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Minutes for September 23, 1959

To: Members of the Board

From: Office of the Secretary

Attached is a copy of the minutes of the Board of Governors of the Federal Reserve System on the above date. 1/

It is not proposed to include a statement with respect to any of the entries in this set of minutes in the record of policy actions required to be maintained pursuant to section 10 of the Federal Reserve Act.

Should you have any question with regard to the minutes, it will be appreciated if you will advise the Secretary's Office. Otherwise, please initial below. If you were present at the meeting, your initials will indicate approval of the minutes. If you were not present, your initials will indicate only that you have seen the minutes.

Chm. Martin _____

Gov. Szymczak _____

Gov. Mills _____

Gov. Robertson _____

Gov. Balderston _____

Gov. Shepardson _____

Gov. King _____

1/ Meeting with Presidents of the Federal Reserve Banks.

A meeting of the Board of Governors of the Federal Reserve System with the Presidents of the Federal Reserve Banks was held in the Board Room of the Federal Reserve Building in Washington, D. C., on Wednesday, September 23, 1959, at 10:00 a.m.

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

Mr. Sherman, Secretary
Mr. Landry, Assistant to the Secretary

Messrs. Erickson, Hayes, Bopp, Fulton, Leach, Bryan, Allen, Johns, Deming, Leedy, Irons, and Mangels, 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. Dunne, Secretary of the Conference of Presidents of the Federal Reserve Banks

Prior to this meeting there had been distributed to the members of the Board a memorandum of the topics that the Presidents would like to discuss. The topics, the statement of the Presidents with respect to each, and the discussion at this meeting were as follows:

1. Wrapped Coin--Costs and Charges. The Conference approved the formula for wrapped coin costs suggested by the May 29, 1959, report of the ad hoc committee on this subject, as modified by the August 19, 1959, report of the Subcommittee on Accounting. The Conference also voted to recommend to the Board of Governors (1) that the timing of imposition of wrapped coin charges based on the foregoing formula be left to the discretion of

individual Reserve Banks providing such service and (2) that the furnishing of free wrapped coin on a limited basis be permitted to continue at any Reserve Bank which feels that the imposition of charges might create substantial bank relations problems.

In elaboration of the second part of the Conference recommendation that the furnishing of free wrapped coin on a limited basis be permitted at any Reserve Bank that felt a charge might create substantial bank relations problems, Mr. Johns stated that in the context of the discussion that occurred it was the view of most of the Presidents that perhaps it was not the business of the Conference to dictate how an individual Reserve Bank should be run. If there were to be a deviation from the application of the principle of recovering substantially the costs of the service as computed under the formula that the Conference had approved, this would raise a question to be settled between the individual Bank and the Board of Governors.

Chairman Martin called for comments with respect to the Conference recommendation on this subject.

Mr. Hayes stated that in the absence of comments by others it seemed incumbent on him to expand on what Mr. Johns had said. The New York Bank was the only one that followed the procedure of furnishing wrapped coin to some of its member banks without charge. He referred to the Board's letter dated February 3, 1959, to the Chairman of the Presidents' Conference in which the Board indicated that it would be preferable to leave to the management of the individual Banks the

determination of whether or not a Reserve Bank should engage in coin wrapping service at all. Mr. Hayes pointed out that, unlike the seven other Reserve Banks currently wrapping coin and charging member banks for this service, the New York Bank provided a small quantity of wrapped coin for country banks without charge, that it had been doing so for the past 35 years, and that it could not possibly provide tellers' coin for the larger banks of the district without a major increase in facilities. To discontinue the service that had been provided for many years to some of its country banks might cause substantial bank relations problems, Mr. Hayes said, and he hoped that the New York Bank would be permitted to continue the practice that it had been following. In response to a question from Governor Shepardson, Mr. Hayes added that he was not suggesting that if the New York Bank made a charge to country banks for wrapped coin it would be forced to provide similar service for all of its member banks. His point was that the situation at the New York Bank seemed to him to differ from that in the other districts furnishing this service.

Governor Mills commented that the question raised was fundamentally one of the extent to which free services should be provided by the Reserve Banks to member banks. This was a question that in his opinion deserved more study, particularly since the System might be overemphasizing the public relations angles with member banks. At some point he felt that there must be a determination of the extent of the free services that properly could be provided to the member banks.

President Johns stated that implicit in this situation was the fact that the Presidents of all of the Reserve Banks other than New York had indicated their willingness and intent to recover substantially the costs of furnishing wrapped coin as determined according to the uniform formula that had been approved by the Conference and submitted for the Board's consideration.

Governor Robertson inquired whether, in making a recommendation that the timing of wrapped coin charges based on this formula be left to the individual Banks, the Presidents' Conference contemplated any outside limit as to when these charges would start.

President Johns responded that the Conference had not set such a time but that some Banks desired leeway. He then suggested that Messrs. Allen and Deming comment.

Mr. Allen stated that the Chicago Bank was not recovering its full costs at the present time but that it agreed with the idea that it should be. At the present time, facilities for coin wrapping at Chicago were not as efficient as they would be when their present building program was completed. He was reluctant to increase the charges this year for this service and perhaps find it necessary to reduce them in a year or so. He would like to be in a position to continue with the present arrangement until 1960 or perhaps 1961, when Chicago would have an improved coin wrapping operation and would be in a better position to determine costs and appropriate charges for this service.

