

Minutes of actions taken by the Board of Governors of the Federal Reserve System on Wednesday, March 16, 1955. The Board met in the Board Room at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Balderston, Vice Chairman
Mr. Szymczak
Mr. Vardaman
Mr. Mills
Mr. Robertson

Mr. Carpenter, Secretary
Mr. Sherman, Assistant Secretary
Mr. Kenyon, Assistant Secretary
Mr. Thurston, Assistant to the Board
Mr. Thomas, Economic Adviser to the Board
Mr. Vest, General Counsel
Mr. Young, Director, Division of Research and Statistics
Mr. Sloan, Director, Division of Examinations
Mr. Hexter, Assistant General Counsel
Mr. Masters, Assistant Director, Division of Examinations
Mr. Cherry, Legislative Counsel
Mr. Hooff, Assistant Counsel

Prior to this meeting there had been sent to the members of the Board copies of (1) a memorandum from the staff dated February 23, 1955, concerning the collective investment of trust funds, and (2) a supplemental memorandum from Mr. Vest to Governor Mills, dated March 2, 1955, concerning the Board's authority over the collective investment of such funds. The question dealt with in the February 23 memorandum concerned the right of a national bank to invest collectively, otherwise than in accordance with the provisions of section 17 of Regulation F, Trust Powers of National Banks, funds of pension trusts and profit-sharing trusts held

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by the bank in its fiduciary capacity. It resulted from the fact that section 10(c) of Regulation F provides that trust funds shall not be invested collectively except as permitted in section 17 of the regulation but section 10(a) provides that trust funds are to be invested in strict accordance with the instrument creating the trust. When this question was presented, the Board, by letters dated September 30, 1954, requested the views and suggestions of the Federal Reserve Banks, the Comptroller of the Currency, and the American Bankers Association; and, although there was a division of opinion, the majority of the replies took the position that a new provision should be added to section 17 of Regulation F so as to authorize separate trust funds composed of pension and similar trusts, under which provision some of the limitations presently contained in section 17, such as the \$100,000 limitation on the amount of the participation of any one trust, would not be applicable. However, for reasons stated in the memorandum, it was the unanimous recommendation of the Board's staff, after consideration of the various alternatives, that Regulation F should be amended so as to permit the collective investment of trust funds otherwise than under section 17 if such investment is specifically authorized by the trust instrument and if each of the trusts whose funds are collectively invested is a part of the pension, profit-sharing, or stock bonus plan of an employer for the exclusive benefit of his employees or their beneficiaries, of the type presently exempted from Federal income taxes under sections 401 and 501 of the Internal Revenue Code of 1954.

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At the request of the Board, Mr. Vest reviewed various aspects of the matter. During his statement he referred to the fact that the Office of the Comptroller of the Currency seemed to lean toward the view that collective investment of trust funds should not be permitted except as provided in section 17 of Regulation F, even if authorized by the trust instrument. He suggested, therefore, that if the Board approved the recommendation of its staff, the matter be discussed again with the Comptroller of the Currency in the interest of obtaining a reconciliation of views before publishing advance notice of any amendment to Regulation F in the Federal Register.

Mr. Vest went on to say that if the Board should decide to act on the basis of the staff recommendation, it might be well at the same time to recognize a situation where several trusts are created for members of the same family, or for similar purposes, and express authority is given for the collective investment of funds. He said it was the opinion of the staff that there was no substantial objection to the commingling of trusts in such cases, that some banks were understood to be following the practice, and that a permissive amendment to Regulation F would seem to be in order. In response to a question, he stated that the Board was not in receipt of a specific request for an amendment to Regulation F.

The members of the Board expressed themselves as favoring the staff recommendation with regard to pension trusts and profit-sharing

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trusts, although they felt that before placing an advance notice of amendment to Regulation F in the Federal Register, there should be consultation with the Office of the Comptroller of the Currency, as Mr. Vest had suggested. The only discussion of substance was occasioned by Governor Robertson's inquiry as to whether there should be exploration of the possibility of including a restriction against investing the trust funds involved in stock of another bank. It was the view of the staff that, although there was some possibility of potential abuse in this direction, a prohibition of the kind suggested, going into the field of a trustee's discretion in investing trust funds, would raise questions of precedent, equity (as between types of trusts and as between national and State banks), and perhaps the Board's authority under the statutes. In addition, Governor Mills mentioned indications that the Congress might within the near future investigate pension fund practices and consider legislative action.

