

FEDERAL RESERVE BANK OF DALLAS

DALLAS, TEXAS 75222

Circular No. 78-29

March 14, 1978

RESERVE BANK DIRECTORS--ACTIONS AND RESPONSIBILITIES

New Regulation and Guide to Conduct

TO ALL MEMBER BANKS IN THE
ELEVENTH FEDERAL RESERVE DISTRICT:

Under the Federal Reserve Reform Act of 1977, the directors of Federal Reserve Banks are prohibited from participating in matters in which they, or related persons or organizations, have a financial interest, except where, after full disclosure by a director or pursuant to general rules published by the Board of Governors of the Federal Reserve System, the financial interest has been exempted by the Board of Governors as too remote or inconsequential to affect the integrity of the director's services.

Accordingly, the Board of Governors has adopted, effective February 17, 1978, a new regulation entitled "Reserve Bank Directors--Actions and Responsibilities" and a "Guide to Conduct for Directors of Federal Reserve Banks and Branches of Federal Reserve Banks." While the regulation has been adopted as a final rule in view of the statute's current application to directors and the desirability of providing directors both guidance and protection from liability, as a practical matter, the regulation will be treated as interim in nature pending receipt by the Board of Governors of comments and views from directors, Reserve Banks, and other interested persons.

Printed on the enclosed pages is the text of the regulation and guide as submitted to the FEDERAL REGISTER. The Board has invited the directors, Reserve Banks, and other interested persons to submit comments and views in writing to the Secretary, Board of Governors of the Federal Reserve System, Washington, D.C. 20551, not later than April 14, 1978. All materials submitted should include the docket number R-0144. After consideration of all comments received, the Board of Governors is prepared to adopt promptly necessary and appropriate amendments to the regulation.

Sincerely yours,

Ernest T. Baughman

President

Enclosure

Extract From
FEDERAL REGISTER,
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[6210-01]

Title 12—Banks and Banking

CHAPTER II—FEDERAL RESERVE SYSTEM

SUBCHAPTER A—BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM

[Docket No. R-0144]

PART 264a—RESERVE BANK DIRECTORS—
ACTIONS AND RESPONSIBILITIES

AGENCY: Board of Governors of the
Federal Reserve System.

ACTION: Final rule.

SUMMARY: As a result of enactment of the Federal Reserve Reform Act of 1977, provisions of the U.S. Code relating to acts affecting a personal financial interest were amended to apply to directors of Federal Reserve Banks. Under the amended statute, a director of a Federal Reserve Bank is prohibited from participating personally and substantially in any particular matter in which the director, the director's spouse or minor child, or other individuals or organizations identified in the statute, have a financial interest. However, such prohibition shall not apply, if the director has first advised the Board of Governors of the Federal Reserve System of the nature and circumstances of the particular matter, has made full disclosure of the financial interest involved, and has received in advance a written determination by the Board of Governors that the financial interest "is not so substantial as to be deemed likely to affect the integrity of the services" which the Federal Reserve System may expect from such director. The statute further provides that such prohibition shall not apply if, by general rule or regulation published in the FEDERAL REGISTER, the financial interest has been exempted by the Board of Governors as being "too remote or too inconsequential" to affect the integrity of directors' services.

This rule is promulgated by the Board of Governors for the purpose of implementing and providing guidance concerning the recently amended statute. Specifically, the rule contains prohibitions against director participation in particular matters, sets forth proposed procedures under which a director may obtain an ad hoc exemption pursuant to the statute, and identifies certain financial interests of directors that the Board has exempted from coverage by the statute as being too remote or too inconsequential to affect the integrity of directors' services.

EFFECTIVE DATE: February 17,
1978; comments due, April 14, 1978.

ADDRESS: Interested persons are invited to review the rule and to submit comments (indicating docket No. R-0144) to Secretary, Board of Governors of the Federal Reserve System, Washington, D.C. 20551.

FOR FURTHER INFORMATION
CONTACT:

Thomas J. O'Connell, Counsel to the
Chairman, Board of Governors of
the Federal Reserve System, Wash-
ington, D.C. 20551, 202-452-2791.