Mr. Deming stated that much the same situation existed at the Minneapolis Bank except that the period was considerably shorter. He thought that perhaps in eight or nine months the Minneapolis Bank would be at a point where it would wish to apply the costs determined by the suggested formula.

Chairman Martin stated that the recommendation of the Presidents' Conference on this as well as on other topics would be taken up at a subsequent meeting of the Board and the Presidents informed of the Board's views.

2. Management Development. The Board's letter of August 11, 1959, requested Conference consideration of (a) desirability of eliminating this function as a separate item in Reserve Bank accounting and (b) possible alternative reporting methods. The Conference concurred in the recommendation of its Committee on Collections and Accounting that the function be consolidated in the function "Training and Education" with a memorandum segregation for any desired classification of the personnel charges involved.

President Mangels commented briefly on this topic, stating that eleven Banks or branches had shown minor expenses under this item during 1958. He added that separate memoranda records could be maintained by the personnel departments of the Banks and information on costs for the management development program furnished upon request.

There was no further discussion of this topic.

3. Armored Car Service. Following the Board's letter of August 6, 1959, the Subcommittee on Cash, Leased Wire, and Sundry Operations canvassed the Reserve Banks concerning (a) extent and use of armored car

service and (b) possible desirability of Reserve Bank ownership and operation of such cars. The Conference adopted the recommendation of the Committee on Miscellaneous Operations that such operation would not be feasible at times in view of (a) the substantial costs involved, (b) the anticipated resultant pressures for increased armored car service to member banks, and (c) the potential of drivers and other employees as a target of union organizations.

In commenting on the recommendation of the Presidents' Conference, Mr. Fulton said that the Reserve Bank Presidents felt that ownership and operation of armored cars by the Reserve Banks would get them into an area of transportation that was not the type of thing in which the Reserve Banks should be engaged. Not only would the Banks be exposed to possible unionization by the Teamsters Union, but there would be an increased problem of safeguarding transportation at longer distances.

Mr. Hayes noted that a key consideration as to the practicability of having the Reserve Banks operate their own armored cars would be the wide variation in needs from day to day. For example, at New York on some days three armored cars would meet the need, while on others as many as 24 were required.

4. Personnel. The Conference concurred in the recommendations of its Committee on Personnel that the Subcommittee on Personnel proceed to undertake study and submit recommendations on: (1) supplementing allowances of retired employees; (2) accident insurance for Federal Reserve employees in travel status; and (3) major medical insurance for retired personnel. (Consideration of these pending matters had been deferred until implementation of the major medical program had been effected.)

There was no discussion of this topic.

5. Reserve City Classification. Following the Board's letter of July 31 to the individual presidents, the topic of new standards for reserve city classification was referred to the Committee on Legislation for study and recommendation. In response to such action the Conference received a report, dated September 9, 1959, from the Subcommittee on Legislation. After extended discussion, the Conference voted (1) to submit such report to the Board, emphasizing the tentative nature of the conclusions therein, with the thought that the report might be helpful in evaluation of the problems involved, (2) to concur specifically in the report's conclusion (page I-5) that "basic changes should not be made in the standards now used unless a reasonable case can be presented in support of such changes", (3) that accumulation of possible supporting evidence to such a case requires expeditious research and testing, in which the Reserve Banks will be happy to participate, if the Board wishes, through a joint committee of Board and Reserve Bank personnel, and (4) to suggest use of interbank balances as the primary principle by which a simple, well-known, and practicable basis of reserve city classification may be obtained.

The Conference also voted to recommend to the Board: (1) that a modest start be made this fall in use of vault cash for reserve purposes in such amount as will not require substantial offsetting open market operations; (2) to consider in the near future the more pressing applications for reclassification to country bank status (as permitted under the recently amended statute), using for the time being the present basis for reserve city classification as the major criterion but with consideration of other factors suggested by the subcommittee report; and (3) to eliminate (either by one action or in stages), as soon as an opportune time arises, the existing central reserve city differential, although this problem is less pressing than the matters of vault cash and individual bank reclassification.

Mr. Johns stated that the Board's letter of July 31, 1959, regarding this topic had been referred to the Presidents' Conference

Committee on Legislation of which Mr. Hayes is Chairman, in view of the fact that that Committee previously had done considerable work on the subject when the legislative proposal was before the Congress. He then called upon Mr. Hayes.

Mr. Hayes said that the Conference Subcommittee had prepared a report dated September 9, 1959, copies of which had been furnished to the Board. After commenting briefly on that report and on the statement submitted by the Presidents' Conference at this meeting, Mr. Hayes referred specifically to the Conference recommendation that a modest start be made this fall in use of vault cash for reserve purposes in such amount as will not require substantial offsetting open market operations. The Conference had in mind that there would be seasonal needs for reserves this fall, he said, and that some release of vault cash might be made to help meet these needs and thus to lessen the need for open market operations. If this were done in a modest amount, it would not be necessary to offset the vault cash thus released by subsequent sales of securities from the System Account after the end of the year. In response to a question from Governor Robertson, Mr. Hayes said that the Conference had not considered in detail the possibility of increasing the time schedule for credits for checks collected to a maximum of three days as a means of partially offsetting reserves that might be released through counting of vault cash. He recalled that the Presidents' Conference had been split wide open on this question last year, and, in view of the limited time available, it had not gotten into the matter again at this meeting.