With regard to the suggestion of the staff concerning the collective investment of family trusts, members of the Board noted that in the absence of a specific request for an amendment to Regulation F, the matter did not appear to be urgent. In the circumstances, they favored additional exploration of the problem by the staff, which would include consultation with the Office of the Comptroller of the Currency.

Thereupon, it was agreed unanimously that in the absence of objection on the part of the Comptroller of the Currency a notice would be placed in the Federal Register inviting the submission of views by interested parties concerning an amendment to Regulation F giving effect to the

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staff recommendation regarding the collective investment of pension, profit-sharing, and similar trusts, as set forth in the memorandum dated February 23, 1955.

Secretary's Note: Pursuant to this action, and it having been ascertained that the Comptroller of the Currency had no objection to the proposed amendment, an appropriate letter was sent to the Federal Register on March 21, 1955. In this connection, a letter reading as follows was sent to the Presidents of all Federal Reserve Banks on the same date, along with somewhat similar letters to the Comptroller of the Currency and to Mr. Joseph H. Wolfe, Secretary, Trust Division, American Bankers Association, New York, New York:

You will recall that the Board's letter of September 30, 1954, requested your views and suggestions with respect to the collective investment by national banks, otherwise than in accordance with the requirements and limitations contained in section 17 of Regulation F, of trust funds established by settlor corporations to provide retirement benefits for employees.

After careful review of the Reserve Banks' replies to that letter and of views expressed by the Comptroller of the Currency and the American Bankers Association, the Board proposes to amend section 10(c) so as to permit the collective investment of funds of trusts which are established under employers' pension, profit-sharing, or stock bonus plans without requiring compliance with the provisions of section 17, provided each such trust is exempt from Federal income taxes and the collective investment is specifically authorized by the trust instrument or by court order. It is believed that there is a distinction between such trusts, which usually are established by corporate settlors, and the generality of trusts, which will continue to be subject to the protective requirements of section 17 when invested collectively.

A draft of the proposed amendment is attached. Publication of this amendment in the Federal Register will allow interested persons sufficient time to submit relevant data, views, or arguments thereon. It is requested that you transmit to the Board any comments or views which may be submitted

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to you by banks or other interested persons concerning the proposed amendment to the regulation.

The Board appreciates your views and suggestions, which were of great assistance in arriving at its decision in this matter.

Messrs. Hexter, Masters, and Hooff then withdrew from the meeting and Mr. Leonard, Director, Division of Bank Operations, entered the room.

At the meeting of the Reserve Bank Presidents with the Board on March 3, 1955, it was stated that the Presidents' Conference had approved a memorandum entitled "Basic Objectives of the Research Function in Federal Reserve Banks", in the form submitted with a memorandum dated February 15, 1955, from the Conference Committee on Research and Statistics. The Board stated at that meeting that it would give further consideration to the statement and that the Presidents would then be advised of the Board's views. Accordingly, copies of the statement had been distributed to the members of the Board and it was brought up for consideration at this meeting.

Governor Mills recalled that the statement of basic objectives of the research function grew out of the report of the Coleman Committee on Federal Reserve Bank budget procedures. One of the recommendations in that report was that a statement be developed which would provide a framework for budgetary consideration of the research function. He said that a number of drafts had been prepared before the statement was approved by the Presidents' Conference.

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In response to a question by Governor Vardaman as to how it was intended that the statement would be used, Mr. Carpenter stated that if approved by the Board, the Reserve Banks would be notified and the statement then would provide a broad basis on which the Reserve Bank directors would consider the budgets for research at the respective Banks.

Mr. Leonard pointed out that Reserve Bank expenses in certain fields are considered to be covered by policy determinations rather than by any mathematical formula. Therefore, it was proposed that a statement be worked out which could serve as a guide to the Banks and to the Board in considering programs and expenditures related to the research function. He said that such a statement would not be considered a permanent document but would be revised and adjusted from time to time. The attempt, he said, was to have some meeting of the minds as to appropriate Federal Reserve activities in the field of research; in other words, a broad definition of the Federal Reserve Bank's area in the whole field of research.