SUPPLEMENTARY INFORMATION:

The Board believes that the following additional information with respect to the rule is in the public interest. Directors of Federal Reserve Banks are charged by law with the responsibility for supervising and controlling the operations of the Federal Reserve Banks, under the general supervision of the Board of Governors of the Federal Reserve System, and for assuring that the affairs of the Banks are administered fairly and impartially. The Federal Reserve Act provides that Reserve Bank directors will be selected with due consideration to the interests of various segments of the population and economy, thus assuring that the Federal Reserve System will receive the benefit of the experienced judgment of individuals from a broad spectrum of the communities that will be affected by actions of the System. For example, the Federal Reserve Act provides that each head office of a Reserve Bank will have nine directors. Three are designated class A directors and are required to be "chosen by and representative of" member banks of the Board of Governors System. Three are designated class B directors and are to be elected by the member banks; three are designated class C directors and are appointed by the Board of Governors. Both class B and C directors are to represent the public with "due but not exclusive consideration to the interests of agriculture, commerce, industry, services, labor, and consumers." All directors are to be chosen "without discrimination on the basis of race, creed, color, sex, or national origin."

The Federal Reserve Act contemplates that directors will be gainfully employed in several designated areas of endeavor, but will devote a portion of their time to Federal Reserve Bank functions. The amended 18 U.S.C. 208 makes applicable to Reserve Bank directors a standard of conduct formulated primarily for application to individuals serving the Federal government full time and generally with no other substantial occupation or calling. While it is the judgment of the Board of Governors that the ethical standards historically adhered to by the boards of directors of Federal Re-

serve Banks have been in accord with the spirit of 18 U.S.C. 208, the unique position of Federal Reserve Bank directors was felt to warrant formulation by the Board of Governors of principal standards, as set forth in this rule, under which any potential conflicts could be resolved in a manner consistent with the interests of the public, the Federal Reserve System, and the directors involved.

Pursuant to the authority contained in 5 U.S.C. 553(b)(B), this rule is being published as a final rule without prior general notice of proposed rulemaking, but with opportunity after receipt of comments for later amendments. The Board has for good cause found that this rule must be adopted immediately in view of the present applicability of 18 U.S.C. 208 to directors of Reserve Banks and the desirability of promulgating an immediately applicable rule for the guidance of such directors at this date. Interested persons are invited to review the rule and to submit relevant data, views, comments, or arguments in writing to the Secretary, Board of Governors of the Federal Reserve System, Washington, D.C. 20551 to be received not later than April 14, 1978. All material submitted should include the docket number R-0144. Copies of any comments received will be made available for inspection and copying upon request, except as provided in § 261.6(a) of the Board's Rules Regarding Availability of Information (12 CFR 261.6(a)). Consideration will be given to any comments received and the Board will amend the rule as determined necessary or desirable.

Title 12, CFR is amended by adding Part 264a to read as follows:

PART 264a—RESERVE BANK DIRECTORS—
ACTIONS AND RESPONSIBILITIES

Sec.

- 264a.1 Purpose.
- 264a.2 Definitions.
- 264a.3 Prohibition against Director participation in particular matters.
- 264a.4 Granting of ad hoc exemptions.
- 264a.5 Exemption of remote or inconsequential financial interests.

AUTHORITY: 18 U.S.C. 208, as amended by the Federal Reserve Reform Act of 1977, Pub. L. No. 95-188, sec. 205, 91 Stat. 1387; 12 U.S.C. 248.301.

§ 264a.1 Purpose.

Directors of Federal Reserve Banks are charged by law with the responsibility of supervising and controlling the operations of the Reserve Banks, under the general supervision of the Board of Governors, and for assuring that the affairs of the Banks are administered fairly and impartially. The Federal Reserve Act provides that Reserve Bank directors will be selected with due consideration to the interests of various segments of the population and the economy, thus assuring that

the Federal Reserve System will receive the benefit of the experienced judgment of individuals from a broad spectrum of the communities that will be affected by actions of the System. For example, the provisions of section 4 of the Federal Reserve Act, as amended by the Federal Reserve Reform Act of 1977, provide that both class B and C directors shall be chosen to represent the public and with "due but not exclusive consideration to the interests of agriculture, commerce, industry, services, labor, and consumers." Section 4 further provides that class A directors "shall be chosen by and be representative of the stockholding banks" of the Federal Reserve System. Recognizing that Reserve Bank directors may have, in their private capacities, business, consumer, or other interests to which legitimate attention is to be given; but recognizing also that these same individuals have fiduciary responsibilities as directors of Reserve Banks, this regulation is promulgated for the purpose of assuring preservation of and adherence to the intent of both the Federal Reserve Act and section 208 of Title 18, United States Code.

