FR 609
Rev. 10/59

Minutes for December 7, 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.

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 _____

Minutes of the Board of Governors of the Federal Reserve System on Monday, December 7, 1959. The Board met in the Board Room at 10:00 a.m.

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

Mr. Sherman, Secretary
Mr. Riefler, Assistant to the Chairman
Mr. Thomas, Economic Adviser to the Board
Mr. Shay, Legislative Counsel
Mr. Molony, Assistant to the Board
Mr. Hackley, General Counsel
Mr. Farrell, Director, Division of Bank Operations
Mr. Solomon, Director, Division of Examinations
Mr. Noyes, Adviser, Division of Research and Statistics
Mr. Daniels, Assistant Director, Division of Bank Operations
Mr. Goodman, Assistant Director, Division of Examinations
Mr. Landry, Assistant to the Secretary
Mr. Brill, Chief, Capital Markets Section, Division of Research and Statistics

Discount rates. The establishment without change by the Federal Reserve Banks of New York and Philadelphia on December 3, 1959, of the rates on discounts and advances in their existing schedules was approved unanimously, with the understanding that appropriate advice would be sent to those Banks.

Coin-wrapping policy (Items 1 and 2). There had been distributed under date of December 2, 1959, a memorandum from Mr. Farrell regarding coin-wrapping policy. Submitted with the memorandum were drafts of a suggested letter to the Chairman of the Presidents' Conference

and a letter which might be sent to President Hayes of the New York Reserve Bank. The memorandum noted that the recommendation on coin-wrapping policy made by the Presidents at their joint meeting with the Board on September 23, 1959, was to the effect that the timing of imposition of wrapped coin charges, based on a formula that had been developed by a committee of the Conference, be left to the discretion of individual Reserve Banks providing such service and that the furnishing of free wrapped coin on a limited basis be permitted to continue at any Reserve Bank which felt that the imposition of charges might create substantial bank relations problems. The study leading up to this recommendation had resulted from the Board's letter of February 3, 1959, to the Chairman of the Presidents' Conference, asking that the Conference review the basis for computing costs of the coin-wrapping operation with a view "to placing the charges for the service on a more nearly uniform basis than now exists, and to securing reimbursement for substantially the costs involved." The Board had stated that in the light of all the circumstances concerned it had reached the conclusion that it would be preferable to leave to the judgment of the individual Banks the question of whether or not a Reserve Bank should engage in coin-wrapping services, but that to the extent individual Banks decided to continue or to adopt a practice of furnishing wrapped coin there should be a uniform approach with respect to the rates charged for that service.

In the opinion of the Division of Bank Operations, there was considerable merit in the suggestion made by the Presidents' Conference that the timing of the imposition of revised charges based on the cost-recovery formula developed by the Conference be left to the discretion of the individual Banks, so as to permit expected economies at certain Banks due to new machines or better space arrangements to be evaluated. On the other hand, the Division felt there was doubt as to the advisability of adopting the recommendation that the furnishing of free wrapped coin on a limited basis be permitted to continue at any Reserve Bank which felt that the imposition of charges might create substantial bank relations problems. The suggested letters to the Chairman of the Presidents' Conference and to the New York Reserve Bank reflected these views of the Division.

Following discussion of possible modifications of the language contained in the letter to the Chairman of the Presidents' Conference, particularly with respect to the question whether the Board should impose a time limit within which the Reserve Banks must impose the revised coin-wrapping charges referred to in the memorandum, Mr. Farrell commented that he understood that the recommendation on coin-wrapping policy made by the Presidents at their joint meeting with the Board on September 23, 1959, reflected agreement on the part of all of the Reserve Bank Presidents except Mr. Hayes. The Minneapolis, Dallas, and San Francisco Banks reportedly felt that the provision by those Banks of coin-wrapping

service at substantially less than cost and the limited service provided by the New York Reserve Bank without charge involved only a matter of degree. Consequently, they found it hard to understand the position taken by President Hayes.

After a comment by Chairman Martin that the question had been pending for an extended period of time, unanimous approval was given to the proposed letters to the Chairman of the Presidents' Conference and to President Hayes. Copies are attached as Items 1 and 2, respectively.

Federal Reserve Bank capital accounts. There had been distributed a memorandum from Mr. Farrell dated December 4, 1959, summarizing reports of the Subcommittee on Accounting and the Insurance Committee which had been submitted to the Conference of Presidents in preparation for discussion of Reserve Bank capital accounts by the Presidents at their forthcoming meeting. The memorandum also referred to a report by the Conference Committee on Research and Statistics, also in connection with capital accounts, which had been distributed to the Presidents and to members of the Board in advance of the discussion of this topic during the meeting of the Board with the Presidents' Conference last September.

