

The attached minutes of the meeting of the Board of Governors of the Federal Reserve System on February 15, 1965, which you have previously initialed, have been amended at the suggestion of Governor Shepardson to revise the language of the paragraph beginning at the bottom of page 25 and continuing on page 26.

If you approve the minutes as amended, please initial below.

Chairman Martin

Governor Robertson

Handwritten initials 'M' and 'R' on two horizontal lines. The 'M' is written inside a circle on the top line, and the 'R' is written on the bottom line.

13609

Minutes for February 15, 1965

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

W

Gov. Mills

Gov. Robertson

R.

Gov. Balderston

CCB

Gov. Shepardson

[Signature]

Gov. Mitchell

[Signature]

Gov. Daane

[Signature]

Minutes of the Board of Governors of the Federal Reserve System on Monday, February 15, 1965. The Board met in the Board Room at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Balderston, Vice Chairman
Mr. Mills
Mr. Robertson
Mr. Shepardson 1/
Mr. Mitchell

Mr. Sherman, Secretary
Mr. Kenyon, Assistant Secretary
Mr. Noyes, Adviser to the Board
Mr. Molony, Assistant to the Board
Mr. Fauver, Assistant to the Board
Mr. Hackley, General Counsel
Mr. Brill, Director, Division of Research and Statistics
Mr. Farrell, Director, Division of Bank Operations
Mr. Solomon, Director, Division of Examinations
Mr. Johnson, Director, Division of Personnel Administration
Mr. Schwartz, Director, Division of Data Processing
Mr. O'Connell, Assistant General Counsel
Mr. Shay, Assistant General Counsel
Mr. Kiley, Assistant Director, Division of Bank Operations
Mr. Leavitt, Assistant Director, Division of Examinations
Mr. Smith, Assistant Director, Division of Examinations
Mr. Smith, Senior Economist, Division of Research and Statistics

Conference on merger and holding company applications (Item No. 1). There had been distributed a draft of letter to the Federal Reserve Banks indicating that a one-day conference at the Board was

1/ Withdrew from meeting at point indicated in minutes.

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planned for March 17, 1965, to consider ways in which the Research Departments of the Federal Reserve Banks could improve their contributions to the material prepared by the Banks and submitted to the Board on bank merger and bank holding company applications. The conference would be attended by representatives of both the Research and Examinations Departments from the respective Banks. One problem to be considered involved the various techniques for the analysis of banking markets and the applicability of those techniques to questions raised by merger and holding company cases. A proposed agenda for the conference was included with the material submitted to the Board.

In discussion Governor Mitchell suggested preparation by the Legal Division of a report on the competitive aspects involved in the bank merger and bank holding company cases decided by the Board last year, with a view to indicating the kinds of facts that were needed to make a proper determination. Explaining his suggestion further, he observed that a number of those cases had involved extension of the activities of a bank into a new area so that the question of overlapping of service areas was not pertinent. When the service areas did not overlap, that might be the end of the story so far as the competitive factor was concerned unless one got into the question of banking concentration. What he had in mind was that research personnel could then come forward with the kinds of evidence

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that would make it easier for the Board to reach a conclusion on this type of case. In many cases coming before the Board he felt that a great deal of information was included that was not necessary for the purpose of reaching a determination. This suggested that some selection of material should be made, and he felt that the Legal Division in outlining the issue of competition could narrow down the amount of information that had to be gathered in particular types of cases. To put it another way, he believed that proper determinations often could be reached with less burden by combing out irrelevant material.

Governor Balderston noted that the Federal Advisory Council at its most recent meeting with the Board had commented on the amount of time that elapsed before decisions were rendered by the Board on merger and holding company cases. He inquired whether information was available showing the amount of elapsed time that occurred last year as compared with previous years, and Mr. Solomon indicated that such information could be compiled if desired.

Governor Balderston also commented that he thought sometimes the Board reached adverse decisions in cases where the other bank supervisory agencies would not have reached such a decision. He was encouraged by the fact that continuing study was being given to the matter, as evidenced by the proposed conference.

Mr. Solomon commented that the affected banks sometimes did not like the way cases were decided by the Board and felt that another

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bank supervisory agency would have decided the cases differently. He mentioned, in this connection, recent applications from two Pennsylvania banks to withdraw from System membership since they were proposing to merge and apparently preferred to file an application with the Federal Deposit Insurance Corporation. Asked whether the Corporation's actions on merger cases appeared to be closer to those of the Board than the decisions rendered by the Comptroller of the Currency, Mr. Solomon said that the Corporation denied virtually no merger applications. However, the cases coming before the Corporation were usually of a considerably different character than those coming before the Board.

