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STATEMENT

by

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CHAIRMAN

of the

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

before the

Subcommittee on Federal Spending Practices

and Open Government

of the

Committee on Governmental Affairs

UNITED STATES SENATE

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The Board's effective consideration of many issues in the financial and supervisory area has also been enhanced by the authority to use minute entry summaries, rather than a verbatim recording, for agenda items closed under several of these exemptions. This has encouraged a continuation of the free and open discussion of sensitive matters that is so important to the deliberations of a collegial body such as the Board. Later, two additions will be suggested to those subjects for which minutes may be used where the Board believes free discussion has been somewhat impeded by the current recording requirement.

Also, the authority to close meetings dealing with recurring items under certain exemptions by regulation rather than by requiring individual advance vote -- the so-called "expedited procedures" provision -- has simplified the Board's operations under the Sunshine law, without any disadvantage to the public.

Expedited Procedures

The Board's regulation provides for a meeting to be closed by a vote of at least four members at the beginning of the meeting if the subjects to be discussed fall within specified exemptions. Typically, such closed meetings deal with subjects involving monetary policy matters, such as the setting of discount rates, use of the discount window, changes in the limitation on payment of interest on time and savings accounts, and changes in

reserve requirements or margin regulations; proposals involving a specific bank or bank holding company formation or further bank acquisition; other bank regulatory matters such as applications for membership, issuance of capital notes, and investments in bank premises; foreign banking matters; and bank supervisory and enforcement actions, such as cease and desist and officer removal proceedings.

In adopting the Board's regulation providing for the use of expedited procedures, it was ascertained that of the 493 meetings of the Board held in the three calendar years prior to enactment of the Sunshine law, 94 per cent could have been properly closed pursuant to exemptions that would sanction use of these procedures. Because of the nature of the Board's activities and the nature of the exemptions that authorize the use of expedited procedures, it may be expected that a substantial percentage of the Board's agenda items will continue to be closed under this procedure.

Board Record of Open and Closed Meetings

Operating under the Government in the Sunshine Act during 1977, 27 per cent of the Board's 114 meetings were either open or the Board's 114 partially open. At these meetings the Board considered 638 individual agenda items, of which 17.5 per cent were open and 82.5 per cent closed. As to many of the closed items, tape recordings of

the Board's discussions were placed in the Board's Freedom of Information Office soon following the meeting, thus making these discussions available to the public. Taking the release of these recordings into account, another 5.3 per cent of the items considered by the Board in 1977 are now open to the public.

For 1978 through June 30, 43 per cent of the Board's meetings were either open or partially open. The Board has considered a total of 377 agenda items during this period; 26 per cent in open sessions, and 74 per cent in closed meetings.

Open Meeting Procedures

The Board has put a good deal of effort into developing a program to aid the public in understanding and obtaining the maximum possible benefit from its open meetings. A pamphlet has been prepared to increase the public's understanding of the application of the Sunshine Act to the Board's meetings. A copy is attached to this statement.

The Board makes most staff memoranda considered at open meetings available to the public upon request submitted prior to the meeting. Such requests are given priority treatment by the Board's Secretary. Before presentation of an item on the agenda at an open meeting, a brief statement of the issues involved is usually made for the benefit of the public. Members of the public attending the meeting are provided with an agenda

summarizing the issues to be discussed. An example is attached to this statement. Photographs of Board Members and seating charts are available in the Board room. Following each meeting a representative of the Public Affairs Office is available for further questioning about the proceedings. In short, the Board endeavors to help the public understand the proceedings at open meetings.

Twenty-five persons attended the first open meeting of the Board on March 28, 1977. Since then attendance has varied widely, depending on the public interest in the subjects to be considered. Attendance was large at one recent meeting in which the Board's proposed membership program, the proposed Community Reinvestment Act regulation, and aspects of the International Banking Act legislation were considered. That meeting was attended by about 85 members of the public. Otherwise, attendance has ranged from 0 to 39, averaging 9 a meeting.

