerce and business." (Federal Reserve Act, secs. 4, 19, and 14)

Thus, it is clear that Federal Reserve responsibility in general is to act in the interest of sound credit conditions and of the accommodation of commerce and business.

Treasury. - The Secretary of the Treasury is authorized to borrow on the credit of the United States for purposes authorized by law and to issue bonds of the United States therefor which "shall be in such form or forms and denomination or denominations and subject to such terms and conditions of issue, conversion, redemption, maturities, payment, and rate or rates of interest, not exceeding 4-1/4 per centum per annum, and time or times of payment of interest as the Secretary of the Treasury from time to time at or before the issue thereof may prescribe." It is likewise provided that savings bonds and savings certificates "may be sold at such price or prices, and redeemed before maturity upon such terms and conditions as the Secretary of the Treasury may prescribe: Provided, That the interest rate on, and the issue price of, savings bonds and savings certificates and the terms upon which they may be redeemed shall be such as to afford an investment yield not in excess of 3 per centum per annum, compounded semiannually. * * *The Secretary of the Treasury is authorized by regulation to fix the amount of savings bonds and savings certificates issued in any one year that may be held by any one person at any

one time." Any obligations "may be offered for sale on a competitive or other basis under such regulations and upon such terms and conditions as the Secretary of the Treasury may prescribe; and his decision with respect to any such issue shall be final." The Secretary is also authorized to borrow in order to "provide for the purchase, redemption or refunding at or before maturity" of any outstanding obligations of the United States. (Title 31 U.S.C., secs. 752, 753(a), 754a and b, and 757c) There are also other statutes of generally similar purport.

The Secretary of the Treasury also has authority to invest the so-called trust funds of the Government, such as the Civil Service Retirement Fund, the Unemployment Trust Fund, the Federal Old Age and Survivors Trust Fund, the Veterans Life Insurance Funds, and others. These are to be invested by him in United States securities or otherwise according to the terms of the specific applicable statutes.

Independence of Treasury and Federal Reserve System

Nothing could be clearer under the law than the fact that the Federal Reserve Board and the Federal Open Market Committee are not in any sense subordinate to the Treasury Department but are independent thereof. The Federal Reserve Board was created by Congress. It is required to make reports to Congress. It is required to include in its annual reports to Congress a full account of all policy actions taken by the Board or by the Open Market Committee. The Attorney General

held soon after the Federal Reserve System was created that the Board is "an independent board or Government establishment" of the United States. 30 Op. Atty. Gen. 308 (1914).

If there had been any doubt as to the independent status of the Board, it was completely removed by the Banking Act of 1935 in eliminating from the Board the ex officio memberships of the Secretary of the Treasury and the Comptroller of the Currency. Under the 1935 Act the seven members of the Board comprise a majority of the membership on the Federal Open Market Committee. The legislative history of this Act indicates clearly that the reason for these changes in the law was to avoid the possibility of the exercise of undue influence by the Secretary of the Treasury on the Federal Reserve Board. In this connection, Senator Glass, in debating the Banking Act of 1935, said (79 Cong. Rec. p. 11776):

"Since the establishment of the system, and now, the Secretary of the Treasury and the Comptroller of the Currency have been members of the Federal Reserve Board. Periodically, it has been urged upon the Banking and Currency Committees of the two Houses of Congress that these two officials should be eliminated, for various reasons. With respect to the Secretary of the Treasury, it was urged--and I know it to be a fact, because I was once Secretary of the Treasury--that he exercised undue influence over the Board; that he treats it rather as a bureau of the Treasury instead of as a board independent of the Government, designed to respond primarily and altogether to the requirements of business and industry and agriculture, and not to be used to finance the Federal Government, which was assumed always to be able to finance itself."

Congress has indicated on several occasions that Treasury financing should not be allowed to become the dominant influence in Federal Reserve System policy. One such indication, as just mentioned, was the removal of the Secretary of the Treasury from membership on the Federal Reserve Board in 1935. Another example is found in the restraint placed upon direct purchases of Government securities by the Reserve Banks from the Treasury.