At the conclusion of the discussion, the calling of the proposed conference on bank merger and holding company cases was authorized, and the letter to the Federal Reserve Banks was approved unanimously. A copy of the letter is attached as Item No. 1.

Messrs. O'Connell and Smith (Research) then withdrew from the meeting.

Examination and supervision of Reserve Banks. In a memorandum dated April 25, 1963, Governor Shepardson summarized the Board's discussion of March 25, 1963, regarding examination and supervision of the Federal Reserve Banks. As pointed out in his memorandum, the Board had desired among other things a more clear-cut delineation of the areas of responsibility and methods of cooperation on the part of

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the Board's several divisions having responsibilities in relation to functions of the Federal Reserve Banks. For the purpose of working out this delineation, Governor Shepardson appointed a staff committee composed of Mr. Solomon as Chairman and Messrs. Noyes, Brill, Farrell, and Johnson.

As part of its review in 1963 of the examination of the Reserve Banks by the Division of Examinations the accounting firm of Haskins & Sells recommended a new directive from the Board to the Division of Examinations. On April 1, 1964, the Board adopted a new directive and on April 6, 1964, Governor Shepardson suggested to the staff committee that it use the directive as a model and prepare proposed directives for other divisions, as well as a general directive to relate the several directives to each other.

With a memorandum dated January 15, 1965, which had been distributed, the staff committee submitted drafts of such a set of directives. Portions of the April 1, 1964, directive to the Division of Examinations that seemed susceptible of general application had been transferred to a general directive to all divisions. Directives covering other functions had been prepared by the respective divisions, including those not represented on the staff committee, and had been reviewed by the committee.

In addition, the staff committee presented for the Board's consideration several matters that it felt deserved special mention.

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These related to responsibility for reviewing the administration of the discount window and responsibility for Protection Departments, Planning Departments, relations of Reserve Bank directors, and coordination of Reserve Bank purchasing.

Following introductory comments by Mr. Solomon, Governor Shepardson noted that the proposed directives to the divisions represented an effort to compile in a regularized manner various assignments that had been given to the divisions, either formally or informally, from time to time. In addition to the matters covered in the proposed directives, five items that did not appear to be covered were presented for the Board's consideration.

Discussion then turned to the first of these items, which related to the discount window. The staff committee had pointed out that at each examination of a Reserve Bank the Division of Examinations makes a thorough review of the Bank's discount and credit function. However, Reserve Bank lending to member banks that might be construed as inconsonant with Regulation A, Advances and Discounts by Federal Reserve Banks, could have occurred early in the period covered by the examination review. The staff committee also pointed out that at the close of each weekly or biweekly reserve computation period the Division of Bank Operations receives reports showing, by names of borrowing banks, the average figures for required reserves and borrowings from the Reserve Bank. Statistical tabulations derived

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from these data were furnished to the Board, but the information did not show whether or not the borrowings were justified. While no member of the Board's staff appeared to have a continuing responsibility for following up on interim questions that might arise concerning Reserve Bank discount policies, the Board itself gave a great deal of attention to this function and discussed it frequently with Reserve Bank personnel on the basis of examinations of individual Reserve Banks or otherwise. Also, the Board had directed Mr. Holland, Associate Director, Division of Research and Statistics, a staff member with special competence in the field because of his former experience as a Reserve Bank discount officer, to review and analyze the data received currently from the Reserve Banks for the purpose of ascertaining any apparent deviations in lending practices from the principles enunciated in Regulation A. Recently instituted meetings of the discount officers of the Reserve Banks, in which Mr. Holland participated, should further improve the administration of the function. While the arrangements currently in effect appeared to provide adequate attention to the discount and credit function, the staff committee recommended that the present ad hoc assignment of Mr. Holland be formalized by assigning him the responsibility for bringing to the attention of the Board, after consultation with and in coordination with the Division of Examinations, any questions regarding the discount function that might arise between examinations of the Reserve Banks.

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Governor Mitchell expressed concern, based on his review of examination reports, that the Division of Examinations was not describing cases of continuous borrowing sufficiently to indicate whether the borrowing was justified or appropriate. Neither did the data received from the Division of Bank Operations indicate whether the borrowing that had taken place was appropriate. The suggestion by the staff committee might be appropriate if Mr. Holland was prepared to look into the facts behind the performance of borrowing banks.