In commenting on his memorandum, Mr. Farrell indicated that the Subcommittee on Accounting was unable to come to an agreement with respect to depreciation procedures and that its report therefore contained two alternate proposals: (1) discontinuance of all depreciation so that Bank buildings would be carried at cost, fixed machinery and

equipment would be charged to expense, and furniture and fixtures also would be charged to expense, resulting in the complete buildings (including machinery and equipment) being carried on the books at $115 million rather than the present figure of $94 million, with the difference of $21 million credited to profit and loss; (2) depreciation procedures along conventional accounting lines, essentially continuing the present procedure with regard to buildings and inaugurating a new procedure for capitalizing and depreciating large future expenditures for furniture and equipment. Mr. Farrell said he had been informally advised by Mr. Mangels, Chairman of the Committee on Collections and Accounting, that he and Mr. Deming, another member of that Committee, looked with disfavor on both of the proposals and were considering submitting to the Presidents an alternate proposal to continue the present depreciation procedure until the depreciation allowance on each building reached 50 per cent of the gross book value, at which point no further depreciation would be taken on that particular building. He observed that the report of the Insurance Committee recommended that the procedure for making annual additions to the reserve for registered mail losses be continued until the reserve reached $15 million, and that as of December 1, 1958, the reserve stood at $11 million. With respect to the report of the Committee on Research and Statistics, he noted that this report took the position that capital accounts of the Federal Reserve Banks were significant as a symbol and should be retained, but that there was a suggestion that the present balances in these accounts might be excessive.

The Chairman commented that it was desirable to discuss these matters prior to the December 15 meeting between the Board and the Presidents of the Reserve Banks. He then asked for further explanation of the recommendation of the Subcommittee on Accounting with respect to depreciation policy.

Mr. Farrell replied that the four members of the Subcommittee on Accounting who were present at a meeting last September were evenly divided. Two members favored continuing the present system and adding a depreciation account for furniture and fixtures, while the other two members favored discontinuing all depreciation, carrying buildings at cost, and charging off fixed machinery and equipment. Although President Mangels had made a third proposal, as noted previously, Mr. Farrell was not certain how much support this proposition would receive.

After a comment by Mr. Hackley that the authority to prescribe uniform practices for System accounting rested with the Board under its general powers of supervision, the Chairman commented that it would be unwise to leave the question of accounting practices unresolved. Personally, he thought there was too much in the contingency fund and that there would be difficulty in defending a surplus of over $800 million, a reserve for contingencies of $98 million, a reserve for registered mail losses of $11 million, and depreciation balances of about $60 million.

Following further comments by the Chairman and by Governor Balderston to the effect that a uniform and consistent policy that could

be justified should be settled upon, Mr. Farrell said that it might be desirable to separate the depreciation question from the question of reserves for contingencies and registered mail losses. It seemed likely that the Reserve Bank Presidents would go along with the recommendations on the contingency reserves, but a meeting of the minds on depreciation practices could hardly be expected before the end of the year.

Governor Mills observed that the System was apparently open to the charge not only of following non-uniform practices of depreciation but also of using unusual methods. He raised the question whether System practices adhered to standard accounting procedures followed by industrial and business organizations, and he suggested that the Presidents' Conference or the Division of Bank Operations might obtain outside technical accounting assistance.

Mr. Farrell agreed that it would be desirable for the System to obtain outside technical assistance. He cited the difference of approach between the Minneapolis Reserve Bank and the Division of Bank Operations with respect to accounting for the cost of the addition to the Bank building.

Mr. Molony suggested that another reason for obtaining outside technical advice on this question was that any act by the System on its own might involve payment of a sizable sum to the Treasury during any given fiscal year.

Mr. Thomas noted that two alternative approaches to this matter were quite clear-cut: (1) to follow generally accepted business accounting practices; (2) to take the position that the Reserve Banks are units of the Government and should therefore follow governmental accounting practices, placing their operations on a pay-as-you-go basis with no capitalization of expenditures. He added that either of these approaches could be justified, but he doubted that it would be possible to justify anything in between.

With reference to Mr. Molony's point, the Chairman said that he had gone back over his notes of Board discussions of this question for the past eight or nine years, from which it was apparent that the Board had avoided meeting the issue. He felt that action should definitely be taken, and he added that he might communicate with Mr. Herz of Price Waterhouse to get comments.

Following a comment by Mr. Farrell that the question of contingency reserves was one of policy rather than accounting principles, Governor Robertson said that he saw no sound basis for continuing present practices. He felt it would be desirable to eliminate the reserves for contingencies and pay over to the Treasury the sum involved.

Governor Mills said that he would prefer to see the amount in the contingency reserves transferred to the surplus accounts of the Reserve Banks on the premise that the Banks should have a reasonable increase in their surplus accounts to keep pace with additions to their

liabilities. Should the contingency reserves be discarded and the amount involved be paid to the Treasury, this would not only constitute a confession of past error but would dissipate accumulated earnings which should be built into the System as it grew. He felt that certain of the Reserve Bank Presidents would argue, as did President Mangels, that the Reserve Banks should, like their member banks, add to capital as they grew until their surplus amounted to double their capital stock, although he recognized that this was a more or less arbitrary relationship.

Mr. Farrell commented that the Board had reached an agreement with the Treasury at the time the contingency reserves were established that any amount therein in excess of $80 million would be put through the profit and loss account in order to give the Treasury 90 per cent of the amount involved.

Mr. Hackley stated that the Board had the implied power to prescribe the form in which the assets and liabilities accounts of the Reserve Banks were carried and that it would be possible for the Board to support accounting procedures that deviated from conventional business practices.

Following a comment by Governor Robertson that he would be unable to answer a question as to the reason for maintaining surplus in the present amount, Governor Mills cautioned against disregarding the possibility of losses in the Federal Reserve System, citing the

example of a gold loan to the United Kingdom which eventually was resolved through advances from the Export-Import Bank. He suggested that the System might be forced to accept risks in the future which, should they involve losses for the Reserve Banks, could cause them to have inadequate capital and surplus, thereby forcing them to request that Congress underwrite the losses.