The Banking Act of 1935 completely prohibited such direct purchases. In 1942 the authority to make such direct purchases, but only in amounts up to \$5 billion, was given by Congress on a temporary basis and has been renewed from time to time. It has always been clearly understood, however, and clearly stated in the legislative history of this subject, that any such direct purchases from the Treasury were to be only for temporary purposes and not for permanent financing. As a matter of fact, the 1935 provision prohibiting direct purchases was based upon the view that the central bank should not have the authority to purchase directly from the Treasury because of the possibility of unlimited borrowing by the Treasury on a fiat money basis. It is clear, however, that a policy under which the System would maintain support in the open market for Government securities at a level inconsistent with the needs of the general economy would have precisely the same effect, even though accomplished by a less direct method, as the purchase of securities directly from the Treasury. Any level of Government securities prices

maintained by the System should be justified on the ground of benefit to the national economy or, more specifically, should be in accord with the directive laid down by the statute that open market operations be conducted for the accommodation of commerce and business and with regard to the general credit situation of the country.

Although the Federal Reserve Banks have authority to conduct open market operations in certain classes of paper other than Government securities, in actual practice open market operations consist almost entirely of transactions in Government securities. It is clear that Congress recognized that this is the case. Thus, in debating the Banking Act of 1935, Mr. Goldsborough, one of the members of the House Banking and Currency Committee who helped to guide the bill through Congress, stated: "I can only generalize, but I am sure it will be sufficiently satisfactory to say that open market operations consist of the buying of Government bonds when the Federal Reserve Board thinks it is necessary to put more money into circulation in order to avoid a depression, and the sale of Government bonds at a time when they deem it necessary in order to prevent a period of wild speculation."

(79 Cong. Rec. p. 13710)

Respective Fields of Legal Responsibility of Treasury and Federal Reserve

It is clear from the brief recital given above of the statutory powers of the Federal Reserve System on the one hand and of the Secretary of the Treasury on the other that their respective functions and responsibilities, insofar as they relate to Government securities, fall generally in different fields. The Secretary clearly has full authority and responsibility with respect to the issuance of Government securities and the terms and conditions upon which they are issued. He also has authority to prescribe the rates of interest on Government obligations, subject to the maximums provided in the statute. The Federal Reserve System on the other hand, through its Open Market Committee, is given full authority to control the purchase and sale of Government securities by the Federal Reserve Banks in the open market and is given a directive that such purchases and sales shall be made with a view to accommodating commerce and business and with regard to the general credit situation of the country.

These provisions giving certain functions to the Treasury and certain functions to the Federal Reserve System are not inconsistent or overlapping (except perhaps in limited areas such as, for example, the investment of Government trust funds). In any event, however, the statutory directive of the Federal Reserve is clear. It is true that action taken by either party may have an important practical effect upon the actions which the other may feel it desirable to take in its field. Their legal responsibilities, however, are different. The decisions of the Secretary with respect to the issuance of securities and the terms of such issuance are final and the Federal Reserve System has no

authority or responsibility with respect thereto. On the other hand, the Federal Open Market Committee has sole responsibility for conducting open market operations in Government securities in accordance with the directive in the law. This legal authority of the Open Market Committee to control the purchase and sale of Government securities by the Federal Reserve Banks is not shared with anyone. So far as the statute is concerned, the Committee is completely independent in the making of its decisions.

Maintenance of Orderly Conditions in Government
Securities Market

The statutory directive with respect to the conduct of open market operations does not contain any specific provision with respect to the maintenance of orderly conditions in the Government securities market. Clearly, however, the maintenance of such orderly conditions has a close relationship to the general credit situation of the country. Obviously the prices and yields on Government securities purchased in the market affect very promptly the prices and yields on other securities. Stated differently, the Government securities market is of concern to the System as a part of the general economic picture. Thus the Open Market Committee has, by implication of the law, a responsibility in taking its actions to consider conditions in the Government securities market as well as other credit conditions in the country. It is entirely within its powers to adjust its purchases and sales of Government securities in the light of prices and interest yields thereon. Its concern, however, is not limited to the prices and yields of Government securities but

extends to the total volume, availability and cost of credit. In recent years, because of the tremendous increase in the amount of Government securities outstanding, the maintenance of orderly conditions in the Government securities market has assumed an important role in the functions of the Federal Open Market Committee. During the period of 1935-40 the Federal Reserve System undertook to maintain orderly conditions in the market for United States securities. The Board explained its position in connection with this matter in its 1939 Annual Report as follows:

"* * * While the System has neither the obligation nor the power to assure any given level of prices or yields for Government securities, it has been its policy in so far as its powers permit to protect the market for these securities from violent fluctuations of a speculative, or panicky nature. Prices of fixed-interest rate securities, including those of the Government, inevitably adjust to changes in long-time interest rates. Consequently, an orderly rise or fall in United States bond prices in response to changes in underlying credit conditions, as expressed in interest rates, does not call for action by the System. * * *

"In undertaking large-scale open-market operations in September 1939, the System was guided principally by the following considerations:

"(1) By helping to maintain orderly conditions in the market for United States Government securities the System can exert a steadying influence on the entire capital market, which is an essential part of the country's economic machinery, and disorganization in which would be a serious obstacle to the progress of economic recovery. The market for United States Government securities is the only part of the capital market in which the System is authorized by law to operate, and Government securities occupy a vital place in that market.