Governor Balderston noted that Governor Mitchell had touched on a point of fundamental management philosophy. If a member bank had borrowed for a certain period of time, this was a fact for the Division of Examinations to report. The circumstances that led the discount officer, who reported to the Reserve Bank President, to permit the borrowing to go on involved a value judgment, and Governor Balderston indicated that he would be concerned about having an examiner substitute his judgment for that of the discount officer. This was a delicate area, and comments by examiners should not be allowed to color the decisions of those who had primary responsibility for administration of the discount window.

Governor Robertson suggested that the facts could be set forth without giving the examiner the power to criticize. The examiner should report what borrowing had taken place and why it had taken place, on the basis of information furnished by the discount officer.

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Governor Mitchell said that he wanted to encourage people to proceed on their own responsibility. However, the essence of an audit was to have examiners go over operating information to see if the operations were being conducted properly and, if not, to assure that they would be conducted properly thereafter. This meant that in the case of the discount window the reasons for borrowings should be spelled out adequately in order to reach a judgment on whether the rules had been followed.

Mr. Solomon commented that the question was how much the Board wanted to be burdened. The examiners reviewed carefully all cases where there had been any appreciable amount of borrowing. Following this review, the question that came up was whether the borrowing involved anything sufficiently close to a possible conflict with the principles of Regulation A so that the matter should be reported to the Board or discussed with the Reserve Bank management, and whether any reference to the matter should be included in the examination report. Such decisions were reached after thorough study. If it was decided that there seemed clearly to be no conflict with the principles of Regulation A, the matter was dropped. If there was any doubt, the situation was brought before the Board for consideration.

Governor Mitchell said he thought this was the right approach, although he might have had a somewhat different judgment in certain cases. It was his impression that the examination reports did not

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give enough evidence on the reasons for borrowing, but it might be that a shading of judgment was involved.

Mr. Brill commented that if the suggestion of the staff committee was followed, this would require some gearing up personnel-wise in the Research Division to take care of the responsibility. If cases of borrowing were followed up closely, a rather significant work burden would be involved.

Mr. Farrell indicated some concern about adequacy of information in the examination reports. Sometimes it was indicated that cases of continuous borrowing had been taken up by the Reserve Bank with the member bank and that the borrowing had been discontinued, but this implied that the member bank borrowed as long as the Reserve Bank was willing to acquiesce. There was nothing to indicate why the Reserve Bank had waited six months, for example, or why renewals of initial borrowing were necessary in the first instance. He saw a need for agreement within the System on a uniform approach to what constituted abuse of the borrowing privilege and what constituted justification for exceptional cases.

Governor Mills indicated that he would be somewhat fearful of policing at Board level the discounting of member banks. This was an area where the discretion of the Reserve Bank management should be acknowledged, except in aggravated cases. As a general statement, it was his impression that at some Reserve Banks the administration of

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the discount window had been consistently too liberal. In other Reserve Banks the relationship of the management to the member banks was such as to prevent abuse of the discount window effectively. At such Banks there might have been great pressure on the discount window if the Reserve Bank management had not brought member banks to an understanding of the principles of discounting and what was appropriate or inappropriate. In his view the day-to-day administration of the discount window should be handled at the level of the Federal Reserve Banks. If the Board became deeply involved, it would be the final arbiter rather than the Reserve Banks. As a general rule, he felt that cases where the Board expressed a direct interest should be rare. He would be concerned if the Board injected itself too deeply into individual cases of discounting.

Governor Robertson expressed the view that the Board normally should not divide up a responsibility between two units of its staff. In the matter of discount window activity, he felt that the Division of Examinations should have full responsibility for reviewing discount operations in connection with examinations, presenting questionable cases to the Board, and following up on those cases. On the other side, it was appropriate for Mr. Holland and the Research Division to review discount operations generally, that is, the broad scope of the discount function, to determine whether the discount window was being operated in the best possible way. But Mr. Holland

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and the Research Division should not go into each individual case. Leadership should be exercised in the way in which it was now being exercised, that is, through frequent meetings of the discount officers in order to obtain a uniform approach, and Mr. Holland's association with that group should continue. But the role of the Research Division should be in terms of broad coverage, not specific cases. Accordingly, he would be opposed to the suggestion of the staff committee.

