

Minutes for March 15, 1966

To: Members of the Board

From: Office of the Secretary

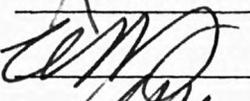
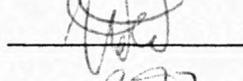
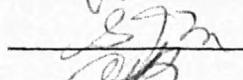
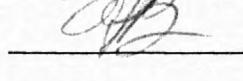
Attached is a copy of the minutes of the Board of Governors of the Federal Reserve System on the above date.

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. Robertson

Gov. Shepardson Gov. Mitchell Gov. Daane Gov. Maisel Gov. Brimmer 

Minutes of the Board of Governors of the Federal Reserve System on Tuesday, March 15, 1966. The Board met in the Board Room at 10:00 a.m.

PRESENT: Mr. Martin, Chairman
Mr. Robertson, Vice Chairman
Mr. Shepardson
Mr. Daane
Mr. Maisel
Mr. Brimmer

Mr. Sherman, Secretary
Mr. Kenyon, Assistant Secretary
Mr. Young, Senior Adviser to the Board and Director, Division of International Finance
Mr. Solomon, Adviser to the Board
Mr. Molony, Assistant to the Board
Mr. Cardon, Legislative Counsel
Mr. Fauver, Assistant to the Board
Mr. Hackley, General Counsel
Mr. Farrell, Director, Division of Bank Operations
Mr. Solomon, Director, Division of Examinations
Mr. Johnson, Director, Division of Personnel Administration
Mr. Kakalec, Controller
Mr. Harris, Coordinator of Defense Planning
Mr. Shay, Assistant General Counsel
Mr. Partee, Adviser, Division of Research and Statistics
Mr. Leavitt, Assistant Director, