A joint meeting of the Board of Governors of the Federal Reserve System and the Presidents of the Federal Reserve Banks was held at the Board's offices in Washington, D. C., on Tuesday, December 9, 1952, at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Evans
Mr. Vardaman
Mr. Robertson

Mr. Carpenter, Secretary
Mr. Kenyon, Assistant Secretary

Messrs. Erickson, Sproul, Williams, Gidney, Leach, Bryan, Young, Johns, Powell, Leedy, Gilbert, and Earhart, Presidents of the Federal Reserve Banks of Boston, New York, Philadelphia, Cleveland, Richmond, Atlanta, Chicago, St. Louis, Minneapolis, Kansas City, Dallas, and San Francisco, respectively

Mr. Heflin, Secretary of the Conference of Presidents

Before this meeting there had been submitted to the Board a memorandum listing the topics to be discussed at this joint meeting and stating the views of the Conference of Presidents with respect to each topic. The topics, the statement of the Conference of Presidents with respect to each, and the discussion concerning them at this meeting were as follows:

1. Discussion of recommendations contained in the Patman Subcommittee Report.

President Leach amplified the introductory paragraph contained in the Presidents' memorandum which read as follows:

The Presidents discussed the specific recommendations for legislation contained in the Patman Subcommittee report as well as the desirability of a Congressional directive concerning responsibilities of the System, the establishment, as recommended by Secretary Snyder, of a consultive and advisory council and the establishment of a commission to study various problems of the financial, monetary, fiscal and debt situation. The discussion was based, in large part, upon the draft statement of November 12, 1952, prepared for the Presidents by the Conference Subcommittee on Legislation, a copy of which is attached for the information of the Board.

The views of the Presidents on the several matters discussed are summarized briefly below.

a. Congressional directives or "mandates". Eleven of the twelve presidents were of the opinion that it would be desirable to seek to have incorporated in the Federal Reserve Act a better statement than now exists of the purposes and function of the Federal Reserve System, the exact wording of such a directive and the method of presenting it to the Congress to be the subject of further study and exploration by the Board and the Reserve Banks.

President Leach said that the Presidents, with one exception, felt that a better directive or mandate incorporated in the Federal Reserve Act would be helpful in providing an improved understanding of the purposes and functions of the System but that they recognized the difficulty involved in wording a mandate which would be appropriate in all circumstances and, at the same time, not be too rigid.

He then referred to three suggestions offered by the Subcommittee of the Committee on Legislation in its memorandum prepared for the Presidents. The first suggestion was to propose an addition of the words "and stability of the value of the dollar" to the Declaration of Policy in the Employment Act of 1946. The second was to insert a "declaration of policy" immediately after the preamble to the Federal Reserve Act, possibly along the lines of the declaration included in the House version of the Banking Act of 1935. The third was to include a longer but more explicit declaration, a possible wording of which was given in the Subcommittee's memorandum.

With reference to the first suggestion, President Leach pointed out that the Subcommittee thought the addition of such language to the Employment Act of 1946 would not be sufficient for the System's needs. He said that most of the Presidents would be prepared to accept something along the lines of the third suggestion of the Subcommittee.

President Leach observed that it was not the feeling of the Conference of Presidents that a mandate was necessary for carrying on the operations of the System but rather that it would be desirable to have one if it were phrased satisfactorily.

In response to a question by Governor Robertson whether eleven of the Presidents favored a mandate of the type of the Subcommittee's third suggestion, President Leach said that this suggestion met with a good reception but that the Conference did not adopt any specific suggestion.

President Williams inquired whether the Board felt that it would be desirable to go forward with a request for a mandate at this time. Chairman Martin responded that the Board had not yet gone into that matter, that he had no opinion at this time, but that he thought the Board might be in a better position to appraise the situation after the middle of January when the legislative program of the new Congress became more clearly indicated.

Concluding comments by President Leach were to the effect that in considering this and other recommendations in the Patman Subcommittee report, the Presidents had given primary consideration to what the position of the System should be, leaving the question of procedure for subsequent consideration.