Governor Shepardson indicated somewhat the same feeling. The meetings of the discount officers, in which Mr. Holland participated, were desirable in order to develop any change in discount window policy that might be deemed appropriate, but responsibility within the Board's staff should not be split. The Division of Examinations looked at the discount records on the occasion of Reserve Bank examinations, and any follow-up should be made by the same Division. Furthermore, Mr. Holland was already heavily burdened, and it would not be desirable to assign him responsibility for detailed follow-up of cases of discounting. As to examination reports, Governor Shepardson said that like Governor Mitchell he sometimes noticed that a report indicated a Reserve Bank had talked with a member bank about the borrowing situation, but the report contained no indication as to the nature of the situation. There was the question how much detail should be included in the examination reports, but he had felt there would be some advantage if the examination

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report contained information not only on the fact that there had been continuous borrowing but also on why the Reserve Bank concerned felt the borrowing was justified. He agreed with Governor Balderston that it seemed questionable whether the examiner should criticize a Reserve Bank's judgment on the adequacy of the reason given for the borrowing, but the examination report would be informative if it showed the reason given by the Reserve Bank. As a matter of principle, he would not favor splitting the assignment of following up on individual cases of discounting; if more information was desired by the Board, he would ask the Division of Examinations to supply it.

Chairman Martin stated that this seemed appropriate to him.

Question was raised regarding the general problem of relationships between the functions of the Division of Examinations and the Division of Bank Operations, and Governor Shepardson referred to the understandings reflected in the directives proposed by the staff committee. Relating this question to the problem of responsibility for the discount window, Governor Mitchell inquired whether the Division of Bank Operations was not the logical division to be charged with any continuing supervisory responsibility. He noted that the Examinations Division went into the Reserve Banks periodically, but in general it was not the function of that Division to be looking at the Reserve Banks continuously. Mr. Farrell noted that at present the Division of Bank Operations did not possess background or experience

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in reviewing discount practices. If such an assignment were made, this competence would have to be developed.

Governor Robertson said he would continue the statistical work where it was now--in the Division of Bank Operations--but that he would place responsibility in the Division of Examinations to make the original analysis of cases of borrowing and to follow up adequately. Governor Mitchell inquired, however, whether it should not be part of the responsibility of Bank Operations, in terms of general principle, for its assignment involved day-to-day responsibility for following the operations of the Reserve Banks. Governor Robertson replied that the examiners were in each Reserve Bank only once each year, but there were people in the Division who could follow up on a regular basis. Any information gotten from Bank Operations was fine and any help by way of analysis or thought from the Research Division was fine, but the responsibility for analyzing and following up on individual cases of borrowing should be in the Division of Examinations. Governor Mitchell commented that this would be a deviation from usual practice, for the responsibility for keeping in touch with Reserve Bank operations was normally lodged with Bank Operations. The reason he kept dwelling on the subject, he said, was that he thought in the discount function there was a many-faced posture exhibited to member banks. In some Reserve districts member banks had more access to the discount window than banks in other districts, and the Board should not tolerate

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the kind of supervisory responsibility that ignored these differences. He and Governor Shepardson had expressed on various occasions the view that discount window administration ought to be relaxed in areas where there were serious credit difficulties, but the Board had not changed Regulation A in such fashion. Irrespective of this, however, he felt that an effort should be made to have more consistency throughout the System than at present.

Governor Robertson said that he thought of the examining work as an inspection service to point up whether there were deviations from policies that had been fixed by the Board. The Board should get advice from all of its divisions in fixing those policies. The Research Division could shed light on the best way of administering the discount window, and this was something the Board should take into consideration in adopting policies. However, the responsibility for detecting deviations from established policies and calling them to the attention of the Board should be the responsibility of the Division of Examinations. That Division also should follow up on specific deviations to see whether they had been corrected. Beyond this, the discount function should be administered uniformly according to proper policies, and such policies should be established.

Following further discussion along this line, Mr. Farrell commented that Bank Operations had not attempted to go into departments such as Personnel, Research, and Discount at the respective

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Reserve Banks. He inquired whether it was being proposed that Bank Operations should review the organization of the Discount Department, for example, to see how many people were involved and whether they were doing an adequate job in reviewing applications. This would go counter to what the staff committee had been trying to do, namely, to centralize responsibilities for particular functions in particular divisions.

Governor Robertson replied that Examinations' job should be to ascertain whether the policies prescribed by the Board were actually being followed. To the extent they were not being followed, this would be out of the hands of Examinations and in the hands of someone else. Bank Operations' job was to keep the Board informed on Reserve Bank competence in any given area. Examinations ought to follow up on cases of individual borrowings and make sure that defects were corrected; but if there were operational deficiencies, it would be Bank Operations' job to make a survey and report back to the Board.

Governor Mitchell suggested a hypothetical situation where, according to the periodic reports, there were several member banks that seemed to be out of line in their borrowing in a district whose Reserve Bank would not be examined for six months. He asked whether it would be Examinations' responsibility to take the step of finding out why these several situations had occurred. Governor Robertson replied that Examinations would be responsible for assuring the

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correction of difficulties noted in the report of examination. Governor Mitchell then said he assumed it would be Bank Operations' responsibility, therefore, to follow up on situations such as he had described.