Noting that he was at the other extreme in his position regarding the advisability of carrying reserve and contingency accounts, Governor Szymczak expressed the view that, should the System be exposed to losses such as contemplated by Governor Mills, it would not be any more nationalized than at present.

The Chairman concurred, saying that he could explain the use of capital and surplus accounts as ordinary accounting procedure but that he was at a loss to explain the basis for the contingency reserve and over $60 million for depreciation.

Discussion ensued regarding the desirability of securing outside technical assistance with respect to the surplus and contingency reserve accounts, leaving the question of depreciation for later study, following which it was agreed to hold this question over for further consideration until the Chairman had had an opportunity to consult with Price Waterhouse to obtain a technical report.

Mr. Fauver, Assistant to the Board, entered the room during the foregoing discussion and Mr. Daniels withdrew at its conclusion.

Items distributed to the Board. The following items, which had been distributed to the members of the Board and copies of which are attached to these minutes under the respective item numbers indicated, were approved unanimously:

	Item No.
Letter to all Federal Reserve Banks regarding the use of real estate agents in providing tenants for Reserve Bank space, prepared pursuant to the understanding at the meeting on December 1, 1959.	3
Letter to Senator Douglas concerning the relationship of monetary policy to imperfections in the pricing mechanism and periodic surges in the demand for loanable funds from the private sector.	4
Draft of amendment to Regulation U, prepared for publication in the Federal Register for comment pursuant to the understanding at the meeting on December 1, 1959.	5

Messrs. Riefler, Hackley, and Brill withdrew at this point.

Definition of currency and coin in Regulation D (Item No. 6). There had been distributed under date of December 4, 1959, a draft of telegram to all Reserve Bank Presidents stating that the definition of currency and coin in Regulation D, including currency and coin in transit to and from a Federal Reserve Bank, was intended to apply to determination of currency and coin countable as reserves, and was not intended to change the practice of those Federal Reserve Banks that had been giving "as of" adjustments for money shipments to eliminate or reduce reserve deficiencies.

Mr. Farrell noted that the proposed telegram was intended to answer a question raised by certain Reserve Banks. It seemed desirable to provide this interpretation, he said, since it was not understood to have been the Board's intention, in permitting the inclusion of a portion of vault cash in reserves, to act in a manner detrimental to the existing position of member banks. The interpretation in the draft telegram would make it clear that the revised definition of currency and coin in Regulation D was not intended to cause any change from present practices in regard to the granting of "as of" adjustments.

Unanimous approval was then given to the telegram to all Reserve Bank Presidents of which a copy is attached as Item No. 6.

Messrs. Thomas, Molony, Farrell, and Noyes then withdrew from the meeting.

Appointment of national bank examiners as Federal Reserve examiners (Item No. 7). Governor Robertson noted that the procedures for examination of Edge Act corporations had been changed, pursuant to a proposal made in Mr. Goodman's memorandum of July 2, 1958, to provide that Federal Reserve examiners would be commissioned national bank examiners and authorized to examine such foreign branches of national banks as the Comptroller might designate, and that national bank examiners would be commissioned as Federal Reserve examiners and authorized to examine foreign branches of State member banks when engaged in examination work in other parts of the world. He said that

George S. Sloan was currently engaged in the examination of Latin American branches of a national bank in his capacity as a national bank examiner, with the assistance of two assistant national bank examiners, Francis R. Schilling and Donald Milne, and that it would be desirable to have these men examine the Virgin Island branches of The Chase Manhattan Bank as well as the Bank of America branch and agency in Guatemala. He referred to the minor expense to the System involved in these suggested examinations, which could be undertaken immediately should the Board approve the appointment of Messrs. Sloan, Schilling, and Milne as Federal Reserve examiners for this purpose. Expenses in connection with the examination of the Virgin Island branches of Chase Manhattan would be borne by the Board under the policy currently followed, he said, but the expenses in connection with examination of the branch and agency of Bank of America would be assessed against the Edge corporation. He suggested that the Board authorize reimbursement to the Comptroller of the Currency for pro-rata travel and per diem expense involved, the salaries of the two assistants, and such salary amount as would not be in conflict with the Board's retirement policy as regards Mr. Sloan, formerly Director of the Board's Division of Examinations. In conclusion, he observed that all of this would contemplate concurrence of the Comptroller of the Currency and clearance with the Superintendent of Banks of the State of New York regarding The Chase Manhattan branches.

Unanimous approval was then given to the appointment of Messrs. Sloan, Schilling, and Milne as Federal Reserve examiners for the purpose indicated, as well as to a letter to the Comptroller of the Currency informing him of such appointments. This letter is attached as Item No. 7.

At this point all of the members of the staff except Mr. Sherman and Mr. Fauver withdrew from the meeting.

Director appointments. Consideration was given to the appointment of directors at Federal Reserve Banks and branches where such appointments for the year 1960 had not yet been made. As a result of the discussion, it was agreed unanimously that the customary steps should be taken through the Chairmen of the Federal Reserve Banks concerned to ascertain whether the individuals listed below were eligible and would accept the appointments indicated and, if they were, to proceed to make such appointments.

1. To appoint J. C. Cowan, Jr., of Greensboro, North Carolina, as a director of the Charlotte Branch of the Federal Reserve Bank of Richmond for the three-year term beginning January 1, 1960.