> b. Advisory Council. The Presidents were opposed unanimously to the creation of an interagency consultive and advisory council as suggested by the Secretary of the Treasury. They also felt that there was danger in the creation of a consultive body of credit-granting or guaranteeing agencies in which the Federal Reserve would participate as one member. It was felt that such a body would create in another form the hazard of placing the System in a subordinate or minority position. The Conference was of the opinion that while there is much to be gained through efforts to bring the actions of these other agencies into consistency with general monetary and credit policy, there is the question as to whether the System should not proceed further with informal approaches on its own initiative. Closer liaison with various agencies, individually, would not seem to involve the same risks to the System's necessary autonomy and independence.

The members of the Board present indicated that they concurred in the views of the Presidents.

c. National monetary commission. The Presidents were of the opinion that the establishment of a commission to make a broad study of the American financial system would be desirable.

President Leach said that the Presidents had in mind that there had been many developments and changes since the study of the National Monetary Commission which preceded the creation of the Federal Reserve System, and that the studies since that time had been in special fields and had not covered the financial organization of the country as a whole. He mentioned in this connection that there was some thought that it might be desirable to have a commission, as in Canada, that would make a broad study periodically, perhaps every ten years.

President Sproul commented that the studies in recent years had been instituted at the request of individual Congressmen, usually with some particular purpose in mind, the result being a series of studies relating to certain aspects of the financial mechanism rather than the mechanism as a whole. He thought that if it were possible to establish a commission of the type envisaged, with provision for periodic review of the country's financial organization, there would be a better prospect for nonpolitical assessment of the situation.

In response to a question by Governor Robertson, President Sproul said he would prefer a commission composed of members of Congress and outside parties. President Leach said that no vote was taken on that point and that there might be some differences of opinion among the Presidents.

Chairman Martin then inquired whether the Presidents considered the establishment of such a commission to be a pressing matter, and President Sproul expressed the view that it would not necessarily be one of the first things to be proposed but that, if the idea of a broad study were suggested, he felt it might be accepted as a part of a legislative program.

Governor Vardaman commented that a proposal for a national monetary commission had been made by Mr. Winthrop W. Aldrich, Chairman of the Board of the Chase National Bank, several years ago, that Mr. Aldrich's plan as outlined to him seemed sound, that if the Board and the Reserve Bank directors sought the appointment of a commission he felt such a commission would be set up within a few months, and that in his opinion the Board and the Presidents should actively consider taking steps toward the establishment of such a commission.

President Williams then spoke of the need for an educational program which would lay the basis for a System request for a broad study of the country's financial structure. He felt that without this preliminary work there probably would be a misinterpretation of the System's interest among the bankers of the country, who would fear a disturbance of the status quo as a result of the study.

Governor Evans agreed that it would be unwise to proceed without giving careful thought to the matter and doing some educational work as suggested by President Williams.

> d. Nonmember bank reserves. The Presidents endorse in principle the recommendation that nonmember banks be required to maintain the same reserves as member banks. However, they do not feel that it is a pressing matter and, therefore, do not think that legislation for the purpose should be initiated by the System at this time.

President Leach said the Presidents recognized that extension of the System's authority over required reserves to all banks would increase the effectiveness of the System's monetary and credit policy but they would not recommend initiation of legislation at this time because of the controversy that would be aroused by such a move.

> e. Additional powers over reserve requirements. The Conference is of the view that additional powers over reserve requirements are not needed at this time. However, they feel that study of the uniform reserve requirement proposal should continue and that prompt consideration should be given to securing legislation which would permit vault cash to be counted as a part of member banks' required reserves with appropriate adjustments in reserve requirements.

President Leach said that a principal reason underlying the opinion of a majority of the Presidents that legislation should be sought which would permit vault cash to be counted as a part of member banks' reserves was that a substantial saving of time and money could be achieved by the Reserve Banks through a reduction of the shipments of currency between the Reserve Banks and the member banks. In addition, such a provision might make membership in the System a little more attractive. On the other hand, the Presidents recognized that it would be preferable to take such a step at a time when reserve requirements were being lowered as a part of the System's credit policy so that the adjustment to the new requirements could be easily made.