"(2) The System also has a measure of responsibility for safeguarding the large United States Government portfolio of the member banks from unnecessarily wide and violent fluctuations

in price. The System cannot and does not guarantee any current prices of Government obligations, nor does it undertake to preserve for member banks such profits as they may have on their Government securities, or to protect them against losses in this account. * * *"

It is to be emphasized, however, that although the Federal Open Market Committee may and does consider the maintenance of orderly conditions in the Government securities market in conducting its operations, it is not required to support the market for Government securities nor is it required to support any issue at any particular level. Its consideration of the Government securities market must be made in the light of and fitted into its responsibility for overall credit conditions. These are matters which it should consider and decide in the light of the statutory directive that open market operations be governed with a view to accommodating commerce and business and with regard to their bearing upon the general credit situation of the country.

The attached Appendix gives certain additional information regarding the history of the Federal Open Market Committee, the legislative history of the Banking Act of 1935, and the statutory directives regarding the exercise of Reserve System functions.

APPENDIX

HISTORY OF STRUCTURE OF FEDERAL OPEN MARKET COMMITTEE TO 1935

No organization similar to the present Federal Open Market Committee was created by the original Federal Reserve Act. An open market committee, which was entirely on a voluntary basis, was originally formed in 1922. It consisted at first of a committee of five Governors of the Federal Reserve Banks and later comprised all twelve of the Governors. The Committee was not provided for in the statute until the enactment of the Banking Act of 1933 (48 Stat. 162, 168). By that Act Congress created a Federal Open Market Committee, consisting of one representative from each Federal Reserve Bank. The following paragraphs were included in the provisions of the Banking Act of 1933 relating to this subject:

"(b) No Federal reserve bank shall engage in open-market operations under section 14 of this Act except in accordance with regulations adopted by the Federal Reserve Board. The Board shall consider, adopt, and transmit to the committee and to the several Federal reserve banks regulations relating to the open-market transactions of such banks and the relations of the Federal Reserve System with foreign central or other foreign banks.

"(c) The time, character, and volume of all purchases and sales of paper described in section 14 of this Act as eligible for open-market operations shall be governed with a view to accommodating commerce and business and with regard to their bearing upon the general credit situation of the country.

"(d) If any Federal reserve bank shall decide not to participate in open-market operations recommended and approved as provided in paragraph (b) hereof, it shall file with the chairman of the committee within thirty days a notice of its decision, and transmit a copy thereof to the Federal Reserve Board."

BANKING ACT OF 1935

The Banking Act of 1935 (49 Stat. 684, 704-706), among other things, reconstituted the Reserve Board and eliminated therefrom the Secretary of the Treasury and the Comptroller of the Currency as ex officio members (sec. 203); reconstituted the Federal Open Market Committee to comprise the seven members of the Board and five Reserve Bank representatives and increased the Committee's authority over open market operations (sec. 205); and prohibited the direct purchases of United States obligations (sec. 206). These changes were contained in Title II of the Act, "fundamental purposes" of which, according to the House Banking and Currency Committee, were--

"To concentrate the authority and responsibility for the formulation of national monetary policy in a body representing the general public interest.

"To modify the structure of the Federal Reserve System to the extent necessary for the accomplishment of these purposes * * *" (H. Report No. 742, 74th Cong., 1st Sess., p. 1)

Elimination of ex officio members of Board. - Prior to the Banking Act of 1935, the Reserve Board comprised six appointive members plus the Secretary of the Treasury and the Comptroller of the Currency as ex officio members. In connection with the reconstitution of the Board by the 1935 Act to comprise seven appointive members only, Senator GLASS explained during debate on the bill that (79 Cong. Rec. 11776-11777)--

"Since the establishment of the system, and now, the Secretary of the Treasury and the Comptroller of the Currency have been members of the Federal Reserve Board. Periodically, it has been urged upon the Banking and Currency Committees of the two Houses of Congress that these two officials should be eliminated, for various reasons. With respect to the

Secretary of the Treasury, it was urged--and I know it to be a fact, because I was once Secretary of the Treasury-- that he exercised undue influence over the Board; that he treats it rather as a bureau of the Treasury instead of as a board independent of the Government, designed to respond primarily and altogether to the requirements of business and industry and agriculture, and not to be used to finance the Federal Government, which was assumed always to be able to finance itself.