2. To appoint John McGee Cheatham of Griffin, Georgia, as a Class C director of the Federal Reserve Bank of Atlanta for the three-year term beginning January 1, 1960.

3. To appoint Jack W. Warner of Tuscaloosa, Alabama, as a director of the Birmingham Branch of the Federal Reserve Bank of Atlanta for the three-year term beginning January 1, 1960.

4. To appoint Walton Maxey Jarman of Nashville, Tennessee, as a director of the Nashville Branch of the Federal Reserve Bank of Atlanta for the three-year term beginning January 1, 1960.

In the event Mr. Jarman was ineligible or for any reason was unable to accept appointment, the same steps would be taken with respect to Andrew David Holt, Knoxville, Tennessee, with a view to appointing him a director of the Nashville Branch for the three-year term beginning January 1, 1960.

5. To appoint John Cowles of Minneapolis, Minnesota, as a Class C director of the Federal Reserve Bank of Minneapolis for the three-year term beginning January 1, 1960. In the event Mr. Cowles was ineligible or was unable for any reason to accept such appointment, authority was given for the same steps to be taken with respect to Robert S. MacFarlane of Minneapolis with a view to appointing him a Class C director of the Federal Reserve Bank of Minneapolis for the three-year term beginning January 1, 1960.

6. To appoint James E. Allison of Tulsa, Oklahoma, as a director of the Oklahoma City Branch of the Federal Reserve Bank of Kansas City for the two-year term beginning January 1, 1960.

7. To appoint Robert Orville Anderson of Roswell, New Mexico, as a Class C director of the Federal Reserve Bank of Dallas for the three-year term beginning January 1, 1960.

8. To appoint Roger Bailey Corbett of University Park, New Mexico, as a director of the El Paso Branch of the Federal Reserve Bank of Dallas for the three-year term beginning January 1, 1960.

9. To appoint John R. Stockton of Austin, Texas, as a director of the San Antonio Branch of the Federal Reserve Bank of Dallas for the three-year term beginning January 1, 1960.

The following actions were taken:

1. O. B. Jesness, presently a Class C director and Deputy Chairman of the Federal Reserve Bank of Minneapolis, was designated Chairman and Federal Reserve Agent for the year 1960 and his compensation was fixed on the uniform basis for the same position at all Federal Reserve Banks, i.e., the same amount as the aggregate of the fees payable during the same period to any other director for attendance corresponding to his at meetings of the board of directors, executive committee, and other committees of the board of directors.

2. Lamar Fleming, Jr., presently a Class C director of the Federal Reserve Bank of Dallas, was designated Deputy Chairman of that Bank for the calendar year 1960.

3. Y. Frank Freeman, presently a Class C director of the Federal Reserve Bank of San Francisco and Deputy Chairman, was reappointed Deputy Chairman for the calendar year 1960.

Chairman Martin reported that, pursuant to the action of the Board at the meeting on November 30, 1959, he had talked with Philip D. Reed with respect to appointment as a Class C director and Chairman of the Federal Reserve Bank of New York and that he was to see Mr. Reed for further discussion of this matter when he was in New York later this week.

Governor Mills inquired whether Mr. Reed contemplated retaining his directorship with an insurance company, to which Chairman Martin replied that he had not mentioned this point but assumed Mr. Reed would retain that directorship. He stated, however, that he would discuss with Mr. Reed the views that the Board had previously expressed with respect to the service of a director of the Federal Reserve Bank of New York as a member of the finance committee of an insurance company.

Messrs. Sherman and Fauver then withdrew from the meeting and the Board went into executive session.

Salary of Mr. Mangels. Following the meeting, Chairman Martin informed the Secretary that during the executive session the Board unanimously approved the payment of salary to H. N. Mangels, President

of the Federal Reserve Bank of San Francisco, at the rate of $40,000 a year for the calendar year beginning January 1, 1960.

The meeting then adjourned.

Secretary's Notes: On December 3, 1959, Governor Shepardson approved on behalf of the Board the recommendation contained in a memorandum from the Division of Personnel Administration dated December 2, 1959, that the pay and leave of Board employees who were on duty on July 3, 1959, be adjusted in conformity with the Comptroller General's decision of November 23, 1959, designed to reconcile the provisions of Executive Order No. 10825, dated June 12, 1959, with those of Public Law 86-362, which was approved September 22, 1959, retroactive to July 1, 1959.

After consideration of the information contained in a memorandum dated December 1, 1959, from Mr. Fauver, Governor Shepardson also approved on behalf of the Board on December 3, 1959, a visit to the Board's offices on Wednesday, February 3, 1960, from 11 to 11:45 a.m. by members of the National Association of Mutual Savings Banks.

On December 4, 1959, Governor Shepardson approved on behalf of the Board a letter to the Federal Reserve Bank of San Francisco (attached Item No. 8) approving the appointment of Stuart S. Lowe, Jr., as examiner.

Pursuant to the recommendation contained in a memorandum dated December 2, 1959, from Mr. Fauver, Governor Shepardson today approved on behalf of the Board a visit by a group of 22 participants in the Economic Development Institute sponsored by the International Bank for Reconstruction and Development on December 10, 1959, for a program which would include luncheon in the Staff Dining Room.