Responding to a further question from Governor Szymczak, Mr. Hayes noted that the Subcommittee's report had touched upon the question of increasing reserve requirements as an offset to permitting the counting of vault cash but that it did not discuss such action in terms of it being a desirable possibility.

Mr. Johns added the comment that there had been some discussion of a possible increase in reserve requirements at the Conference but that there was no enthusiasm for such action.

Governor Balderston then inquired of Mr. Hayes whether the Conference had considered linking together action on the vault cash proposal and a request for more detailed reports that would assist in providing better figures on the money supply.

To this, Mr. Hayes responded that the Conference had not come to grips with several of the detailed problems connected with this legislation and that he was sure the Conference had not contemplated any extensive additional collection of data in connection with implementing the vault cash provision.

Governor Shepardson stated his understanding that any plan for counting vault cash would probably have to be accompanied by some compensating offset, perhaps through increasing reserve requirements. He inquired whether the Conference had considered the possiblity of taking advantage of the seasonal need for additional reserves during the latter part of this year as a time for releasing some of the vault cash, with

the thought that advantage also could be taken of the return flow to the Banks of reserves after the first of the year by raising reserve requirements as a means of recapturing some of the reserves.

Mr. Hayes noted that the Subcommittee report to which he had referred earlier contained a number of conclusions regarding the subject of vault cash. The Conference had not debated these in full, although it generally went along with the Subcommittee's report. His recollection was that the Conference did not contemplate a large release of reserves through vault cash. If, however, a large release were made, he thought that an increase in reserve requirements might be explored.

Governor Balderston noted that under certain circumstances a release of vault cash might cause a differential of 4 or 5 percentage points between reserve requirements for banks that were classed as reserve city banks and those classed as country banks. He suggested that in the event the differential in real reserve requirements were quite large, pressure would be increased for reclassification of individual banks from the reserve city status to country bank status.

Mr. Hayes observed that this was a valid point. He added that although the Presidents had not had an opportunity to consider all of these matters in detail it was generally their view that some action to permit vault cash to be counted against reserve requirements during the fall months of this year would be desirable.

Mr. Bryan stated that on the matter of moving to a three-day maximum deferment schedule, Mr. Mangels had brought this question up

in Conference discussion but, being pressed for time, it was not debated in full. He (Mr. Bryan) recalled that he was one of the Presidents who was opposed to moving from a two- to a three-day deferment schedule when this matter was considered earlier and that he had voted vigorously against it. Nevertheless, if the Board wished to make a massive injection of new reserves in connection with the vault cash proposal, he would state now that, if the deferment question was taken off the table and considered again, he might wish to change his position in view of the new legislation. In other words, Mr. Bryan said, he did not think the proposal for moving to a three-day maximum deferment schedule in connection with implementing the vault cash proposal should be fully ruled out of consideration.

Governor Robertson said that he thought this was probably the most important and difficult administrative problem facing the System right now. He suggested that it would be helpful to all concerned if the individual views of the Presidents could be put in memorandum form and sent to the Board.

Mr. Hayes stated that he was delighted to hear this comment. The report of the Subcommittee on Legislation had listed several steps that might be taken in connection with the new legislation and these, he thought, should be considered by whatever group was testing and analyzing the problem of standards of classification for cities and for banks. This would amount to a very intensive study by a task force which the Presidents' Subcommittee

thought might consist of a joint committee including representatives from all parts of the System.

Governor Balderston stated that he felt the System was in a difficult position. It had asked the Congress to grant the authority to count vault cash to remedy inequities among banks, and it also had asked for the authority on the grounds that this would help to disseminate currency around the country as an emergency defense measure. These two considerations made him incline toward the view that the Board should not delay in implementing the legislation that had now been passed by the Congress. Consequently, vault cash should be cut out from the herd and dealt with promptly as a problem that is administratively solvable at this time, leaving for more extensive study the matter of standards of classification of cities and individual banks. This problem of classification had been under study off and on for many years and he felt that it would take a great deal of analysis before a satisfactory arrangement could be agreed upon. He would join with Governor Robertson in inviting comments from the Reserve Banks as to how the System might proceed this fall, or at the latest in January of 1960, to permit vault cash to be counted either in whole or in part, with or without compensating action through changing reserve requirements.

Chairman Martin said that it would be desirable to bear in mind that the Treasury on three occasions had brought up the problem of the

Mint in supplying coin in connection with permitting the counting of vault cash. While those in the Federal Reserve might have a different view, this was a problem with which the Treasury was very much concerned, as indicated by its representatives having raised the question on three separate occasions. Before moving on vault cash the Board would have to have definitely in mind all aspects of this particular question. He agreed with the suggestion that anyone who wished to come forward with ideas for dealing with the problem should feel at liberty to submit his ideas. For himself, the Chairman said that the more he had thought about the matter the more he had come to the conclusion that sooner or later the System was going to have to start off at some point into uncharted ground because he did not believe that any amount of study of this problem would obviate the necessity for a certain amount of experimentation.