"Moreover, it was represented that these officials, except when of their own initiative they wanted something to be acted on, rarely ever attended meetings of the board. I think the present Secretary of the Treasury has attended only two or three meetings. I do not think I, as Secretary of the Treasury, ever attended more than one or two meetings of the Board; but, all the same, I dominated the activities of the Board, and I always directed them in the interest of the Treasury, and so did my predecessor, the present Senator from California [Mr. McAdoo]. That, however, was because when he functioned it was during the war, and when I functioned it was in the immediate post-war period, when the difficulties of the Treasury perhaps exceeded those of the war period. Certainly they were not less.

"In the Banking Act of 1932, which passed the Senate overwhelmingly, there was a provision eliminating the Secretary of the Treasury, and upon a record vote it was retained in the bill by 62 to 14, after considerable discussion on the floor, which indicated that the Senate concurred in the better judgment of those who think the Secretary of the Treasury and the Comptroller of the Currency should not be on the Board.

"That provision would have been retained in the Banking Act of 1933 but for the fact that the then Secretary of the Treasury, in wretched health which eventuated in his death, was greatly concerned about the matter, and was rather importunate and insistent in desiring to be retained as a member of the Board. In the bill which we have reported, however, we leave off both the Secretary of the Treasury and the Comptroller of the Currency, with no dissent from these officials. The bill constitutes the Board of Governors of the Federal Reserve System of seven members, to be appointed by the President, by and with the advice and approval of the Senate. The President is authorized to appoint one of these governors as chairman of the Board, and another as vice chairman of the Board."

During the Senate debate on the bill, Senator BORAH referred to certain statements of Dr. Miller, then a member of the Board,

concerning certain relationships initiated in 1927 between the Federal Reserve Bank of New York and the Bank of England. In connection with the initiation of such relationship, Senator GLASS responded (79 Cong. Rec. 11910)--

"MR. GLASS. That simply illustrates what I have said for years. It was first presented to the Secretary of the Treasury, and the Secretary of the Treasury, together with the governor of the New York Federal Reserve Bank, dominated the Board. The Secretary of the Treasury ought not to be on the Board."

Senator THOMAS also adverted to this matter concerning the New York Reserve Bank and pointed out specifically that the Secretary of the Treasury supported this much criticized relationship between the New York Reserve Bank and the Bank of England which was opposed by five Board members. Senator GLASS replied that (79 Cong. Rec. 11924)--

"MR. GLASS. I have said all along that the Secretary of the Treasury had too much influence on that Board, and for that reason we have omitted him as a member of the Board."

Senator THOMAS went on to refer to Dr. Miller's statement that the Board must have "a national viewpoint" and owe "undivided allegiance to the general-public interest. Its judgment should not be warped by the viewpoint of any particular section * * * or by the special interests of any particular group." To this Senator GLASS replied (79 Cong. Rec. 11924)--

"MR. GLASS. We accepted his suggestion, and it is embodied in the bill."

Reconstitution of Federal Open Market Committee. - Prior to the Banking Act of 1935, this Committee was composed of 12 members -- one representative from each Reserve Bank. Its function was to consult

with the Board whose function, briefly, was to prevent open-market operations by the Banks except with Board approval. But, the Board could not compel the Banks to engage in such operations (Federal Reserve Act, Sec. 12A, as added by Sec. 8 of the Banking Act of 1933).

In the bill which became the Banking Act of 1935, the House Committee proposed an Open Market Committee of 5 Reserve Bank representatives. The Committee was to function on a consultive basis, but the Board was to have power to require as well as to prevent open-market operations by the Reserve Banks. In this regard, the House Committee said (H. Report 742, 74th Cong., 1st Sess., pp. 9-10)--

"* * * it is essential that the Board be given the same definite responsibility and final authority with respect to the open-market policies of the Federal Reserve System as it already possesses with respect to discount rates * * * and * * * reserves * * *.