Governor Shepardson informed the Secretary that there had been brought to the attention of the members of the Board a memorandum dated December 3, 1959, in which Mr. Young, Director, Division of Research and Statistics, reported an inquiry from the Department of State as to whether the Board would make time available to him to attend a two-day OEEC technical conference to be held in Paris, France, sometime between January 7 and January 17, 1960. Governor Shepardson advised that it had been agreed to accede to the request of the State Department, with the understanding that expenses incident to Mr. Young's travel would be paid by the Board on a nonreimbursable basis. (In connection with this trip by Mr. Young, which also included a brief stop in London to visit the Bank of England, Governor Shepardson later approved on behalf of the Board an amount for official representation expenses not to exceed $100.)

Secretary

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON 25, D. C.

Item No. 1
12/7/59

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

December 7, 1959.

Mr. Delos C. Johns, Chairman,
Conference of Presidents,
c/o Federal Reserve Bank of St. Louis,
P.O. Box 442,
St. Louis 66, Missouri.

Dear Mr. Johns:

This refers to the recommendations in connection with coin-wrapping policy made by the Conference of Presidents at the joint meeting with the Board on September 23, 1959, that--

(1) The timing of imposition of wrapped coin charges based on the cost-recovery formula adopted by the Presidents' Conference be left to the discretion of the individual Reserve Banks providing such service.

(2) 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.

The Board concurs in the proposal to leave to the discretion of the individual Reserve Banks concerned the question of when to revise their charges to conform to the formula adopted by the Presidents, with the understanding that the Board will be informed when the new charges are made effective. While no specific time limit for applying the revised charges is set, the Board's concurrence in this proposal is based on the comments at the joint meeting on September 23 as recorded in the minutes of that meeting.

The Board believes that the wrapping of coin is essentially a retail type of operation that goes beyond the function of the Reserve Banks as the primary source of supply for currency and coin. It recognizes that many small banks can not afford modern coin-wrapping equipment and that there are economies inherent in a centralized operation, but it does not believe that these arguments are

persuasive reasons for furnishing the service at less than cost. Accordingly, the Board does not accept the Presidents' recommendation 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.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

Item No. 2
12/7/59

OFFICE OF THE CHAIRMAN

December 7, 1959.

Mr. Alfred Hayes, President,
Federal Reserve Bank of New York,
New York 45, New York.

Dear Al:

Enclosed is a copy of a letter that has been sent to the Chairman of the Presidents' Conference with regard to coin-wrapping policy.

The Board is not unsympathetic to the bank relations problems this letter may cause you. It believes, however, that the justification for any coin-wrapping services by the Reserve Banks is somewhat tenuous and that the furnishing of wrapped coin at less than cost, even on a limited basis, increases the System's vulnerability to criticism in this connection to an undesirable extent.

The question of coin-wrapping policy has been carefully considered over a period of several years, and the Board is of the firm opinion that it is not appropriate for the Federal Reserve Banks to offer coin wrapping as a free service for member banks. The Board therefore feels that it should not authorize any exception to the policy of recovering substantially the cost of any coin-wrapping service that may be offered.

Sincerely yours,

(Signed) Wm. McC. Martin, Jr.

Wm. McC. Martin, Jr.

Enclosure

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON 25, D. C.

Item No. 3
12/7/59

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

December 7, 1959.

Dear Sir:

The Board's letter of June 12, 1953 (F.R.L.S. #3188.1) concerns the leasing of unused space in new Federal Reserve Bank buildings or additions pending need of such space for bank operations.

Recently a question was raised whether there would be any objection to finding tenants through real estate brokers.

While each situation should be decided on its own merits, and in some instances it might be necessary as a last resort to pay real estate commissions, the Board is of the opinion that in general it would be preferable for the Reserve Banks to obtain their own tenants.

Very truly yours,

Merritt Sherman,
Secretary.

TO THE PRESIDENTS OF ALL FEDERAL RESERVE BANKS

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

Item No. 4
12/7/59

OFFICE OF THE CHAIRMAN

December 9, 1959.

The Honorable Paul H. Douglas,
United States Senate,
Washington 25, D. C.

Dear Senator Douglas:

Thank you for your letter of November 5, expressing your appreciation for the Board's contribution to your Committee's study of Employment, Growth, and Price Levels.

For our part, we have been most impressed with the fine work that your Committee and its staff have been doing in bringing together the thinking of qualified persons, in formulating questions to be addressed to us and to other agencies, and in the studies thus far published.

In reading over the material that has been presented to your Committee, it occurs to me that there are two aspects of the problems under study that may deserve more explicit consideration than has been given to them so far. For this reason, I am taking the liberty of bringing them to your attention in this letter.

The first point that I have in mind relates to imperfections in our price system--variously referred to as cost-pushes, ratchet effects and administered prices--and perhaps it can best be phrased in the form of a question. Granting that there are these imperfections as regards the behavior of individual prices and that they create inflationary pressures or biases in economic processes that cannot be effectively dealt with by monetary policy, does it follow from this that monetary policy should be less (or more) restrictive than if such phenomena did not exist? I am sure that all serious students of economic policy are concerned with this question, and to some extent, their views are implied in their responses to other questions. I know this is true, for example, in the case of much of the material which the Federal Reserve has furnished to your Committee.

As I understand it, the argument presented by those who advocate acceptance of creeping inflation is that institutional factors which are not dealt with directly by Government action

are likely to cause money wages and administered money prices in certain basic industries, to increase more rapidly than is consistent with full employment of the labor force and the growth of other productive resources. Therefore, unless these wages and prices are, in effect, reduced by inflating the price of everything else, we will suffer from chronic underemployment. In other words, these advocates suggest that monetary and, indeed, fiscal policy as well, should be used openly to frustrate the bargaining efforts of organized labor and the pricing policies of certain industries. Only in this way, they imply, can a workable equilibrium be achieved between the marginal productivity of labor and real wages and between the relative prices of competitively marketed and administered price goods.