6. Retail Trade Statistics. The Conference considered the proposal made by the Bureau of the Budget that, appropriations permitting, the Bureau of the Census take over the retail trade statistics program on July 1, 1960. The Conference noted that under the proposal the Federal Reserve System, including the individual Reserve Banks, would have the opportunity to contract with the Bureau of the Census for more detailed information (e.g., data for standard metropolitan statistical areas) than that contemplated by the Census program. The Conference voted to recommend to the Board that the proposal be adopted.

The Conference also voted to authorize its Committee on Research and Statistics to evaluate staff suggestions for technical deletions and

modifications of department store statistical series without formal reference to the Conference. The Committee was authorized to dispose of relatively insubstantial matters on its own initiative and to communicate with the presidents in other cases.

President Irons stated that Mr. Young, Director, Division of Research and Statistics, had given him a copy of a memorandum dated September 18, 1959, specifying what the Bureau of the Census and the Bureau of the Budget planned to do: namely, to seek a $400,000 budget appropriation for fiscal year 1961 to enable Census to take over responsibility for department store data and to provide statistics for the United States as a whole and for standard metropolitan statistical areas. He observed further that the opportunity for individual Reserve Banks to contract with the Bureau of the Census for more detailed regional information was believed by the Conference to be a desirable approach to a problem that had been discussed for years. It would not only help the Reserve Banks to maintain their contacts with department stores, but it would assist in solving the public relations problem that was inevitable in a shift of responsibility for the department store statistics that had been collected by the Federal Reserve since 1919. It was on this basis that the Conference recommended adoption of the approach suggested, and it had authorized its Committee on Research and Statistics to take certain steps as a means of expediting the program outlined.

7. Emergency Planning--Commercial Banks. The Conference voted to approve the recommendations made by its Special Committee on Emergency Planning as a result of a letter from Mr. John J. McCloy, Chairman of the Advisory Committee on Commercial Bank Preparedness, to Mr. Hayes, expressing disappointment on the progress of emergency planning in commercial banks and requesting a general summary from each Reserve Bank as to possible reasons for inaction on the part of commercial banks in its district. The Special Committee's recommendations were (1) that each Reserve Bank provide the Special Committee with its views on reasons underlying any delay in commercial bank emergency planning in its district, and (2) that the Board of Governors consider a joint program with the other two Federal bank supervisory agencies whereby the status of emergency planning operations in each bank examined would be discussed briefly in the open section of the examination report.

After Mr. Hayes had commented on the recommendations of the Special Committee on Emergency Planning, which are set forth above and which the Conference had voted to approve, Governor Robertson stated that he felt it desirable to obtain the views of the Presidents as recommended on reasons underlying any delay in commercial bank emergency planning. With respect to the recommendation that the Board of Governors consider a joint program with the other Federal bank supervisory agencies looking toward discussion of emergency planning operations of commercial banks in the open section of the examination report, Governor Robertson said that this was a matter that had been discussed among the supervisory agencies. They had concluded that they should make no out and out effort to carry this planning forward until a decision had been reached as to what the program for banking would be in an emergency. This was because it was important to the banks in making plans to know what approach was to be taken, that is, whether banks were to be closed, or whether the approach

was to be one where the banks would remain open. Once a program was definitely formulated, there could be an all-out attempt to sell the banks on making preparedness plans. At that time, Governor Robertson said, the first step toward selling the program probably should be taken by a bankers' committee such as the one now headed by Mr. McCloy, to be followed up by the State bankers' associations and then by the supervisory agencies. After that, in his opinion, it would be appropriate to put comments regarding the planning of individual banks in the open section of the examination report.

Mr. Hayes said that there was a great deal to what Governor Robertson said. However, he was concerned about relations with commercial bankers as regards the present program, which the Federal Reserve had been urging upon them. If the System now took the view that it should not press for this program, there was a danger that the banks might become confused as to what was desired of them at the moment.

Governor Robertson agreed that this danger existed but said he did not believe the banks could be told just what was wanted of them until it was known what the program was to be.

President Johns said that Governor Robertson had explained to his satisfaction what we were waiting for, and he then inquired as to whom the banks were waiting on for a decision regarding the approach to be taken.

Governor Robertson responded that the program must be one that Government was behind. An effort was being made to work out a program

between the Federal Reserve and the Treasury and, once that was agreed upon, the program for the commercial banks could go forward. In response to a question from Mr. Leach as to cash agent banks, Governor Robertson said that there had been no change in the plans along that line or as to check collection, and he did not believe that anything was likely to result in a decision against having cash agent banks set up.

Governor Shepardson inquired why many of the things pertinent to a defense planning program for commercial banks might not now press ahead.

Mr. Hayes responded that banks could go ahead in planning for the appointment of officers to handle the operations of the bank, setting up records systems, and in planning for protection of assets as well as some other matters. It was difficult to get into some important aspects of planning or to get enthusiasm until the banks knew what it was intended that they should accomplish in an emergency.