§ 264a.2 Definitions.

For purposes of this part, the following definitions shall apply:

(a) The term "director," unless otherwise indicated, means a head office or branch director of a Federal Reserve Bank.

(b) The term "Board of Governors" means the Board of Governors of the Federal Reserve System.

(c) The term "board" means the board of directors of a Federal Reserve Bank.

(d) The term "related person" means (1) a partner of a director, (2) any organization in which the director is serving as an officer, director, trustee, partner or employee, or (3) any person or organization with whom the director is negotiating or has any arrangement concerning prospective employment.

(e) The term "participate" means to act through decision, approval, disapproval, recommendation, the rendering of advice, investigation, or as is otherwise within the meaning of the provisions of 18 U.S.C. 208.

(f) The term "particular matter" means a judicial or other proceeding, application, request for a ruling or other determination, contract, claim, controversy, charge, accusation, arrest or other subject within the meaning of the provisions of 18 U.S.C. 208.

§ 264a.3 Prohibition against Director participation in particular matters.

(a) Pursuant to the provisions of 18 U.S.C. 208(a), no director may participate personally and substantially in a particular matter in which, to the di-

rector's knowledge, the director, the director's spouse or minor child, or related persons have a financial interest unless such action is otherwise permitted by 18 U.S.C. 208(b) and §§ 264a.4 or 264a.5 of this part.

(b) Except as provided by 18 U.S.C. 208(b) and §§ 264a.4 or 264a.5 of this part, no director shall participate in deliberations or decisions of a Reserve Bank board when the question presented is whether the board should approve or ratify an extension of credit by a Reserve Bank to a bank which is, in the opinion of the President of the Reserve Bank, in a hazardous financial condition, and

(1) Where the director has knowledge that he, his spouse, or minor child has a financial interest in the proposed transaction as a result of:

(i) Being a borrower or applicant for credit from the borrowing bank, other than consumer credit as defined in Regulation Z (12 CFR 226.2 (p));

(ii) Maintaining a depository relationship with the borrowing bank in an amount exceeding that covered by federal deposit insurance; or

(iii) Owning stock, stock options, bonds, notes or other forms of indebtedness issued by the borrowing bank, the market value of which exceeds \$100,000 or represents more than 1 percent of the value of that class of stock, stock option, bond, note, or other form of indebtedness issued by the borrowing bank.

(2) Where the director has a financial interest in the proposed transaction as a result of:

(i) Service by the director as an officer or director of the borrowing bank;

(ii) Service by the director as an officer or director of another bank that is known by the director to be located in the same geographic market for local banking services as the borrowing bank and is known by the director to be in direct and substantial competition with the borrowing bank;

(iii) Service by the director as an officer or director of another bank that is known by the director:

(A) To have outstanding or to be negotiating an extension of credit from, or to, the borrowing bank, other than federal funds or foreign exchange transactions; or

(B) To maintain a correspondent or depository relationship with the borrowing bank in an amount exceeding that covered by federal deposit insurance; or

(iv) Service by the director as one of the principal officers of any business enterprise that constitutes the director's primary business or professional occupation where such business enterprise is known by the director:

(A) To have outstanding or to be negotiating a direct extension of credit or direct line of credit from the borrowing bank;

(B) To maintain a principal depository relationship with the borrowing bank in an amount exceeding that covered by federal deposit insurance; or

(C) To own stock, stock options, bonds, notes or other forms of indebtedness issued by the borrowing bank, the market value of which exceeds \$100,000 or represents more than 1 percent of the value of that class of stock, stock options, bonds, notes or other form of indebtedness issued.

(3) Where the director has knowledge that a partner of the director has a financial interest in the proposed transaction; or

(4) Where the director has a financial interest in the proposed transaction as a result of the director's participation in current negotiations or arrangements concerning prospective employment with the borrowing bank.

(c) It is recognized that a Reserve Bank board can, within the spirit and letter of its responsibilities, delegate to appropriate officials of the Reserve Bank authority to act with respect to extensions of credit to individual banks determined to be in hazardous financial condition, thus avoiding both ratification by the Board and applicability to the directors of the prohibitions of this section. Such delegation would not preclude continued advice to the board of appropriate information regarding bank conditions in the district so as to enable the board fully to perform its general oversight responsibilities.

§ 264a.4 Granting of ad hoc exemptions.