The objections to a policy of deliberately engineered creeping inflation seem to me to be manifold. I hope the problems generated by such a policy, with respect to the whole process of saving and investment and for the balance of payments, have been adequately treated in my responses, and those of others, to the questions asked by your Committee. If this is the case, all that needs to be said here is that these problems would be greatly intensified by any effort to absorb wage increases and administered prices through calculated inflation.

Beyond this, I think there is a very serious question as to whether such a policy could possibly succeed in the accomplishment of its primary objective. Would those who are in a position to administer prices or extract wage settlements in excess of productivity gains be content to maintain the same pace when they discovered that their efforts to capture a larger share of the real income stream were being frustrated by calculated inflation? Would they not increase their demands further to improve their relative position?

Thus, it seems probable that, far from encouraging a high level of employment and growth in the economy, a policy of calculated creeping inflation would not make any contribution--and certainly not a lasting one--toward the correction of the difficulties toward which it was directed. On the contrary, it would involve all of the social injustices that economists universally agree accompany inflation, and it would also disrupt the saving and investment process, which must function efficiently if vigorous growth and high level employment are to be sustained.

If we reject a policy of deliberate inflation, what should be the role of monetary policy in a situation in which the

over-all price level or average of prices is being pushed up by administered costs and prices? Increases in the general level of prices, and the expectation of further increases, regardless of their origin, diminish the incentive to save and increase the incentive to borrow. Hence, unless credit expansion is limited to a rate of growth consonant with the increase in the physical output of goods and services a cost-push inflation will automatically become a demand-pull inflation as well. This point is spelled out in one of the papers I referred to in my replies to your Committee, but I would like to quote it in this context.

"It is the fact of rising prices or anticipation of rising prices that provides the incentive to borrow to finance overaccumulation of inventories and the construction of plant capacity in advance of need. It is the fact of rising prices or the anticipation of rising prices that leads to misallocations of investment and miscalculation of investment decisions. It is rising prices or the anticipation of rising prices that diverts savings into equities, and that dissipates their ability to finance growth, in short, that diminishes the supply of loanable funds and accentuates the demand in such a way as to force high and rising interest rates. Finally, it is the fact that a country's prices have risen above those of its competitors that prices a country out of world markets and initiates a deficit in the balance of payments. All of these reactions, which place great strains on the monetary and fiscal mechanism, ensue irrespective of whether an inflation may be described as cost-push or demand-pull.

"In the credit market, these situations increase the profitability of operating on borrowed funds even at very high interest costs. They increase, therefore, the demand for borrowed funds far above the amounts made available by savings and unless they are resisted by appropriate fiscal and monetary policies, i.e., by balanced budgets and by restraints on the availability of reserves, they result inevitably in an expansion of bank-created money.

"Because borrowing to anticipate inflation appears very profitable, the pressure of customers on their banks to borrow is very heavy and this in turn brings pressure on the Federal Reserve Banks to expand reserves. If this pressure is resisted, interest rates may have to rise quite sharply before the force toward overexpansion is contained. If the pressure is not contained and bank-created money is used to finance these hedges against inflation, the inflation, even if it started as a cost-push type, will by that very fact be converted into one of the demand-pull variety."

This indicates how the pressure of cost-pushes on price levels leads to conditions in which monetary policy tends to be forced into a more restrictive position than would otherwise be the case and the level of interest rates tends to be higher than would otherwise be required to maintain the balance between savings and investment. On the one hand, it gives strong support to the desirability of direct and vigorous attack on cost-push elements themselves. On the other hand, it suggests to me that the adoption of a "stable plus cost-push" goal for prices could not lead to anything but trouble. It would both encourage the proliferation of cost-pushes and, at the same time, provide the demand-pull to match them. We come back to what appears to me the inescapable conclusion that deviation from the objective of reasonable price stability for all arms of public economic policy would multiply our difficulties, not reduce them.

The second, and related question which I think deserves more examination and probing, might be stated as follows: Does the demand for credit from consumers and for private investment sometimes converge on the market with such vigor that it defies any reasonable application of general monetary and fiscal measures, producing either uncontainable inflationary forces or the impoverishment of certain socially desirable programs which are unable to compete for loanable funds, and perhaps having both effects? If this happens, should an attempt be made to expand bank credit sufficiently to satisfy all creditworthy borrowers at a lower rate of interest than the demand and supply relationship between real savings and investment would establish? This sort of a surge in the demand for credit in the private sector, it is argued, presents a problem not unlike that to be faced should the Federal Government be required to expand its expenditures and borrowing rapidly in a defense emergency. The implication is that bank credit expansion--a form of forced saving through inflation--is the only way to meet this problem so as to prevent socially undesirable distortions in the economic system.

To me, this line of reasoning is indefensible, on both moral and economic grounds. To the extent that such a program could succeed, even temporarily, it could do so only because the public was deceived as to the nature of the policy and its effects. The moral objection to any national policy based on public deception seems to me overwhelming. On economic grounds, this kind of monetary policy could not possibly succeed for more than a very short period. Even before the economic effects became fully apparent, they would be anticipated by those who would seek to protect themselves from the ravages of inflation, or to profit from it. The inevitable result would be a rapid decline in the volume of savings and an even more rapid rise in the rate of interest than would otherwise have occurred.