Governor Mills commented that within the broad framework for research and statistical studies provided by this statement, there would continue to be specific control of expenditures through the usual budget procedures.

Following several comments concerning ways in which the statement might have been strengthened or otherwise improved, Chairman Martin said if the statement were going to be considered as a permanent "constitution" for the research function, he also would have suggestions for changes in

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it, but that as he understood the matter, it was merely for the guidance of the Board and the Federal Reserve Banks in reviewing the Banks' research budgets. In the circumstances, he suggested that the statement be approved by the Board.

Thereupon, the statement of basic objectives of the research function, reading as follows, was approved unanimously, with the understanding that, as stated by Chairman Martin, it would serve as a guide for budgetary purposes and would not constitute a document prescribing rigidly the scope of the research activities, and with the further understanding that an appropriate letter concerning the Board's action would be sent to the Federal Reserve Banks:

If the Federal Reserve System is to perform its lawful function successfully, it must form its judgments and make its policy decisions on the basis of the best and most pertinent economic information obtainable as analyzed and interpreted by technically competent personnel. The basic objective of the research function, both at the Board and in the several Federal Reserve Banks, is to provide such a factual, analytical, and interpretative foundation for Reserve Bank and System action.

The research function is not synonymous with the work of a Research Department. Although a Research Department may be presumed to devote its resources primarily to the discharge of the research function, this function may, in practice, be shared by other departments in a Bank. Conversely, a Research Department may be assigned any duties that a Bank's administration sees fit, whether they pertain to the research function or not.

The special characteristics of the research function in the Federal Reserve System grow out of the special characteristics of the System itself. The System is the nation's monetary authority and is endowed by law with certain powers by which it can influence the supply, cost, and availability of credit for the purpose of producing beneficial effects in the nation's economy at large.

The pursuit of this general objective makes it necessary that the Board of Governors of the Federal Reserve System and

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each Federal Reserve Bank engage in a program of economic research to which there are no a priori limits, but only those imposed by canons of good judgment as to the value of the results in relation to the cost.

The basic objective of the research function, i.e., to provide the broad foundation of economic information and analysis needed for intelligent policy action, is quite general in character. In practice it resolves itself into the equally basic but more specific objective of developing a flow of statistical data and a fund of analytical and interpretive material in those special areas of investigation that are particularly important to the System in the discharge of its legal responsibilities.

- 1) The first area is central banking, a field that is concerned with the System's monetary function. The theoretical problems inherent in the nature of the System powers; the applicability of those powers, severally or collectively, and their relative efficacy in various economic contexts; the effects actually produced by their exercise; and the problems of their administration, must all be matters for continuous study, not only by the Board's staff, to assist the Board in the discharge of its responsibilities, but also by the staffs of the Banks to assist the presidents and directors in the discharge of their responsibilities.

Since the Federal Reserve System must work through the mechanism of the commercial banking system and the money markets, the continuous study of the characteristics and activities of these parts of the nation's financial apparatus is a necessary corollary of central banking research.

- 2) A second area of research consists in the development, maintenance, improvement and analysis of a sufficient number of significant statistical series to depict adequately current economic conditions and trends and current monetary and credit conditions and developments. The analysis of such information should provide the basis for conclusions as to the adequacy of bank credit for the sound growth of the economy and as to the need for Federal Reserve action to restrain developments in bank credit which may threaten to endanger the stability of the economy, or to promote developments which may foster such stability.

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3) A third area of research is the analytical and interpretive study of the economies of the various Federal Reserve Districts. Statistics seldom carry their own explanation on their face. They are designed to answer the questions "what" and "when". For better understanding, however, they should be supplemented by studies answering "why" and "where". The dissimilarity in the economies of the various Districts; their different rates, patterns, and directions of economic development; their different degrees of responsiveness to general economic changes; and the varying impact of System policies within these different regional settings are all matters of which policy makers should be fully aware. In addition there is an implied legal responsibility, which flows from the structure of the Federal Reserve System, for the Reserve Banks to be thoroughly conversant with the availability of bank credit within their own districts and of the determinants of that availability.

This area of research, however, should not be thought of as restricted to analyses of regional economic developments, but should be defined as including the continuous analysis and study of general economic conditions both in their regional and national aspects and, where pertinent, in their international aspects as well.