Governor Robertson added the comment that if the group now working on the program were to build up enthusiasm through a strong selling program and find itself unable to answer questions as to what was really expected of the banks, there might be a let-down that would put the whole program back. He also said, in response to a comment by Governor Balderston, that in general the largest banks of the country had moved farther along with defense planning than had the smaller banks.

Mr. Erickson inquired whether a decision on the approach to be taken by banks might be reached in the near future, and Chairman Martin said that he thought a conclusion on this point might be arrived at within a reasonable period of time.

8. Reserve Bank Capital Accounts. The Board's letter of July 17, 1959, addressed to the Presidents requested a review of the Reserve Bank capital accounts, and the topic was referred jointly to the Committees on Collections and Accounting and on Research and Statistics for preliminary study. Following oral reports by the respective Chairmen of the Committees, the Conference engaged in extended discussion of various aspects of the subject with particular reference to certain basic principles and problems involved, preliminary to a general exchange of views with the Board of Governors. The members of the Conference were of the unanimous opinion that it would be desirable for Reserve Banks to retain their present form of capital structure but were not prepared at this time to suggest specific amounts or ranges for the components of such structure outside the statutorily determined capital stock account.

The Conference also voted to refer (1) the question of the adequacy and level of the reserve for registered mail losses under the Loss Sharing Agreement to the Insurance Committee and (2) the question of fixed assets accounting to its Committee on Collections and Accounting.

Mr. Irons said that the Committee on Research and Statistics realized that this was a topic on which there could be wide differences of opinion as well as extended discussion. The Committee had attempted to develop some principles as to whether capital and surplus accounts were appropriate for a Federal Reserve Bank. The Committee's report, copies of which had been furnished earlier for distribution to the members of the Board, took the position that as a matter of principle it would be desirable for the Reserve Banks to retain the present form of capital structure and financial accounts, and this position had been endorsed unanimously by the Conference

of Presidents. Mr. Irons noted that, while this did not indicate how much should be kept in any of these capital accounts, the Conference did generally take the approach that the financial accounts of the Federal Reserve Banks should be somewhat similar to what could be supported for private business or banking institutions, giving some recognition that there might be reason for modifications between the two. If, however, the position were that there was something short of Government in the nature of the Federal Reserve Banks, then that position should be reflected in the financial organization of the Reserve Banks and in their statements and accounts. In using the phrase that the Reserve Banks should "retain their present form of capital structure" the Conference had in mind that this included retention of contingency reserves and reserves for depreciation. Mr. Irons noted that the Conference also voted unanimously to refer the question of the adequacy and level of the reserve for registered mail losses under the loss sharing agreement to the Insurance Committee of the Presidents' Conference for study and recommendation as to what might be a defensible amount of such reserves, and that it had referred to the Committee on Collections and Accounting the question of fixed assets accounting and the amounts of reserves for depreciation on furniture and equipment. Mr. Irons added that one other conclusion of the Conference was that the Federal Reserve System should be very careful to be consistent in what it claimed for itself. It did not believe that the System consistently could, on the one hand, claim an exemption from certain measures on the grounds that it was other than Government and then come along and claim for accounting purposes that it was quasi-Government. Mr. Irons concluded his statement with the comment that in further study of this matter the Conference, either through appropriate committees or otherwise, would be glad to

work with the Board in trying to arrive at conclusions that would be defensible in terms of the basic principles that were accepted for institutions such as the Federal Reserve Banks.

Governor Robertson said that, sifting through the report of the Committee on Research and Statistics, he had tried in vain to find some reason why the System should have the various capital accounts referred to other than that it wished to paint a picture that it was comparable to a private institution. He doubted that this would be an answer to any Congressional committee as to why Federal Reserve Banks needed these accounts.

Mr. Irons said that reference had been made to the fact that the Federal Reserve Banks could operate even if they did not have capital, surplus, or contingency reserves. That was not being questioned. However, Mr. Irons said, there was more to the problem than that, and he cited an expression used by Mr. Bryan, President of the Atlanta Bank, that the capital and surplus accounts of the System were symbolic: the System could operate without them, just as the country could operate without a flag. He went on to say that if the Reserve Banks were to operate without capital, he thought we should abandon any concept of their being "banks" and, instead, call the Federal Reserve a monetary authority. He did not think this was what the System wanted, and he did not think that a majority of the Congress wanted that concept. To try to answer the question suggested by Governor Robertson, Mr. Irons said he thought the absence of capital accounts for the Federal Reserve Banks would mean their complete nationalization. Some might say that this was already true in practice, but personally, he did not think this was true, and he did not wish to lose any more than had already been

lost toward full nationalization of the System. The Federal Reserve performed in its day-to-day operations a good many things that were truthfully banking, such as check collection, and none would deny that the mixed element of activities included some that were purely governmental, such as credit policy. Mr. Irons felt that the whole question needed much more study than had been given to it in order that the System might develop a more plausible and foolproof defense than it now had.

Governor Robertson said that, at the time the Federal Reserve was set up, reasons were advanced for the form it took, and he felt that if it had not already been done the Committee of the Presidents' Conference should look into that history to see what was then thought of the value of this symbol.