Rather than inflation, the first approach to a solution to this problem lies in a sound general monetary and fiscal policy. Of equal importance is the elimination of those imperfections in the operation of the price and wage mechanism mentioned in connection with my first point. If we do these things I believe there is a strong likelihood that we will avoid the kind of surges of credit demand that are postulated. If they still occur then we should certainly consider the application of selective controls on credit use by consumers and businesses. I would like to hope that these can be avoided because I am sure that they are bound to interfere with the process by which resources are directed to their most efficient uses in a free enterprise economy. When one weighs the alternatives, it seems clear that such controls would be preferable to either calculated or uncontrolled inflation, but we should recognize that they involve a degree of regimentation never before accepted in this country except in time of war.

I have addressed myself to these questions at some length because I think there may have been some real misunderstanding of my position. My interest in a monetary policy directed toward a dollar of stable value is not based on the feeling that price stability is a more important national objective than either maximum sustainable growth or a high level of employment, but rather on the reasoned conclusion that the objective of price stability is an essential prerequisite to their achievement.

I want to emphasize that I am most concerned with the preservation of freely competitive markets and the correction of any institutional imperfections which exist in the working of the price mechanism. While such imperfections cannot be corrected simply by a sound monetary and fiscal policy; they surely cannot be corrected by an unsound financial policy.

Nor does a sound general monetary policy necessarily, in itself, accomplish the optimum distribution of loanable funds among various sectors of the economy. It is not only the right but the duty of Government to assure that socially necessary programs are adequately financed. But, again, this objective can never be well served by unsound general monetary or fiscal policies. If, as a matter of public policy, the financing of school construction, for example, should have an over-riding priority in the allocation of resources, this can be accomplished in a number of ways, but we can be sure that it would not be accomplished by the general expansion of bank credit and money.

I trust that these additional comments will be helpful to your Committee in its work of clarifying for the Congress and

the nation the basic issues involved in attaining and maintaining optimum levels of employment and vigorous growth, as well as a structure and level of prices conducive to both.

Sincerely yours,

(Signed) Wm. McC. Martin, Jr.

Wm. McC. Martin, Jr.

Item No. 5
12/7/59

FEDERAL RESERVE SYSTEM

[12 CFR PART 221]

[Reg. U]

LOANS BY BANKS FOR THE PURPOSE OF PURCHASING
OR CARRYING REGISTERED STOCKS

NOTICE OF PROPOSED RULE MAKING

Part 221 [Regulation U], issued by the Board of Governors of the Federal Reserve System pursuant to the authority cited therein, prescribes the maximum loan value of the collateral in the case of any loan by a bank which is secured directly or indirectly by any stock and made for the purpose of purchasing or carrying any stock registered on a national securities exchange (a "purpose loan").

One of several amendments to this Part adopted by the Board June 15, 1959 (24 Federal Register 3867), broadened the provisions of § 221.3(b)(1) relating to the definition of "carrying" in order more effectively to prevent the excessive use of credit for purchasing or carrying securities. This amendment has given rise to a number of questions leading to interpretations of the section. With a view to making these interpretations more readily available, the Board is considering a proposed amendment which would draw together and codify them and include them in the proposed new wording of the section.

The first sentence of the present § 221.3(b)(1) provides that a loan need not be treated as a loan for the purpose of "carrying" registered stock which the borrower has owned free of any lien for a continuous period of as much as one year. The proposed amendment would make it clear, in affirmative language, that a loan is to be deemed a loan for the purpose of "carrying" if the borrower owns any registered stock, whether or not pledged as security for the loan, which he has not owned free of any lien for a continuous period of as much as one year, subject to the exceptions stated in the present regulation, viz., loans for the purpose of meeting emergency expenses not reasonably foreseeable at the time the stock was acquired or for meeting recurring expenses which the borrower has customarily met by temporary borrowing. The proposed amendment would also except loans made for "substantially similar purposes". Whether these exceptions apply is, of course, a question of fact to be determined in the light of the circumstances of the particular case.

The proposed amendment would further make it clear that any such loan is to be considered a purpose loan <u>only</u> to the extent of the current market value of the registered stock owned by the borrower at the time of the loan less any credit outstanding for the purchase or carrying of such stock. In other words, a loan of $5,000 to a borrower who has owned for less than a year registered stock with a current market value of $1,000 would be a loan for the purpose of "carrying" only to the extent of $1,000 and

would require collateral as provided by the regulation for a loan in such amount. (The loan would not, of course, be for the purpose of "carrying" if it fell within one of the exceptions described above.)

The proposed amendment would also make it clear that the "one year rule" is applicable only with respect to loans made after June 15, 1959. Loans made prior to that date, even though they would have been purpose loans under the present regulation, would not become subject to the requirements of the regulation.

Finally, the proposed amendment would make it clear that, in determining the one year period, there may be included any period during which the borrower owned other stock where such stock was sold and registered stock immediately purchased with the proceeds and also the period during which any registered stock received by the borrower by way of gift or inheritance was previously held by the donor or decedent.