Governor Mills suggested a different approach. The statistical data prepared for Bank Operations by the Reserve Banks presumably was available to Examinations. If Examinations, being in possession of that material, discovered a bank that had at the time of most recent examination been borrowing continuously and was still borrowing, then it seemed to him Examinations would be in a better position to bring that particular problem to the Board. By the same token he understood the Division had work papers from examinations that might prove useful in detecting sore spots. The Division could likewise investigate through examinations when they encountered member banks that might be presumed to be overstepping their borrowing privileges. However, correction would have to come at the Board level because the Board here was dealing with the supplying and withdrawing of reserves, which was a credit policy function and not a function for which the Division of Examinations would wish to have responsibility.

Governor Robertson said he could agree with Governor Mills in a case where Examinations found a bank borrowing for a long time in violation of the principles of Regulation A. The Division should be expected to get a report that the borrowing had been terminated. However, when new information came in between examinations, the Division should not consider that a defect existed without finding out why.

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Mr. Solomon said that obviously no one would take the responsibility for saying that there was a violation without going into the matter, and Governor Mitchell inquired who would be supposed to go into it. Governor Robertson suggested that Examinations ordinarily should not go into the matter until it went back to the Reserve Bank to make an examination. If, in the meantime, enough information had been received to create a suspicion of breakdown in the discount operation, the Examinations Division could go in, but this would not be simply if a bank had been borrowing for a month. A borrowing of six months might mean a breakdown in the discount function at the Reserve Bank concerned. Mr. Solomon commented that this was more or less what was suggested by the staff committee except that the Research Division would go into the matter, and Governor Robertson commented that the only basis for Research to be in the picture was that it had a man who was familiar with the discount function. This would not necessarily always be true.

Governor Mills wondered what the attitude of a Federal Reserve Bank President would be if he received a searching inquiry from Bank Operations or Research. He turned back, Governor Mills said, to the thought that the clearing function should be accomplished through the Division of Examinations rather than through Bank Operations or Research.

Mr. Smith noted that the question had come up because the staff committee recognized there was a gap between examinations.

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Reports were received on a current basis, and the question was who should follow up. This could be done by any division that the Board designated, but Examinations might already have some familiarity with a borrowing situation that showed up in the current reports. It might involve a case that was questionable at the time of examination. With that background, it might be a little simpler if the interim job of following up was put in Examinations.

Governor Shepardson observed that one thing the Board and the staff committee had been striving for was some specific delineation of responsibilities. He felt that the problem of reviewing borrowings was appropriately a function of Examinations, the Division that looked at such borrowings at the time of examination and presumably should ascertain the supposed justification. He thought the following up should be done through the Division that looked at all of the information when it went in for the purpose of making an examination. On the other hand, the question whether the discount function was efficiently handled was appropriately within the scope of Bank Operations. That Division should look at the matter in the same manner as any other operation, from the standpoint of efficiency. The broader study relating to the establishment of discount policy should bring in the contribution of Research. The conference of discount officers, with which Mr. Holland was associated, was working toward the evolvement of possible changes in policy. Having established policy, however,

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the Board should look to the Division of Examinations to determine whether a member bank's borrowing was in line with such policy, and that Division should also follow up on any departures from established policy as indicated by the current statistical reports.

Mr. Brill said the primary interest Research might have in following up on borrowings would be to determine whether there was some economic factor contributing to persistent borrowing that should be recognized. There had been no feeling in the staff committee discussions that the Research Division was best equipped to do a policing job on whether Federal Reserve Banks were adhering to the Board's regulations. The discussion was in terms of the competence of a particular individual. Assuming this competence could be matched by other divisions over a period of time, the Research Division would have no desire to stay in this field, except insofar as follow-up procedures elicited economic information.

Mr. Johnson commented that any delegated responsibility to the staff for review purposes should be handled by persons of competence who would be respected by the Federal Reserve Banks. Otherwise, this would be a source of irritation to the Reserve Banks.

Governor Shepardson then suggested that apparently the Board agreed that operational responsibility fell within the Division of Bank Operations. Adherence to established policy in terms of individual borrowings should be followed up by Examinations. Perhaps

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there would be questions of justifiable use of the discount window that should be taken up with Research, because such matters might raise the question whether a change in policy should be made, but the implementation of established policy should be assigned to Examinations.

Mr. Farrell inquired whether he was to understand that the same general principle applied in the case of the personnel function, for example, or the research or legal functions.