The Board maintains a mailing list for notices of meetings. In addition to printing notices in the Federal Register, the Board makes advance notices of meetings available to the public at the Board's Freedom of Information and Public Affairs Offices and at the Treasury Department's press room. Also, notices of open meetings are provided to a news wire service for use on its Washington "city wire." All notices invite the public to address inquiries to the Board's Public Affairs Office, which is prepared to provide details about any meeting. In the event of an unexpected change in an

open agenda item, when advance written notice is unlikely to be received in time by the public, media representatives who regularly attend such sessions and individuals known to have an interest in particular matters on the Board's agenda are advised of the change by telephone. When the change is significant, calls are also made to each of the persons on the Board's Sunshine mailing list -- approximately 40 in number.

Records of Meetings

As indicated earlier, the Board has also made a conscientious effort to comply with the spirit of the Sunshine Act with respect to the availability of minutes, transcripts, and recordings.

The record of each closed Board meeting is made available to the public in the Board's Freedom of Information Office promptly after the meeting, unless the Board has voted to withhold part or all of the discussion under the Act's exemptions. For closed meetings there are either minutes, or recordings which may be listened to by members of the public. Transcripts of recordings can be obtained upon request. Cover sheets attached to the released material indicate whether the entire record is available and list any subjects withheld. Material that is withheld temporarily is released as soon as it is determined that the exemptions under which it was withheld no longer apply.

The public may come into the Freedom of Information Office and obtain immediate access to pertinent files, minutes and records.

Costs of Government in the Sunshine

While we have endeavored to maximize the benefits to be derived from implementation of the Act, it should be noted that such efforts are not without associated costs. We have had to reassign resources within our staff so that two persons now work solely on Sunshine matters, one processing public announcements and the other processing the recordings and minutes of closed meetings. In order to meet our open meeting and recording obligations, it has been necessary to install a public address and multi-track recording system at a substantial cost to the Board. Compliance with the substantive and technical requirements of the Act continues to place heavy additional demands on staffs of the Secretary, the General Counsel's office and others. We estimate that the cost to the Board of complying with the Sunshine Act is approximately \$100,000 per year.

Another cost, of a somewhat different nature, but of particular concern to me, relates to the delay in processing of matters before the Board as a result of compliance with procedural requirements of the Act. For instance, some items which prior to the Act were brought to the Board at a moment's notice are now delayed as much as two weeks to accommodate the Sunshine public notice and voting requirements. Items ready for Board action at

an open meeting have been deferred in order that a grouping of such matters may be presented at one open meeting, rather than requiring the public to attend a series of meetings, each with only one or two open items on the agenda. The Board continues to consider appropriate steps that might be taken to minimize such delay.

Suggested Amendments to the Act

The Board has previously written to you about its concern as to any requirement that the Board's discussion of legislative matters be held in open meetings prior to their presentation to the Congress. It is the Board's belief that Congress dealt with this question by adopting exemption (9)(B) under which an agency's deliberations may be closed if public discussion would make known information, the premature disclosure of which would be likely to frustrate significantly implementation of a proposed agency action. Two reasons support closing of legislative items on the basis of this exemption.

First, the legislative process usually contains elements of negotiation and compromise, and premature disclosure of positions on legislative matters could significantly frustrate the attainment of legislative goals sought by an agency. Discussion of legislative matters often involves the consideration of strategy to be pursued in the accomplishment of legislative objectives favored by the Board.

For example, the Board may decide to support a particular legislative proposal but determine at the same time to support various alternative proposals should the Board's preferred position prove unacceptable to the Congress. Premature disclosure of the fact that the Board is willing to support alternative proposals could significantly frustrate the Board's ability to obtain support for its primary objective.

Second, Congress often expects that views on legislative matters will first be given to Congress. The important working relationship between Congress and the agencies could be significantly frustrated if agency views on legislative matters were prematurely disclosed to the press and the public.