President Gilbert expressed the view that the matter of vault cash was only one phase of the whole problem of member bank reserves and it would be preferable to have a study of the entire question before determining the legislation that the System should propose.

> f. Franchise tax. The Presidents agreed that if legislation to reimpose a franchise tax on Federal Reserve Banks should be proposed, the System should not oppose it provided adequate provision is made for the surplus accounts of individual Reserve Banks. Some of the Presidents feel that the System should initiate legislation to secure reimposition of the tax.

Chairman Martin said that the Board had given consideration to whether the System should initiate legislation and whether, if legislation were introduced by others, the Board should oppose its enactment. The

Board's discussion, he said, took into account the various arguments for and against its taking either of the courses.

> g. <u>Taxation of Federal Reserve Bank stock</u>. The Conference, with one President dissenting, agreed that if legislation eliminating tax exemption of dividends on Federal Reserve Bank stock issued prior to March 28, 1942, should be proposed, the System should not oppose it. However, the Presidents felt that the System should not initiate such legislation.

President Leach said the Presidents felt the System had no responsibility to propose legislation to eliminate the tax exemption with respect to dividends on stock issued prior to March 28, 1942. However, the majority believed that if such legislation should be proposed by others, the System should not oppose its enactment.

Chairman Martin commented that the Board, after discussion of this matter, felt that the question was one for decision by Congress and the member banks.

> h. <u>Budgets and audits</u>. For the reasons set forth in the statement prepared by the Conference Subcommittee on Legislation, and in the statements of the Chairman of the Board of Governors and the Presidents in the Patman Committee hearings, the Presidents are strongly opposed to
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> (1) the submission of Board or Reserve Bank budgets to Congressional committees;
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> (2) the audit of the Board's accounts by the General Accounting Office;
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> (3) any compulsory audit of the Reserve Banks by outside auditors or the General Accounting Office.

In response to an inquiry by Governor Vardaman whether the Presidents would be as strongly opposed to a regulation issued by the Board of Governors providing for outside audits of the Reserve Banks as they would be to a legal requirement, President Leach said it was felt that a needless expense would be involved because there would be a duplication of the examinations conducted by the Board's staff.

Chairman Martin stated that the Board was undertaking to have Arthur Andersen and Co. audit the Board's accounts for the last nine months of 1952 and the year 1953.

At the request of Chairman Martin, Governor Robertson discussed the decision of the Board to have representatives of Arthur Andersen and Co. accompany the Board's examiners on one examination each year for the purpose of reviewing the adequacy of the examination procedures and determining whether the procedures were being carried out properly. In this way, he said, the Board would have an impartial opinion as to the adequacy of its examination procedures and would be prepared to defend them if necessary. He brought out that no audit of the Reserve Bank's accounts by the audit firm or actual participation by the firm in the examination would be involved, and that whether the arrangement would need to be continued for more than two or three years was a matter on which a decision would have to be made later.

During a discussion of the contemplated arrangement, one of the Presidents stated that his Bank would like to have the benefit of any observations which might be made by the audit firm concerning the Bank's auditing procedures, and it was suggested that any such observations might most appropriately be passed on to the Bank through the Board's staff.

> 1. Federal Reserve organization. The Conference Subcommittee on Legislation did not consider proposals affecting the size of the Board of Governors, salaries and terms of office of Board members and other matters directly relating to the Board, and no position was taken on these questions by the Presidents. If the Board wishes the views of the Presidents they would be glad to consider these matters and discuss them at a later meeting.

There was no discussion of this topic.

> 2. Borrowing by member banks from Federal Reserve Banks for the purpose of lessening or avoiding excess profits taxes. The Conference discussed at length the problem of member bank loan administration, including the tax considerations mentioned in the Board's letter of November 20, 1952. The Presidents reviewed their administrative responsibility in the field of loans and discounts to member banks and discussed loan procedure in their districts, illustrating it in some instances by reference to discount applications of specific banks. They keep in mind, among other things, the criteria mentioned in the Board's letter of November 20, but do not believe that any specific test or formula

would be satisfactory in all cases. In this connection the Presidents would be interested in any information the Board may have which reflects the experience or views of the Department of Internal Revenue with respect to allowing or disallowing such borrowings in determining excess profits tax liability.