The information and analyses developed by a Federal Reserve Bank in discharging its research function are not meant to lie dormant. They are meant to be serviceable to the Board of Governors, to the officers and directors of the Bank, to the business community, the general public, and to certain specialized groups such as the professors of money and banking in colleges and universities.

Although the task of disseminating economic information is not a logically necessary part of the research function, it is, nevertheless, a function in which research personnel are particularly well-qualified to share because of their contacts with those persons and agencies who provide them with economic data and information as well as with those who make use of the product of their research activity.

At this point Mr. Johnson, Controller, and Director, Division of Personnel Administration, entered the room.

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Governor Mills referred to the authorization given to him at the meeting of the Board on February 23, 1955, to proceed with arrangements for a meeting of Reserve Bank discount officers. He said that a letter had gone forward on March 11 to Mr. Young, Chairman of the Presidents' Conference, suggesting that such a meeting be held in Washington, D. C., on April 26 and 27, 1955, and submitting a list of items which might be included in the agenda.

Governor Mills then referred to the request made at the meeting on March 10, 1955, that he discuss with Mr. Thurston the current policy relating to articles written by members of the staff for outside publication. He said that the matter had been the subject of discussion and that a memorandum of policy and procedures had been drafted which largely restated and reaffirmed the procedure now in effect. It was his recommendation that the memorandum be approved.

Thereupon, unanimous approval was given to the memorandum referred to by Governor Mills, which was as follows:

OUTSIDE PUBLICATION OF STAFF ARTICLES

It will be helpful to division heads if the Board will take the present occasion to reaffirm or modify the policy concerning articles written by the staff for outside publication which has been followed since the spring of 1949 when the matter was last discussed by the Board.

Under this policy staff members have written articles about the Federal Reserve System and its functions, or articles growing out of their staff work on other economic and technical subjects, for professional or technical publications (with no fee). In the usual case, articles offered for outside publication have had the benefit of reading and

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criticism by staff associates and division officers, and have been revised in the light of suggestions received. In the Division of Research and Statistics the articles have then been given a concluding professional review by Miss Burr on the director's behalf and in the Division of International Finance by Mr. Dembitz. After this the articles have been submitted to Mr. Thurston for his review and judgment. From time to time, Mr. Thurston has referred articles to other staff officers for their reaction and advice. But as a practical matter, the final determination for outside publication has been made by Mr. Thurston and the division officer through which the article has been submitted.

In our experience this procedure has assured the desired review as to subject, competence of technical treatment, and substance. It has also made certain that the article was brought to the attention of Mr. Thurston for determination as to outside publication.

The question of publication by our professional staff has a vital bearing on maintenance of the top-level quality of economic research needed as a basis for considering credit and monetary actions. Development of a research group involves much more than selection of a competent staff, its effective organization for operation at the Board, and a research program. A research staff needs to strive continually to improve its performance and its professional standing. To this end, it is important to encourage the staff to publish articles on economic and technical subjects in outside professional and similar journals as well as in the Bulletin and other Board publications.

At the same time, it is generally recognized, by the staff as well as by the Editorial Committee, that certain subjects may not be appropriate for outside publication by the Board's staff. In most instances, the resolution of problem publication subjects can be most readily effected through discussion between Mr. Thurston and the staff officers most immediately concerned.

It is suggested that the Board approve continuance of this publication procedure.

There had been sent to the members of the Board copies of a draft of letter to the Honorable William L. Dawson, Chairman of the House Committee on Government Operations, reporting on Bill H. R. 2643, which would

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direct the Comptroller General to make an audit of the Board of Governors, the Federal Reserve Banks, and the Federal Open Market Committee for the period December 23, 1913, to December 31, 1954.

At the conclusion of a brief discussion, Mr. Thurston was requested to prepare another draft of the letter on the basis of comments submitted to him by members of the Board and to distribute copies of the revised draft with a view to consideration at another meeting of the Board.

Minutes of actions taken by the Board of Governors of the Federal Reserve System on March 15, 1955, were approved unanimously.

At this point all of the members of the staff except Messrs. Carpenter and Johnson withdrew from the meeting.

Before this meeting there had been sent to the members of the Board copies of a report submitted by Mr. Johnson under date of February 24, 1955, on the budget performance of various offices and divisions of the Board for the year 1954.