Nevertheless, the Board's application of exemption (9)(B) to legislative discussions has been questioned by parties asserting that it was improper to use this section to close a meeting considering testimony to be given to the Congress. For this reason, the Board urges your Subcommittee to take action in the form of either an amendment or a clear statement in support of the Board's interpretation.

Even if the authority to close the discussion of legislative matters under exemption (9)(B) is clarified, another basic problem remains of the inhibiting effect that a requirement for verbatim recording has on the Board's consideration of legislative matters. According to my colleagues on the Board, the free and

spontaneous exchanges that were formerly present in Board discussions of legislative matters have been somewhat constrained by the recording requirements for such a meeting. It would seem that the Board and other collegial agencies should be able to communicate to Congress positions that have been formulated during a meeting that has permitted uninhibited expression of each member's views. The public interest would not be harmed if agency deliberations were conducted in closed nonrecorded sessions where the results are later exposed to the public in the course of committee hearings. The Board recommends that the law be amended to permit legislative discussions to be subject only to the maintenance of minutes.

Discussion of sensitive personnel matters has also been hampered by the Act's recording requirements. Board members, meeting in collegial fashion, cannot be expected to express in complete candor their views regarding candidates for senior Federal Reserve positions, when each word spoken is recorded. The creation and retention for at least two years of substantial numbers of recordings reporting such sensitive deliberations seems unwise and, moreover, unnecessary. Accordingly, the Board also recommends that the Act be amended to enable an agency to discuss individual personnel matters in closed session subject to the maintenance of minutes rather than the verbatim transcript or recording now required.

Mr. Chairman, I assure you that the Board intends to continue to carry out the letter and spirit of the Government in

the Sunshine Act to the best of its ability. I hope these comments have been responsive to the Subcommittee's request, and I will be pleased to answer any questions you may have.

Attachments

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Open Meeting Agenda

Wednesday, May 10, 1978

1. Summary Agenda: Because of its routine nature, no substantive discussion of the following item is anticipated. Summary agenda items are generally resolved on the basis of the written documentation without detailed discussion by the Board members. Typically, staff recommendations are uniform and in accord with established policy. Questions may be asked by Board members, but if any Board member wishes to express a substantive view on the merits of a proposal, the item is moved to the regular discussion agenda.

Summary Item 1(a):

Proposed interpretation of Regulation A (Extensions of Credit by Federal Reserve Banks) to provide that a bankers' acceptance secured by a field warehouse receipt covering readily marketable staples is eligible for discount by a Federal Reserve Bank, despite the fact that the warehouseman is an employee of the owner of the goods.

Reserve Bank loans to member commercial banks, known as discounts, must be secured by collateral deemed "eligible" for discount by specific Board action. Recently, the Board was asked to review its 1933 interpretation concerning the eligibility for discount of bankers' acceptances secured by field warehouse receipts. Under that interpretation, such acceptances were determined to be ineligible for discount because the actual custodian of the goods was so closely identified with the owner of the goods that, in the Board's view, the lending bank's security might be impaired. A review of the 1933 interpretation seemed desirable because of changes in commercial practice and law in the 44 years since its adoption. Furthermore, under the Board's Regulation D (Reserves of Member Banks), the sale of ineligible acceptances by member banks results in additional reserve liability for the member bank, thereby making the question of ineligibility of significance to member banks.

A proposed interpretation reversing the 1933 position of the Board was issued for comment in December 1977. Of the 23 comments received, all but two favored adoption of the proposed interpretation. As a result of the comments received, certain technical changes have been made to the proposed interpretation, but the final edition is essentially the same as the proposed.

Staff is recommending approval of the proposed interpretation.

2. Discussion Item:

Proposal for a Uniform Interagency Bank Rating System (UIBRS) to evaluate and rate commercial banks.