"* * *

"The amendment will [place] * * * responsibility for national monetary and credit policies squarely upon the Federal Reserve Board. It will eliminate conflicts of jurisdiction and policy because the final decision as to all matters affecting national policies would be vested in the Federal Reserve Board."

Mr. HOLLISTER was among the dissenting minority of the House Committee which thought Title II of the bill placed too much power in the Board. During the debate in the House, he said (79 Cong. Rec. 6568-6569)--

"One of the chief objections to this bill is through the open-market provisions by which the Federal Reserve Board is given power to compel Federal Reserve banks to enter into open-market operations on the buying side. When that is once passed, then we have put into the control of the Federal

Reserve Board a most dangerous instrument. We have reached the point then where, if sufficient Treasury control is exercised on the Federal Reserve Board, the Federal Reserve Board in turn may compel the Federal Reserve banks of the country, which, of course, have the reserves and the excess reserves of the various member banks in their vaults, to keep on buying and buying and buying Government obligations, even though all wise bankers and all careful economists would have served notice long before that the Government might not continue to issue obligations of the nature they are compelling the banks to acquire."

When the bill was reported by the Senate Banking and Currency Committee, the House version of the Open Market Committee had been changed. The Senate proposed that the Open Market Committee be composed of the seven members of the Reserve Board and five Reserve Bank representatives, and that the Committee as so constituted should determine open-market policy and direct the Reserve Banks to engage or not to engage in open-market operations (S. Report No. 1007, 74th Cong., 1st Sess., pp. 12-13).

The bill then went to the Conference Committee which, briefly, adopted the Senate proposal as described above (H. Report No. 1822, 74th Cong., 1st Sess., pp. 49-50). The version adopted by the Conference Committee was the one finally enacted.

In presenting the Conference version to the House in debate, Mr. STEAGALL said (79 Cong. Rec. 13705-13706)--

"This means that we have fought out in this House, in the Senate, and in the conference the question of Government control of the open-market operations, the rediscount rates, and the reserve requirements of the Federal Reserve banks, and as a result of this controversy we have a bill which writes into the law a safeguard that insures the investment of these powers in a Government-controlled board.

"The vote would be 7 to 5 if we assume that the 5 members representing the banks would go contrary to the 7 members representing all the people of the country or the public at large. The Senate bill had in it a provision requiring the appointment of 2 members of the 7 constituting the Federal Reserve Board to be experienced bankers. This provision was stricken out in conference.

"So we have written into this law the principle that the Government, the sovereign people of the United States, shall have control of the Board that dictates the vast powers of the Federal Reserve System.

"* * *

"But last, or in any event, certainly not least, is the provision in this bill, embodied in the conference report, that changes the personnel of the Federal Reserve Board. The Board is now made up of 6 appointed members, plus 2 ex officio members -- the Secretary of the Treasury and the Comptroller of the Currency. The measure reported to the House contains a provision for a new board of seven members, with the power of appointment placed in the President of the United States. The President of the United States is clothed with the power to reorganize the Federal Reserve Board.

"So as to bring the System with its vast resources and powers into full harmony with the advanced policies of the present administration.

"We all know that it does not matter so much what we write into the law as it does who administers the law. We have provided a practical method for employing the powers of the Federal Reserve Board. Under the law now existing the Board is without power to put into execution any policies which it may determine upon.

"Under the present law policies must be originated by a committee consisting of the 12 governors of the Federal Reserve banks and approved by the Federal Reserve Board, but there is no authority to compel compliance. One bank can nullify any policy though it may have approval of the Federal Reserve Board and the other 11 banks.

"Under this bill the power is fixed definitely in the Board, which represents the people of the United States, and the power of compliance is placed unreservedly in their hands.

"That is what is in this bill. It is not all that I would like to see; it is not all that many Members of this House would like to see; but it represents a great reform, a great forward practical plan for the exercise of the sovereign power of the Government to control the Nation's credit and monetary policy in the interest of all the people of the United States."

EMPLOYMENT ACT OF 1946

The Employment Act of 1946 states that

"SEC. 2. The Congress hereby declares that it is the continuing policy and responsibility of the Federal Government to use all practicable means consistent with its needs and obligations and other essential considerations of national policy, with the assistance and cooperation of industry, agriculture, labor, and State and local governments, to coordinate and utilize all its plans, functions, and resources for the purpose of creating and maintaining, in a manner calculated to foster and promote free competitive enterprise and the general welfare, conditions under which there will be afforded useful employment opportunities, including self-employment, for those able, willing, and seeking to work, and to promote maximum employment, production, and purchasing power." [Act of February 20, 1946, (60 Stat. 23); U.S.C., Title 15, Sec. 1021]

All Government agencies have an equal responsibility to carry out this directive as far as practicable.