Following a supplementary statement by Mr. Johnson and a discussion of the report, Governor Mills inquired whether the reduction in the number of employees on the Board's staff was resulting in necessary overtime to such an extent that some of the positions eliminated from the budget should be reinstated. There was also a discussion of whether the salaries paid by the Board, particularly to persons in stenographic and clerical positions, were in fact comparable to those in other Government offices and whether salaries of certain positions should be raised.

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Governor Vardaman referred to the position which he had taken previously with respect to outside employment of members of the staff and raised again the question whether Board personnel should be permitted to have such connections. Governor Balderston commented on situations which he had seen before he became a member of the Board in which outside employment had injured the health of employees and their value to the institution in which they were primarily employed. He expressed the view that wherever an employee felt the need for outside employment, the matter should be investigated. The further comment was made that from time to time employees might undertake obligations or responsibilities which they would not be able to discharge from any salary that the Board would be justified in paying for the services rendered and, for that reason, would seek outside employment to supplement their income.

It was agreed that these questions should be considered by the Board at an appropriate time, and Chairman Martin stated that after Governor Shepardson, the newly-appointed member of the Board, had assumed his duties the Board would have a full review of its procedures.

Governor Mills referred to the statement in the annual report submitted by the Employees' Committee to the Board's employees for the year ending March 31, 1955, regarding the suggestion of employees that the umbrellas be returned to the tables on the patio adjoining the cafeteria and the reasons why the suggestion was not carried out.

Following a discussion of this matter, it was understood that Mr. Johnson, as

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Director of the Division of Personnel Administration, would look into the situation and submit a report to the Board.

Chairman Martin stated that President Powell of the Federal Reserve Bank of Minneapolis had invited Mr. Riefler, Assistant to the Chairman, to speak at the Bank's annual money and banking workshop on May 7, 1955, on the subject of recent monetary policy from the standpoint of the Federal Reserve System.

The acceptance of the invitation by Mr. Riefler, should he desire to do so, was approved unanimously.

Governor Robertson stated that there was a growing practice under which brokers pledge with a bank securities belonging to their customers and borrow Government securities from the bank which they then use as collateral for loans from another bank at a lower rate than could be obtained if the customers' securities were pledged as collateral for the bank loan. The practice, Governor Robertson stated, raised the question of proper reporting of these transactions in call reports, for the reason that the banks lending the Government securities apparently continue to show the securities among their investments and do not show the holding of stock market collateral as security for the loan of Governments. He added that several years ago there was a provision in the call report requiring that such transactions be reported, that the provision had been dropped as being of little importance, and that he had asked the staff to study the matter and prepare for consideration by the Board an amendment to the

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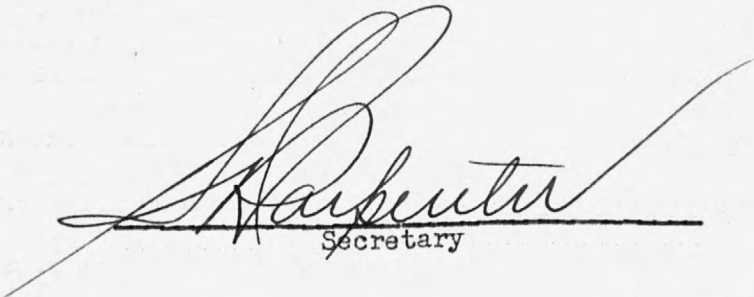
instructions for the preparation of the call report which would require that the securities held under these arrangements be properly reported.

The following letter for the signature of Chairman Martin to Mr. Charles N. Shepardson, the newly-appointed member of the Board of Governors, was approved unanimously:

Your letter of March 10, in which you submit your resignation as a director of the Houston Branch of the Federal Reserve Bank of Dallas, has been brought to the attention of the Board of Governors and, in accordance with your request, the Board has accepted your resignation, effective March 18, 1955. In taking this action, the members of the Board requested me to convey to you their appreciation of the contribution you have made to the Federal Reserve System through your service as a Branch director.

The comments contained in your letter with respect to your association with the Houston Branch are most gratifying. We, of course, are looking forward with great pleasure to your becoming associated with us here in Washington.

The meeting then adjourned.



Secretary