After extensive discussions among staff of the Federal bank regulatory agencies, preliminary agreement on the key performance dimensions of commercial bank operations has been reached. The proposed UIBRS describes a general framework for a uniform approach to rating banks. It was designed to measure the quality of a bank's operating performance and reflect in a comprehensive manner the institution's overall financial condition.

UIBRS builds upon and improves the present Federal Reserve approach to rating banks by explicitly including earnings and liquidity as components in the evaluation of a bank's performance, in addition to capital, asset quality and management. UIBRS also sets forth the important judgmental considerations and essential factors that must be weighed in the process of assessing each of these performance dimensions as well as in assigning a composite rating. The proposed system expands the performance gradation scheme to allow the rating of each individual dimension of a bank's operating performance on a scale of one to five. Finally, qualitative criteria are described for five distinct composite categories which relate the degree of supervisory concern to the seriousness of an institution's problems. Common use of these five composite categories among the agencies will introduce an important element of uniformity into the rating of banks and enhance interagency communication with respect to individual institutions.

Staff is recommending approval of the Uniform Interagency Bank Rating System.

3. Discussion Item:

Proposal to publish for comment an amendment to Regulation Y to permit bank holding companies to underwrite property and casualty insurance related to extensions of credit.

The performance of this activity by bank holding companies is not included among those that have been designated by the Board in Section 225.4(a) of Regulation Y (Bank Holding Companies) as "closely related" to banking. The discussion at this meeting should focus on whether there is sufficient basis to consider property and casualty insurance underwriting as closely related to banking and whether to publish a proposal for comment that would add this activity to the list included in Regulation Y.

The Board's staff is divided in its recommendation. The Division of Banking Supervision and Regulation and the Legal Division, although not making a final determination at this time, believe there is evidence that underwriting property and casualty insurance that protects collateral related to extensions of credit is an activity closely related to banking.

The Division of Research and Statistics, however, recommends that the Board not propose property and casualty insurance underwriting as a permissible activity for bank holding companies under Section 4(c)(8). Staff believes the underwriting of property and casualty insurance is an activity which is only marginally related to banking, and that there are no functional or historical reasons to consider the activity to be bank related.

4. Discussion Item:

Proposed amendments to Regulations G (Securities Credit by Persons Other Than Bank, Brokers, or Dealers), T (Credit by Brokers and Dealers), and U (Credit by Banks for the Purpose of Purchasing or Carrying Margin Stocks) to provide that only those dealers submitting bid and offer quotations for a given stock to an automated quotation system will be counted as market-makers in determining whether a stock should be shown on the Board's list of Over the Counter margin stocks.

Since the early 1930's, the Federal Reserve has been directed by law to restrain the excessive use of credit for the purpose of buying securities. This is done by requiring that funds lent to acquire securities be a certain amount less than the market value of the securities. The difference between the credit value and market value of any security is the margin, which is normally expressed as a percentage. Margin requirements apply to certain securities traded on the over-the-counter market, as well as to securities listed on a national securities exchange. The Board publishes a list of covered over-the-counter stocks. One of the requirements for inclusion on the Board's list is that a certain number of dealers make bona fide bids and offers for such stock.

When the OTC list was first published by the Board in 1969 the "pink sheets" of the National Quotation Bureau were the only consistent source of the required price information. Since that time an automated quotation system, NASDAQ, has been developed to a point where price information on all stocks on the Board's list can now be obtained from it.

Information from the "pink sheets" is now duplicative of material from NASDAQ. Moreover, reviewing it requires an expenditure of staff and computer time no longer deemed necessary to complete the analysis required in surveying the stocks eligible for the Board's list. Accordingly, in March 1978, the Board issued for comment the proposed amendments to Regulations G, T, and U (docket no. R-0147) to permit the Board to use survey data from NASDAQ only. Of the fifteen comments received, all but one supported the Board's proposal. Staff is now recommending final adoption of the amendments as proposed.