Governor Shepardson replied that the matter of operating efficiency should be a responsibility of Bank Operations. That Division should look at operational efficiency across the board at a Reserve Bank.

Governor Mitchell commented that it would be difficult, of course, for people from Bank Operations to walk into a Research Department and say that the department should lay off six clerks. The product of such a department was completely interwoven with the personality of the officer in charge.

Governor Shepardson replied that he would not expect Bank Operations to have anything to say about the research program as such, but in every operation there was a general question of operating efficiency to be considered. Someone other than a research person could look at the use of personnel and at space requirements and might be able to make good observations without any concern about the research program per se.

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Governor Mitchell said he agreed except that he could not envisage exactly how the suggested approach could be implemented effectively.

Governor Robertson said that for today he would merely go to the discount function. He would step gingerly so far as an across-the-board approach was concerned and feel his way along a little.

Mr. Farrell commented that the staff committee report was set up basically along the other line. It envisaged that the Board's Research Division would have responsibility for the Research Departments of the Federal Reserve Banks, and presumably the Personnel Division would have no responsibility regarding the staffing of the Research Departments. Bank Operations would have no responsibility as to whether the Research Department had too much space, too many clerks, or too many typewriters.

Governor Robertson said he would leave the research function responsibility where it was now. He would make the discount function responsibility an exception to the general principle reflected in the proposed staff directives.

Governor Mitchell said his first concern was to have staff responsibilities specifically delineated so the Board would know where they were. The question of who exercised the responsibilities was a matter of secondary concern. He would have a little preference for seeing the discount function responsibility with Bank Operations,

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but it was true that Examinations was better equipped to handle it today. Mr. Holland was best equipped and the Division of Examinations second best.

Governor Robertson suggested resolving the question of discount function responsibility by going along with the proposition Governor Shepardson had stated, and there was general agreement with this suggestion.

The discussion then turned to the part of the memorandum from the staff committee that pointed out that the Division of Examinations reviews the adequacy of the Protection Departments of the Reserve Banks. However, these constituted a specialized area that would benefit from surveys from time to time by special experts in such matters. The staff committee recommended that the Board, after consultation with the Reserve Bank Presidents, engage the Federal Bureau of Investigation to make a survey of the Protection Department at each Reserve Bank office. The survey would cover matters such as the staffing and disposition of the guard force, qualifications and training for guard protection, and electronic and other mechanical protective devices in use. Such a survey would amount to an up-dating of previous surveys of this nature, the most recent having been made by the FBI in 1947. The Division of Examinations would work closely with the FBI in such surveys, would follow up in subsequent examinations any recommendations made in the surveys, and would attempt to see that the

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Reserve Banks continued to maintain the standards suggested by the surveys.

Governor Mitchell said he was under the impression that there was a great deal of difference from one Reserve Bank to another in the cost of operating Protection Departments. The issue here was as much a matter of economy, perhaps, as a matter of protection. Thus, it should become a responsibility of Bank Operations. Both that Division and the Division of Examinations should be referred to as working with the FBI in any surveys.

Mr. Solomon commented that in almost all operations there was an interlinking of final output and the efficiency with which it was achieved. This required close cooperation in reviewing any function.

Governor Mitchell responded that this was why Bank Operations should be included: it was interested in economy and efficiency.

Mr. Smith commented that Examinations could provide proper follow-up, but the Division did not at present have the expertise in this area to challenge what the Reserve Banks felt was appropriate. The Division did not have an expert report available that it could follow up on in a logical way.

Governor Shepardson commented that the proposal for a survey was desirable. The responsibility for carrying through and looking at the operation, including both the personnel involved and the use

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of protective devices, was a function of Bank Operations rather than Examinations. At each examination the latter Division would take a look, but if it found something questionable in this area the problem should properly be referred to Bank Operations. The latter Division would call the attention of the Reserve Banks to whatever deficiencies it found. The responsibility for carrying through was more a function of Bank Operations than Examinations.

Mr. Solomon said that if the purpose was to deal with efficiency, economy, and savings, he could see how that was a matter for Bank Operations. However, in terms of security and safety he would suppose the Division of Examinations would be expected to follow through, having in mind that the Reserve Banks should not waste money in the process and that Bank Operations might have an interest in seeing that there was no waste.

Governor Balderston said that finding variations from standards approved by the Board was a responsibility of the examiners. However, when it came to fixing up something, that was the responsibility of the Board itself, with the help and guidance of Bank Operations. The examiners should not be running the Federal Reserve Banks when it came to fixing up defects. This was a misuse of the examining function and led to confusion.