Mr. Irons said that the Committee had gone into this to some extent and it had attempted to touch upon the historical aspects in the memorandum that had been distributed. He thought that a good case could be made for the position the Committee on Research and Statistics had taken, adding that a historical study would call for intensive and high-level research. He agreed with Governor Robertson that this was a question that would have to be answered sooner or later, and this was another reason why a committee of the Conference would be delighted to work, either independently or jointly with the Board, in further study of the subject.

Chairman Martin said that it was important to bear in mind the reasons why this topic came up now. It had been raised in hearings

before the Congress this year, but in addition for three years the Bureau of the Budget had had a staff recommendation that would take over to the Government all of the surplus of the Federal Reserve Banks. The System had been fortunate in having an Administration that was sympathetic to the general position of the central bank. However, the Director of the Budget had discussed the matter with him (Chairman Martin) this past summer, and a bill actually had been drafted for the purpose indicated. The Chairman noted that there was little difficulty in defending the principle Mr. Irons had stated with those who are already sympathetic with that approach, but the amount of the surplus or of contingency or depreciation reserves was another matter. Here the System could be accused of padding the accounts, and it would be in a difficult spot if this question came up. He was glad that the session of the Congress just ended had come without action by the Congress or by a Committee for review of this question. He hoped that before the next session of the Congress opened the System would have a positive and definite approach and that it would be able to get something to the Chairmen of both the Senate and the House Banking and Currency Committees fairly early in January before anyone else raised the question. This was the real importance of the topic and was why it had been placed on the agenda for a preliminary discussion at this meeting. This was something that could move very fast. In May of this year the question was not active, but in July when other matters were being debated the subject was causing serious concern among the friends of the System in the Congress.

Mr. Bryan withdrew from the room at this point.

Governor King stated that, as he understood the history of the System, it was set up in the way it was in order to obtain the confidence and support of the banking community. To depart from that concept would be breaking faith with a large group of those who had helped found the System. If the illusion were created that the System was trying to accumulate reserves unnecessarily, that would be a detriment to the System and to the whole country. He questioned whether there was any reason for a reserve for contingencies. There might be a valid reason for a reserve for registered mail losses, but to have a reserve for contingencies created an illusion: it did not cover anything that was not covered in surplus. His feeling was that the System should move to dispel such illusions that were certain to work to the detriment of the System.

Mr. Erickson inquired of Governor Robertson whether, in view of his interest in examination procedures and banking structure problems, he had found that the fact the Federal Reserve was set up in the same way as commercial banks had helped convince member banks that they should increase their capital. He added that this had been found helpful in the Boston District.

Governor Robertson responded that he could not remember any instance in which an analogy to a Federal Reserve Bank had been brought into the picture where examiners were attempting to get a commercial bank to increase its capital.

Mr. Hayes said that he was in thorough agreement with the Conference approach to this problem. He agreed with Chairman Martin that the System should make a positive approach to it, and he assumed that this merely meant explaining what the System was doing and why. If it meant a positive approach in the way of giving up some of its funds, he would not advocate that because that would be prejudging. The System might end up with doing that but it should not take that approach now. The fact that these reserves were mentioned in the present Federal Reserve Act and in the original Federal Reserve Act should carry great weight, in Mr. Hayes' opinion. The Reserve Banks performed many banking services and charged for these on a true cost basis. That meant they should definitely use accepted accounting principles. He was impressed, he said, with the fact that the public both here and abroad looked on the Federal Reserve Banks as organizations run in a business way. Without casting aspersions on Government, theirs was a different method of running accounts, and this had been a strength of the Federal Reserve System with the public and abroad. Mr. Hayes said that he thought any change in that approach should be made with great reluctance and probably not at all. There was a question in his mind as to whether the burden of proof was not on those who thought the System should give up some of its funds, rather than on the System to say why it should not.

Mr. Hayes went on to say that he started with the assumption that, in view of the size of the System's operations and of its

assets and its broad scope, it was not overcapitalized. It was easier to cut down capital accounts than to build them up. Perhaps the System should be in position to take on functions that seemed desirable and for which it might have to absorb losses, for example a stabilization account. Whatever the System did in giving up sizable sums to the Treasury was going to be a matter subject to the charge that the System was helping a given Administration to get a budget balanced. For these and other reasons, Mr. Hayes thought that the System should move very slowly, should do a lot of hard thinking, and should not contemplate any major action soon.

Mr. Leedy said that the Conference action had been reflected correctly in the statement submitted to the Board: it had endorsed the approach stated in the report of the Committee on Research and Statistics. He had sensed, however, that at least a majority of the Presidents believed that the System should not continue indefinitely to be accumulating surplus. Perhaps a majority would subscribe to the reimposition of the franchise tax on the Federal Reserve Banks, and perhaps a majority would not continue to syphon off 10 per cent of earnings after payment of dividends but would limit further additions if some agreement could be reached as to the proper level of the surplus account. Mr. Leedy said he also sensed the feeling that there was little need for any large contingency reserve in addition to surplus. In the light of what Chairman Martin had said as to what had developed this past summer, he assumed that it would be completely consistent with the recommendation of the Presidents' Conference that there be further study of the subject with the idea of assisting the

Board (provided that was what the Board desired) so that between now and the end of the year when the System would be faced with making additions to its present surplus accounts it would have a view as to what program should be followed at the end of the year. This would be his own view.