The Act provides, in part, that the President shall transmit to the Congress at each session thereof "an economic report * * * setting forth * * * (3) a review of the economic program of the Federal Government * * *; and (4) a program for carrying out the policy declared [above] * * *, together with such recommendations for legislation as he may deem necessary or desirable".

The Act also establishes a Council of Economic Advisors, appointed by the President, whose duties, among other things, are --

"(1) to assist and advise the President in the preparation of the Economic Report;

"* * *

"(3) to appraise the various programs and activities of the Federal Government in the light of the policy declared in section 2 for the purpose of determining the extent to which such programs and activities are contributing, and the extent to which they are not contributing, to the achievement of such policy, and to make recommendations to the President with respect thereto;

"(4) to develop and recommend to the President national economic policies to foster and promote free competitive enterprise, to avoid economic fluctuations or to diminish the effects thereof, and to maintain employment, production, and purchasing power;"

STATUTORY DIRECTIVES REGARDING EXERCISE OF RESERVE SYSTEM FUNCTIONS

There are set forth below principal statutory directives to the Federal Reserve System regarding the exercise of its functions.

Reserve Bank Credit to Member Banks. - Section 4 of the Federal Reserve Act, as amended, provides that each Federal Reserve Bank "may, subject to the provisions of law and the orders of the Federal Reserve Board, extend to each member bank such discounts, advancements, and accommodations as may be safely and reasonably made with due regard for the claims and demands of other member banks, the maintenance of sound credit conditions, and the accommodation of commerce, industry, and agriculture." In addition, the Board is authorized to "prescribe regulations further defining * * * the conditions under which" such credit may be extended to member banks; and the Board may suspend member banks from System credit facilities if "undue use is

being made of bank credit for the speculative carrying of or trading in securities, real estate, or commodities, or for any other purpose inconsistent with the maintenance of sound credit conditions." [Federal Reserve Act, sec. 4, as amended by Act of June 16, 1933, sec. 3 (48 Stat. 163); U.S.C., title 12, sec. 301]

Change of Reserve Requirements. - By section 46 of the Act of May 12, 1933 (48 Stat. 51, 54), the Board was authorized to increase or decrease the reserve balances of member banks with the approval of the President during any emergency existing "by reason of credit expansion". In lieu of this emergency power, there was added to the law in 1935 a provision authorizing the Board, "in order to prevent injurious credit expansion or contraction", to change the reserve requirements for member banks, any such change to be within a limit of twice the percentages specified in the statute. [Federal Reserve Act, sec. 19, as amended by Act of August 23, 1935, sec. 207 (49 Stat. 706); U.S.C., title 12, sec. 462b.]

Open-Market Operations. - The Banking Act of 1933 established a "Federal Open Market Committee". This was accomplished by the addition of a new section 12A to the Federal Reserve Act which provided that, with respect to open-market operations under section 14, "The time, character, and volume of all purchases and sales of paper described * * * as eligible for open-market operations shall be governed with a view to accommodating commerce and business and with regard to their bearing upon the general credit situation of the country." [Act of June 16, 1933, sec. 8 (48 Stat. 168)]

The Banking Act of 1935 further amended the law in this regard. While this amendment did not redefine the general guide or standard for open-market operations introduced by the Banking Act of 1933, it placed specific responsibility therefor in the "Federal Open Market Committee" which was reconstituted to comprise the seven members of the Board and five Reserve Bank representatives. In addition, the Reserve Banks were authorized and required to engage in open-market operations only as the Committee might direct. [Federal Reserve Act, sec. 12A, as amended by Act of August 23, 1935, sec. 205 (49 Stat. 705-706); U.S.C., Title 12, sec. 263. Further technical amendment not changing the policy guide was made by Act of July 7, 1942. (56 Stat. 647)]

Rates of Discount. - The Federal Reserve Banks are authorized "To establish from time to time, subject to review and determination of" the Board, "rates of discount to be charged by the Federal Reserve Banks for each class of paper, which shall be fixed with a view of accommodating commerce and business." [Section 14(d) of the Act (38 Stat. 265); U.S.C., title 12, sec. 357]