President Leach reviewed the discussion by the Conference of the problem of loan administration, stating that the Presidents were aware of the possibility that some members were borrowing for the purpose of lessening or avoiding excess profits taxes, that they agreed this was not a proper purpose of borrowing, that the officers of a number of the Reserve Banks had conferred with member banks where there was reason to believe that such a practice was being followed, but that banks borrowed for combinations of purposes and it usually was not possible to prove conclusively that a bank was borrowing for excess profits tax purposes. He also said that the Presidents had in mind the various considerations which should guide their loan procedures, that the situation appeared to call for the exercise of judgment more than the establishment of any tests or formulas which would be applied in all cases, and that each application apparently must be considered on its own merit.

President Leach pointed out that there was some danger in fixing stringent lending standards because in some circumstances the

System would rather have member banks borrow than sell securities. He remarked that even if the excess profits tax should expire on June 30, 1953, banks would be able to derive a benefit from borrowing throughout the whole of that calendar year. In the circumstances, he felt that borrowing for excess profits tax purposes might come to light late in 1953.

Governor Robertson said it was his understanding, although he had not taken the matter up formally, that the Bureau of Internal Revenue had looked into some cases where it appeared that the purpose of borrowing might have been to avoid or lessen excess profits taxes but that the Bureau had not disallowed the borrowing in any case and that it did not intend to make a policy of investigating the purpose of the borrowing.

In the ensuing discussion, Chairman Martin alluded to the increased borrowing by member banks from the Federal Reserve Banks and stated that the Reserve Bank directors have a real responsibility in passing on such loans.

Several of the Presidents commented on the loan procedures followed by their respective Banks, on the extent of borrowing by certain groups of banks within their districts, and on the steps taken where it appeared that member banks were borrowing too freely.

President Young said that certain member banks in the Seventh

District had been obtaining renewals of 90-day advances made under the authority of the last paragraph of section 13 of the Federal Reserve Act on the security of United States Government obligations, that this practice had been discussed with two or three of the member banks, and that the Reserve Bank directors last week decided to follow a policy of making no further advances to member banks under this paragraph of the Act, thus forcing member banks to secure advances for periods not exceeding 15 days under the authority of paragraph 8 of section 13.

There followed a discussion of the effect of an increase in the discount rate upon borrowing by member banks and, although it was not felt that such an increase would discourage banks from borrowing for excess profits tax purposes, some of the Presidents suggested that a continuation of member bank borrowing at the recent level would make it imperative that serious consideration be given to discount rate policy.

President Leach remarked that it might be possible to obtain a better general picture of the situation in January following the period of seasonal borrowing and that if at that time the larger banks were continuing to borrow heavily, it might be well to give thought to a letter to the member banks regarding the appropriate purposes of borrowing from the Federal Reserve.

Chairman Martin referred to the discussion of discount rate policy at the meeting of the Federal Open Market Committee yesterday and stated the problem was one which merited continuous study by the members of the Board and the Presidents.

3. Payment by Federal Reserve Banks of notes of other Federal Reserve Banks. The Conference discussed the Board's letter of November 19, 1952, concerning the desirability of securing legislation to permit a Federal Reserve Bank to pay out notes of other Federal Reserve Banks. The Presidents wish to point out that this question was not considered on its merits at the September meeting of the Conference and that after full discussion of the matter at this meeting of the Conference they would favor repeal of the third and fourth sentences of paragraph 3 of Section 16 of the Federal Reserve Act to make it permissive for a Federal Reserve Bank to pay out notes of other Federal Reserve Banks.

President Leach indicated that, based on earlier estimates, the proposed change in the law might result in a saving to the System as a whole of as much as $750,000 annually.

President Bryan said it was important to keep in mind that a number of technical problems would be involved if the law made it compulsory for a Federal Reserve Bank to pay out notes of other Reserve Banks and for this reason he would not want to see the System propose any legislation until a statement had been prepared for the Congress discussing these points. He thought it would be a grave mistake, especially in view of the long-established tradition, to change the law except on a permissive basis under which the notes would remain the liability of the issuing Reserve Bank. President Bryan foresaw the possibility of a situation where a Reserve Bank might run short of reserves and would choose to restore its position by sending back notes of another Reserve Bank.