Governor Balderston said that he thought Mr. Leedy's comments came closer to the real problem before the System than anything else said thus far at this meeting. The System had lost the initiative on this problem, and the System and the Chairman were on the defense. Two questions, both of which stemmed from decisions of the past that were arbitrary and were not prompted by principle, were being asked: First, why does the Federal Reserve need a contingency reserve in addition to its surplus? Second, why does the System hold back 10 cents from every dollar after expenses and dividends when that money could go to the Treasury? Unless the System had a very clear answer to these two questions, and quite apart from the principle stated this morning with which he (Governor Balderston) agreed, it would be desirable for Chairman Martin to be in a position to discuss with the Chairmen of the Banking and Currency Committees a definite proposal that would do the right thing by the Treasury and the country as well as by the System. In Governor Balderston's judgment, it would be wise for the System to do this before a proposal was submitted by some of its critics.

Mr. Leach said that, as to the need for a surplus, the Congress itself had established the principle that surplus should equal 100 per cent

of subscribed capital. Mr. Leach thought this could be taken as a minimum proper amount, but the problem was to justify accumulating any surplus above that amount.

Mr. Johns commented that at its meeting yesterday the Conference was not really of a different view from many of the things being said around the table this morning. However, it seemed to him that before the System pursued this subject further, it would be helpful to know whether there was a view in the System that the Federal Reserve Banks did not need any capital structure in order to operate. If this were the prevailing view, then the question of how much there should be in surplus and contingency reserve and depreciation reserve would evaporate. As had been stated, it was the unanimous view of the Conference that the Banks should retain the present form of capital structure, and to the Presidents this seemed to be the place where they should try to get on common ground. He could recall no position on the part of any member of the Conference of wishing to defend to the death the dollar amounts in those accounts. As indicated before, the question of the adequacy of the reserve for registered mail losses had been referred to the Insurance Committee for study, and it seemed to some of the Presidents that the amount in that account was too high. With respect to Governor Robertson's comment, Mr. Johns said that while the Bank of issue could operate without capital funds, this should be balanced off against the view that the Reserve Banks look like the kind of banking organizations that people are accustomed to look at, and in dealing with public confidence

this view seemed to be one that should be considered. It might be difficult to demonstrate the value of this point, but he felt that it should not be overlooked.

Governor Mills remarked that if at any time the Federal Reserve System came into a position where it would have to look to the national Government to underwrite its risks and its potential for making losses, at that time the Federal Reserve would be effectively nationalized.

Chairman Martin said that he had been bothered during the past session of Congress by what seemed to be basic deficiencies in the System's informational setup. Answers to questions that had been dealt with over the years seemed to have become lost and could not be readily located when they were needed. Senators or Congressmen who were friendly to the System had been extremely critical because they felt the System had not developed machinery for answering simple questions that come up. He was perhaps concerned more with the public than with the Congress, which was only reflecting the view that the Federal Reserve had not thought these problems through. On a question such as this one, it was not an answer to say that the System had been following its present procedure for many years and would like to continue doing the same thing. Perhaps the System needed a historian who would be responsible for developing material to respond to questions that might be presented by committees or individual members of the Congress or by the public.

Mr. Johns raised a question about a formal study group in the System which might look into the question of capital accounts, and perhaps be helpful in meeting the problem that the Chairman had just mentioned. The Conference wished to make as great a contribution as possible, and it would be desirable to avoid duplication in use of the System's resources in further studies of the question.

Governor Shepardson noted that the Presidents' Conference had indicated its basic philosophy regarding capital accounts. He assumed that the Board would be reviewing this subject within the near future and would take a position regarding this basic philosophy. After this question was resolved, it might be desirable to appoint a special committee that would then proceed through the appropriate subcommittees to consider any detailed problems that might develop out of the System position taken. In this connection, he noted that the topic had been referred to the Conference Committee on Collections and Accounting, and he wondered whether a report would be submitted by that Committee.

Mr. Mangels said that so far as the Accounting Committee's part in the project was concerned, he had sent a "fishing" letter to the Presidents of the other Federal Reserve Banks. The purpose was to get their thinking on the entire elimination of the reserves for contingencies, on what should be done on depreciation, and on what should be the status of the surplus account. Of the five or six who had responded, the majority favored a reduction to some extent of the balance in the

reserve for contingencies. They also agreed that there should be a ceiling on the surplus. Mr. Mangels then commented briefly on possible ways of limiting the amount of surplus, suggesting that there would be some logic in limiting it to 200 or 250 per cent of paid-in capital in view of the former franchise tax provision. He went on to say that the steps that seemed to be called for were (1) a policy determination, and on this the Conference view was indicated by its endorsement of the report from the Committee on Research and Statistics; (2) a decision as to the extent to which surplus and reserve accounts should be maintained; and (3) consideration of the question of timing in the event a decision was reached to surrender some of the funds to the Treasury. So far as accounting principles were concerned, Mr. Mangels said that one of the directors of the San Francisco Reserve Bank who was a partner in a nationally-known firm of public accountants had expressed the view that there was no need at all for a Federal Reserve Bank to maintain a reserve for contingencies, but he had not commented particularly on the capital account itself.