Later during the meeting question was raised whether the Board had intended to change the proposal of the staff committee so as to

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substitute the Division of Bank Operations for the Division of Examinations as the division that would work with the FBI in surveys of the Protection Departments. The response given was that the Board intended for both divisions to participate and cooperate in the FBI surveys, that Examinations would be responsible for reporting and following up deviations from safety provisions and standards adopted as a result of the surveys; and that Bank Operations would be responsible for recommendations as to operational efficiency within the adopted standards of safety.

As to Reserve Bank Planning Departments, the staff committee's memorandum noted that it appeared that no division of the Board's staff had thought specifically in terms of its having responsibility with respect to the Planning Departments. The staff committee recommended that the Division of Bank Operations be directed to give continuing attention to this function.

Agreement was expressed by the Board with this recommendation.

As to relations of Federal Reserve Bank directors, the staff committee's memorandum noted that the Reserve Banks obtained reports of indebtedness and of outside business activities from their officers and key employees. The Division of Examinations reviewed these reports at each examination. Reserve Bank directors, however, occupied a different position; the law contemplated that they would serve on a part-time basis and have other business interests. No division of the Board's staff appeared to have direct responsibility for reviewing the adequacy

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of arrangements by the Reserve Banks for avoiding conflicts of interest by their directors or possible abuses of information by them. On the other hand, there were existing instructions on the subject, and these were supplemented by meetings of the Board with new directors and with the Chairmen and Deputy Chairmen of the Reserve Banks. While this matter therefore already received considerable attention, the staff committee recommended that the Legal Division be directed to give continuing attention to the subject, including the possible development from time to time of further statements or instructions that the Board might issue on the subject.

Agreement was expressed by the Board with the recommendation of the staff committee.

On the fifth matter called to the Board's attention in the memorandum, the staff committee noted that no member of the Board's staff appeared to have any direct responsibility for pursuing actively with the Reserve Banks the possibilities of reducing expenses through arrangements for the centralized or coordinated purchasing or leasing of equipment, services, or supplies. However, the subject did receive attention from the Conference of Presidents of the Federal Reserve Banks and various subcommittees of the Conference with which members of the Board's staff were associated. The staff committee suggested that the Board might wish to discuss this matter with the Conference of Presidents with a view to determining whether or not any more formal coordination was desirable.

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Governor Mitchell inquired if it was the practice of the examiners to check on whether bids were asked on a competitive basis, and Mr. Smith replied that this depended on the circumstances. Governor Mitchell then inquired whether there was any requirement that competitive bids be asked, and Mr. Farrell replied in the negative. Mr. Farrell went on to say that the field of purchasing was one in which he felt that the System could be vulnerable to criticism. He cited certain instances where it had developed that products or services would be available more economically if purchased on a System basis. He added that subcommittees of the Presidents' Conference had moved into certain areas but had shied away from others. In his opinion, if any broader program of coordinated purchasing was desired, a firm letter from the Board would be required stating that something more formal than had been considered in the past should be done by an appropriate committee.

Governor Mitchell suggested that there were two phases of the matter. First, there was the question of prescribing appropriate policies--sensible rules--to be followed in Reserve Bank purchasing. These would be in rather general terms. He was surprised to hear that such policies had not been prescribed. The second question related to the possibility of pooling purchases at a saving to all Banks. This would be an extremely complicated job.

Governor Balderston inquired whether the Presidents' Conference had ever made a thorough investigation of the question whether the Reserve

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Banks should make or buy certain products or supplies, and Mr. Farrell replied in the negative.

Chairman Martin then expressed the view that the whole matter of Reserve Bank purchasing should be referred to the Conference of Presidents for a report. Governor Robertson agreed that this would be appropriate, but he felt a list of questions should first be developed that could be submitted to the Conference. Chairman Martin suggested that Mr. Farrell be asked to prepare a list of questions, and there was agreement with this suggestion.

Reverting to the earlier discussion of the discount window, Mr. Farrell inquired whether an effort should be made to have the Division of Examinations represented at the discount officers' meetings in which Mr. Holland participated in order to get the full flavor of the discussions. Mr. Smith indicated that Mr. Holland felt this might present some problems; Mr. Smith thought the Division of Examinations could get the flavor of the discussions satisfactorily from Mr. Holland. Governor Mitchell suggested that the matter might be reviewed further with Mr. Holland.

Subject to changes reflecting the amendments agreed upon at today's meeting, the directives from the Board to its staff regarding responsibilities for examining Federal Reserve Banks and exercising supervision over them were then approved unanimously, with the understanding that copies would be sent to the Federal Reserve Banks for their information.