(a) The prohibitions of 18 U.S.C. 208 and § 264a.3 of this part shall not apply if the director first advises the Board of Governors of the nature and circumstances of the particular matter before the board and makes full disclosure of the financial interest involved and receives in advance a written determination made by the Board of Governors, or its designee, pursuant to 18 U.S.C. 208(b)(1), that the interest is not so substantial as to be deemed likely to affect the integrity of the services which the Federal Reserve System may expect from such director.

(b) Telegraphic communications from the President, First Vice President, Secretary or General Counsel of a Reserve Bank to the Board of Governors on behalf of a director and setting forth the precise nature of both the particular matter before the board and the financial interest involved shall be considered to meet the director's duty of full disclosure set forth in paragraph 264a.4(a). Telegraphic response to the same identified officials of the Reserve Bank by the Board of Governors, or its designee, shall be deemed to meet the requirement of a written determination by the Board of Governors set forth in paragraph 264a.4.

§ 264a.5 Exemption of remote or inconsequential financial interests.

(a) Pursuant to the provisions of 18 U.S.C. 208(b)(2), certain actions of directors of Federal Reserve Banks may be exempted from the prohibitions of 18 U.S.C. 208(a) and § 264a.3 of this part, if by general rule or regulation published in the *FEDERAL REGISTER*, the financial interest involved has been determined to be too remote or too inconsequential to affect the integrity of directors' services. Financial interests will be viewed as too remote or too inconsequential:

(1) In circumstances in which a director's action on a matter will not directly, substantially, and predictably affect the financial interest; or

(2) In circumstances in which a director's independence of judgment will not be affected by the financial interest.

(b) The Board of Governors has determined that the financial interests of a director, the director's spouse or minor child, or related persons in the following matters are too remote or too inconsequential to affect the integrity of directors' services and, accordingly, the prohibitions of 18 U.S.C. 208(a) and § 264a.3 of this part shall not apply to a director's participation in such matters:

(1) Deliberations concerning and ratification of ordinary and routine extensions of credit to a member bank that have previously been made by officials of the Reserve Bank under appropriate provisions of the Federal Reserve Act, regulations and policies of the Board of Governors and the Federal Reserve Banks, and the established operating procedures at the director's Reserve Bank;

(2) Deliberations concerning or affecting a financial institution, to the extent the financial interest in such matters results from:

(i) Maintenance at the financial institution of a checking or other deposit account covered by federal insurance;

(ii) A fiduciary relationship involving the utilization of the financial institution's trust or investment advisory services;

(iii) The receipt from the financial institution of consumer credit, as that term is defined in Regulation Z (12 CFR 226.2(p)); or

(iv) Participation in federal funds or foreign exchange transactions with the financial institution;

(3) Deliberations concerning or affecting a financial institution or other enterprise to the extent the financial interest results from ownership of stock, stock options, bonds, notes, or other forms of indebtedness, the market value of which is less than \$100,000 and represents less than 1 percent of the value of that class of stock, stock option, bond, note or other form

of indebtedness issued by the financial institution or other enterprise.

(c) Section 264a.3(b) of this part specifically identifies certain financial interests, the existence and knowledge of which will preclude a director from participating in deliberations or decisions of a Reserve Bank board (except through recourse to the procedures set forth in § 264a.4) when the question presented is whether the board should approve or ratify an extension of credit by a Reserve Bank to a bank which is, in the opinion of the President of the Reserve Bank, in hazardous financial condition. Financial interests identified in § 264a.3(b) are viewed by the Board as offering a clear potential for conflict. The Board has determined that any other financial interest that a director, the director's spouse or minor child, or related persons may have in such extensions of credit to banks in hazardous condition are too remote or too inconsequential to affect the integrity of directors' services and, accordingly, the prohibitions of 18 U.S.C. 208(a) and § 264a.3 of this part shall not apply to a director's participation in such matters. These would include, for example, financial interests that might result from:

(1) A director's ownership of stock of a bank or business that may have an interest in the condition of the borrowing bank; or

(2) A director's service as a director or trustee of a business or other organization, other than a bank, that may, itself or through a subsidiary, have an interest in the condition of the borrowing bank.