This concluded the discussion of the topics listed for consideration at this joint meeting.

Governor Robertson referred to his remarks at the joint meeting of the Board and the Presidents on September 26, 1952, concerning the program being formulated by an interagency committee consisting of representatives of the three Federal bank supervisory agencies to keep the banking system in operation in the event of an emergency. He said that a draft of the plans had been completed and that at a meeting last week of representatives of the three Federal bank supervisory agencies and the National Association of Supervisors of State Banks it was agreed that before submitting the draft to the National Security Resources Board it would be desirable to have the benefit of the views of the Reserve Bank Presidents, the members of the Federal Advisory Council, and representatives of the State bank supervisors and the American Bankers Association. After noting that the committee wished to have these comments by the end of the current month, Governor Robertson stated that at the conclusion of this meeting each President would be handed two copies of the statement of the program, one for his own use and the other for transmission to the member of the Council from his district with a request for his comments.

Question was raised whether the material should be handed to the outgoing or incoming member of the Council, in those districts where a new Councilman had been appointed for 1953, and Governor Robertson suggested that the matter be taken up with the individual now in office since his views were desired before the end of the year.

Governor Robertson also stated that although he had discussed the proposed program in very general terms with the Reserve Bank representatives who attended the recent meeting on emergency operations, it seemed desirable that the matter be kept confidential and that there be no discussion with other Reserve Bank personnel at this time, and that after the plans were submitted by the interagency committee a decision would be made whether the program should be given broader distribution. He further stated that the plan was to be submitted to a few of the State bank supervisors for comment but that he did not yet know the identity of that group.

Governor Robertson said that at the meeting of the interagency committee consideration was given to ways and means of getting the larger commercial banks to take proper precautionary steps to protect their assets, records, and personnel in the event of war emergency, it having been ascertained through a survey that relatively few of these banks appeared to have set up adequate programs. It was suggested, he said, that letters be sent to the larger banks requesting certain information but it was his opinion that, in lieu of such letters, it would be preferable as a first step for the Presidents or other senior officers of the respective Reserve Banks to discuss the matter personally with the commercial banks concerned. Governor Robertson stated that, if agreeable to the Presidents, the Board would send each President a letter indicating the commercial banks in his district which should be contacted and the information which the Board would like to have furnished to it regarding the programs of these banks.

Following a discussion, it was understood that the procedure suggested by Governor Robertson would be followed.

In response to an inquiry by President Williams whether there were any matters discussed at the Conference of Reserve Bank Chairmen in Chicago which might be commented upon at this time, Chairman Martin said that there had been consideration of the objectives, scope, and content of the public relations program of the System and that, while no formal action was taken, he felt that the exploration of the nature of the problem was quite helpful and that progress was being made, with an understanding that such a program would have to be carried out at the "grass roots". He added, however, that precise definitions of the concept of the problem must still be formulated.

Chairman Martin stated that the problems involved in Reserve Bank budget procedures also were discussed with the Chairmen, that their responsibilities for expenses in the light of the semi-public character of the Federal Reserve Banks were stressed, and that the Chairmen were requested to convey to the other directors of their Banks that they should approach the budgets on the basis that they might be called upon to justify them before a Congressional committee.

Chairman Martin then summarized the discussion with the Chairmen of the Board's desire to establish beginning with 1954 a policy of rotation of Class C directors under a plan whereby no director would be reappointed after serving two full terms of three years each unless he was then designated as Chairman and Federal Reserve Agent, in which event he might serve one more term for a total of not more than three full terms. Chairman Martin said that the Board was aware that the transition to this policy would involve certain problems and that it hoped these could be worked out satisfactorily.

President Bryan commented on the problems created by the policy being followed by the Federal Reserve Bank of Atlanta of limiting the service of directors appointed to its branch boards to one full term.

President Gidney said that the Cleveland Bank followed the policy of informing all branch directors when appointed by the directors of the Cleveland Bank that their service would be limited to one term.

Thereupon the meeting adjourned.

S. R. Carpenter
Secretary.