Governor Shepardson said that in mentioning the Accounting Committee he had in mind the need for review of the accounting principles involved so that the System could have a position that was not inconsistent with the views of persons in that field.

Mr. Johns said that the Committee on Accounting and Collections had already been asked to study this matter and that he presumed the

Committee would present additional views at a future meeting of the Conference and at a joint meeting of the Presidents with the Board.

9. Additional Items of Information Arising Out of Current Conference Meeting. In addition to the foregoing matters, the following items of possible interest to the Board were considered by the Conference. They are reported herein as a matter of information.

a. The Conference received the summary of reports submitted to the Subcommittee on Collections by the Reserve Banks concerning the nature and extent of their adoption of recommendations contained in the November 25, 1958, report of the ad hoc committee of that Subcommittee. In presenting the summary, Mr. Mangels observed that adoption of recommendation seemed to have resulted in (1) improved System operating uniformity, and (2) some reduction in the amount of and fluctuations in float. The Conference noted that save for late presentation of remittance drafts and the treatment of Saturdays and holidays for availability purposes, there had been substantial adoption of the recommendation by Reserve Banks. The Conference voted to direct the Committee on Collections and Accounting to review Reserve Bank treatment of Saturdays for availability purposes with a view to possible System uniformity in this respect.

b. The Conference accepted and approved (one President dissenting) the May 20, 1959, letter-report of the Insurance Committee recommending that money shipments between commercial banks "for the account of" a Reserve Bank be covered under the Loss Sharing Agreement if the shipments otherwise comply with the Loss Sharing Agreement and conform to the following statement of conditions:

1. The shipments should be made at the request of or under an arrangement approved by a Federal Reserve Bank.

2. The shipments should be for the benefit of a Federal Reserve Bank as evidenced by reduction in volume of shipments to or from the Federal Reserve Bank, resulting in decreased handling by and reduced costs to the Federal Reserve Bank.

3. Any costs of transportation of the shipments should be borne by a Federal Reserve Bank.

4. The shipments should be between member banks or offices of a member bank.

c. The Conference accepted and approved the August 28, 1959, report of the Subcommittee on Electronics recommending (1) selection of the Federal Reserve Banks of Boston, New York, and San Francisco for pilot installations of mechanized check handling equipment; (2) deferment until the December 1959 Conference (and submission of a subsequent Subcommittee report) of selection of other pilot installations under the program; and (3) that the Federal Reserve Banks of Philadelphia, Cleveland, and Chicago keep the Subcommittee advised of developments which might affect their selection for the latter installations or for additional pilot installations that might be recommended by the Subcommittee as a result of any further proposals from manufacturers.

d. The Conference rejected by a vote of seven to five the recommendations of a joint report, dated May 19, 1959, of the Insurance Committee and the Subcommittee of Counsel on Emergency Operations, viz. (1) adoption of System policy of complete protection of cash agent banks against all agency hazards, including risks of loss due to own negligence or breach of contract, and (2) implementation of this recommended policy by eliminating the negligence and breach of contract exception clauses from the form of agency agreement and covering the exceptions under the existing provisions of the Loss Sharing Agreement.

The Conference (1) expressed its preference, as a matter of principle, that indemnification of cash agent banks be effected by Federal Reserve absorption of premium on an appropriate surety bond and (2) directed the Special Committee on Emergency Operations to re-examine and make recommendations on the question of cash agent indemnification in the light of the foregoing expression of principle.

Chairman Martin then referred to a discussion that he had had with Mr. Deming regarding use of the discount window. He added that he understood

some of the reports by members of the Federal Advisory Council regarding the discussion of this subject at the Council's meeting with the Board on September 15, 1959, might have needed clarification.

Mr. Deming said that when the Under Secretary of the Treasury was in Minneapolis recently he had expressed the belief that the large banks of the country that normally do Treasury underwriting do not recognize that they could come to the Reserve Banks to borrow during such periods. Mr. Deming said that he had assured the Under Secretary that the banks in the Twin Cities understood that they could come in for this purpose. The Under Secretary's point was not that the Reserve Banks had been too restrictive in use of the discount window, Mr. Deming said, but rather that some of the larger banks did not understand its use in connection with Treasury financings.

Mr. Allen said that he was sure there was no misunderstanding on the part of the Chicago banks on this point. However, he had been somewhat disturbed at the report of the Chairman of the Federal Advisory Council to the directors of the Chicago Bank last week when he said that the members of the Council had the impression that the Board of Governors agreed that there should be greater access to the discount window during the next few months and that the members of the Council had been encouraged to go back and lay the situation before their local Reserve Bank Boards. 1/

In a brief discussion of the matter, Chairman Martin recalled some of the comments at the meeting with the Council. In the discussion, he

1/ Should have read President of the Federal Advisory Council.

had suggested to the Council that the members talk with their local boards of directors regarding the use of the discount window and he had emphasized the view that credit should be available at all times. He did not believe, however, that the Council should have gotten the impression that the Board felt a change in the administration of the discount window was called for.

Thereupon, the meeting adjourned.

Secretary