(d) The functions of directors often include their participation in discussions concerning (1) international, national, and regional economic and financial conditions, (2) monetary policy, (3) general conditions, trends or issues with respect to bank credit, (4) establishment of rates to be charged for all advances and discounts by Federal Reserve banks, subject to review and determination of the Board of Governors pursuant to the Federal Reserve Act, and (5) statutes and proposed or pending legislation in which the Federal Reserve System has a legitimate interest. The foregoing matters are not particular matters of the type described in 18 U.S.C. 208 and, therefore, that statute is not applicable to participation in such matters. However, even if the statute were held to be applicable to participation in such matters, the Board of Governors has determined that the financial interests of a director, the director's spouse or minor child, or related persons in such matters are too remote or too inconsequential to affect the integrity of directors' services and, accordingly, the prohibitions of 18 U.S.C. 208(a) and § 264a.3 of this part shall

not apply to a director's participation in such matters.

(e) Nothing in this section shall preclude a director from refraining, to the extent consistent with responsibilities imposed upon the directors by the Federal Reserve Act, from participation in a particular matter. The Board hereby gives notice of its intention to undertake a continuing review of the experience of Reserve Bank boards under this regulation with a view to assuring preservation of and adherence to the intent of both the Federal Reserve Act and 18 U.S.C. 208, as amended. In the course of such review, particular attention will be given to the provisions of this section.

NOTE.—A Guide to Conduct for Directors of Federal Reserve Banks and Branches of Federal Reserve Banks appears in the Notices section of this issue of the *FEDERAL REGISTER*.

Board of Governors of the Federal Reserve System, February 17, 1978.

THEODORE E. ALLISON,
Secretary.

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serve directors should be guided by the following principles.

(1) Directors of Federal Reserve Banks, in carrying out their System responsibilities, should avoid any action which might result in or create the appearance of:

(a) Using their position as director for private gain,

(b) Giving unwarranted preferential treatment to any organization or person,

(c) Impeding System efficiency or economy,

(d) Losing complete independence or impartiality of action,

(e) Making a decision as a director outside of official System channels, or

(f) Affecting adversely the confidence of the public in the integrity of the Federal Reserve System.

(2) Directors should strictly preserve the confidentiality of System information that, if revealed, could inure to the private benefit of any person or organization or could impair or compromise the effectiveness of System operations and policies. In public speeches and communications, directors should avoid statements that suggest the nature of any monetary policy action that has not been officially disclosed.

(3) Class C directors are prohibited by the Federal Reserve Act (12 U.S.C. 303) from owning stock of any bank. In furtherance of the intended purpose of this prohibition, as a matter of System policy, class C directors appointed or reappointed following adoption by the Board of Governors of this Guide should also refrain from ownership of stock of a bank holding company. Directors should consider the stock ownerships of a spouse or minor child living at home to be their ownerships. Interests held or acquired by a class C director in a bank holding company, and interests held or acquired by the director's spouse or minor child in a bank or bank holding company should be promptly disposed of unless, after full disclosure to the Board of Governors or its designee, it is determined that retention of such stock would not, in the circumstances presented, significantly conflict with the underlying philosophy of the Act. Nothing set forth in this paragraph should be viewed as precluding a class C director from investing or participating in a diversified mutual fund, investment company, or other form of investment plan whose management may from time to time direct the purchase of stock, ownership of which is otherwise precluded by this paragraph, provided that the class C director's role is that of a passive investor and the director does not contribute in any manner to the investment decisions.

NOTE.—A regulation relating to directors of Federal Reserve Banks has been adopted

by the Board of Governors pursuant to 18 U.S.C. § 208 and appears in the Rules and Regulations section of this issue of the **FEDERAL REGISTER**.

Board of Governors of the Federal Reserve System, February 17, 1978.

THEODORE E. ALLISON,
Secretary.

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[6210-01]

**DIRECTORS OF FEDERAL RESERVE BANKS AND
BRANCHES OF FEDERAL RESERVE BANKS**

Guide to Conduct

Directors of Federal Reserve Banks have a special obligation to maintain the integrity and reputation of the Federal Reserve System. In their capacity as directors, these individuals are changed by law with the responsibility of supervising and controlling the operations of the Reserve Banks, under the general supervision of the Board of Governors, and for assuring that the affairs of the Banks are administered fairly and impartially. Chosen, as they are, from diverse segments of the community at large, directors are expected to bring to their deliberations the benefit of experienced judgment and advice on specific matters within their respective districts and on other general issues confronting the System as a whole. To assure the proper performance of System business and the maintenance of public confidence in the System, it is essential that directors, through adherence to high ethical standards of conduct, avoid actions that might impair the effectiveness of System operations or in any way tend to discredit the System. Therefore, Federal Re-