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Governor Shepardson then withdrew from the meeting.

Request of Congressional subcommittee. Mr. Solomon related that he and Mr. Cardon, Legislative Counsel, had met with members of the staff of the Permanent Subcommittee on Investigations of the Senate Committee on Government Operations who had asked that one or two bank examiners be loaned to the Subcommittee on a nonreimbursable basis for a period of approximately 60 days to review "closed banks" to see about the possibility of tie-ins with underworld elements. Mr. Solomon then described his preliminary inquiry to determine the availability of persons for this purpose.

After discussion, the Board agreed that steps should be taken to comply with the Subcommittee's request, and Mr. Solomon was authorized to work out an arrangement with one of the Reserve Banks.

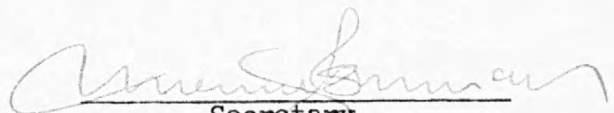
Secretary's Note: Arrangements were made for two examiners from the Federal Reserve Bank of Philadelphia to be loaned to the Subcommittee. They were Chief Examining Officer James P. Giacobello and Examiner William J. McCuen.

The meeting then adjourned.

Secretary's Note: Governor Shepardson today approved on behalf of the Board the following items:

Memorandum from John C. Chisolm, Cafeteria Laborer, Division of Administrative Services, requesting permission to work for a local warehouse.

Memorandum from Roy L. Stephen, Cafeteria Laborer, Division of Administrative Services, requesting permission to work for a local warehouse.


Secretary

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

WASHINGTON, D. C. 20551

Item No. 1
2/15/65

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

February 17, 1965.



Dear Sir:

A one-day conference at the Board is planned for March 17, 1965, in order to consider ways in which the Research Departments of the Federal Reserve Banks can improve their contributions to the material prepared by the Banks and submitted to the Board on merger and holding company applications.

Some suggestions to the Reserve Banks regarding the preparation of such material were made by the Board in a letter dated December 20, 1962. One of the suggestions was that it would be helpful to get the benefit of the different viewpoints represented by the examining, research, and legal functions. A major objective of the conference now being planned is to improve the coordination of Research Department efforts with the work of Examinations Departments. It would be desirable, therefore, to have at least one representative from each of those departments at each Reserve Bank attend the conference, preferably staff members who work directly with the merger and holding company applications.

In the past two years, there has been considerable experimental work on various techniques for the analysis of banking markets. It would be highly useful at this conference to consider the applicability of these techniques to the various market questions raised by merger and holding company cases and to consider the desirability of further work along these lines.

Please furnish the names of the representatives of your Bank who plan to attend the conference as soon as they have been ascertained.

Very truly yours,

A handwritten signature in cursive script, appearing to read "Merritt Sherman".

Merritt Sherman,
Secretary.

Enclosure.

TO THE PRESIDENTS OF ALL FEDERAL RESERVE BANKS.

Conference on Research Contribution to
Bank Merger and Holding Company Cases

March 17, 1965

TENTATIVE AGENDA

- I. Mr. Holland - Introductory remarks.
 - II. Mr. F. Solomon - Research contribution to the analysis of specific cases.
 - III. Techniques for analysis of banking markets.
 - A. Introductory statement regarding the application of the major sources of information in defining markets, determining market shares, and analyzing competitive conditions. Mr. A. Phillips.
 - B. Application of available statistical sources to the development of measures of market shares for subsection of a city or metropolitan area. Mr. O'Leary, Philadelphia.
 - C. Use of expert knowledge - proposal to use an examiner's questionnaire to develop information on market shares and competitive conditions in small cities and towns with a limited number of banks. Mr. T. Smith.
 - D. Experimentation with bank customer surveys:
 1. Pilot projects in Bergen County, New Jersey and Rockland County, New York, to obtain information on how the small business customer views his banking alternatives and selects his banking connections. Mr. Platt, New York.
 2. Report on pretesting for survey of small and medium size business customers of banks; presentation of draft questionnaires of business and household bank customers. Mr. Greenspun.
 3. Proposed pilot survey in Beloit-Janesville market areas in order to test questionnaire design and interview approach for small and medium size business customers.
 4. Techniques utilized in Richmond study of three large and three small cities. Mr. Wallace, Richmond.
 - IV. Mr. Holland - Summary of comments and discussion.
- Lunch - probably after item III-C -- Governor Shepardson will comment on the Board's need for economic analysis in merger cases.