In considering both the existing and proposed wordings of the section, it should be noted that (with exceptions not relevant here) the margin and retention requirements imposed by this regulation apply only to purpose loans by banks where the loans are secured, directly or indirectly, by some stock. However, the question whether a loan is for the purpose of "carrying" is different from questions concerning collateral. If the loan is a "purpose" loan (and is secured by <u>some</u> stock), then the margin requirements of the regulation apply, regardless of whether or not the collateral includes the particular stock being "purchased" or "carried".

Moreover, it should be borne in mind that the purpose of the regulation is not to be defeated by collusive or evasive arrangements, as, for example, where the borrower is a corporation and stock to secure the loan is pledged by a third person who controls the borrower and who owns registered stock acquired within the previous year.

The proposed amendment to § 221.3(b)(1) is as follows:

(b)(1) Under this Part, a loan is deemed to be for the purpose of "carrying" a stock registered on a national securities exchange to the extent that the loan is used directly or indirectly to reduce or retire indebtedness incurred to purchase or carry any stock so registered. Under this Part, a loan made after June 15, 1959 to a borrower who owns stock registered on a national securities exchange, which he has not owned free of any lien for a continuous period of at least one year, also is deemed to be for the purpose of "carrying" that stock to the extent of its current market value at the time the loan is made less any credit already outstanding for purchasing or carrying that stock; provided, that such a loan shall not be deemed to be for the purpose of carrying such stock if the loan is to be used to meet emergency expenses not reasonably foreseeable at the time the stock was acquired or to meet recurring expenses which the borrower has customarily met by temporary borrowing, or for a substantially similar purpose. For purposes of the preceding sentence, the period during which the borrower has

owned any stock so registered which was received by gift or inheritance (but not as compensation or by exercise of an option) shall be deemed to include the period of ownership of the donor or decedent; and the period during which the borrower has owned any stock so registered which was

(i) purchased immediately with the proceeds from the sale of any other stock,

(ii) received in exchange for any other stock in connection with a corporate reorganization or recapitalization, or

(iii) received in respect to any other stock as a result of a stock split or stock dividend (but not by exercise of subscription rights),

shall be deemed to include the period during which the borrower owned the other stock.

This notice is published pursuant to section 4 of the Administrative Procedure Act and section 2 of the Rules of Procedure of the Board of Governors of the Federal Reserve System (12 CFR 262.2). The proposed change is authorized under the authority cited at 12 CFR 221.

To aid in the consideration of the foregoing matter, the Board will be glad to receive from interested persons any relevant data, views, or arguments. Although such material may be sent directly to the Board, it is preferable that it be sent to the

Federal Reserve Bank of the district which will forward it to the Board to be considered. All such material should be submitted in writing to be received not later than January 11, 1960.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.

(SEAL)

TELEGRAM
LEASED WIRE SERVICE

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON

Item No. 6
12/7/59

December 7, 1959.

To the Presidents of all Federal Reserve Banks

Definition of currency and coin in Regulation D, including currency and coin in transit to or from a Federal Reserve Bank, was intended to apply to determination of currency and coin countable as reserves, and was not intended to change the practice of those Federal Reserve Banks that have been giving "as of" adjustments for money shipments to eliminate or reduce reserve deficiencies. It is assumed, of course, that "as of" adjustments resulting in duplicate credit will be avoided.

(Signed) Merritt Sherman
Sherman

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON 25, D. C.

Item No. 7
12/7/59

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

December 7, 1959.

The Honorable Ray M. Gidney,
Comptroller of the Currency,
Main Treasury Building,
Washington 25, D. C.

Dear Mr. Gidney:

This will confirm Mr. Goodman's telephone conversation this afternoon with Chief National Bank Examiner Haggard advising that, in line with earlier discussions with Mr. Haggard, at a meeting this morning the Board of Governors approved the appointment of National Bank Examiner George S. Sloan and Assistant National Bank Examiners Francis R. Schilling and Donald Milne as Federal Reserve Examiners for the purpose of examining the four Virgin Island branches of The Chase Manhattan Bank, New York, a State member bank, and the Guatemala City branch and agency of Bank of America, New York, a corporation organized under the provisions of Section 25(a) of the Federal Reserve Act. Chief National Bank Examiner Haggard advised informally that Mr. Sloan will be able to conduct the examinations as discussed informally with Mr. Sloan during his recent visit.

The Board appreciates the cooperation of your Office in arranging for Mr. Sloan to conduct these examinations, and you will understand, of course, the Board will reimburse your Office for the expenses involved upon such basis as may be agreed upon.

In line with Mr. Haggard's suggestions, appropriate commissions will be forwarded direct to Mr. Sloan covering these examinations.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON 25, D. C.

Item No. 8
12/7/59

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

December 4, 1959.

CONFIDENTIAL (FR)

Mr. Eliot J. Swan, First Vice President,
Federal Reserve Bank of San Francisco,
San Francisco 20, California.

Dear Mr. Swan:

In accordance with the request contained in your letter of November 25, 1959, the Board approves the appointment of Stuart S. Lowe, Jr., as an examiner for the Federal Reserve Bank of San Francisco, effective January 1, 1960.

It is noted that Mr. Lowe is indebted to the San Jose Office of The Hibernia Bank, San Francisco, California, a nonmember bank, in the amount of $12,825.06, for the purchase of a home. Accordingly, the Board's approval of the appointment of Mr. Lowe is given with the understanding that he will not participate in any examination of The Hibernia Bank until his indebtedness has been liquidated.

Very truly yours,

(Signed) Kenneth A. Kenyon

Kenneth A. Kenyon,
Assistant Secretary.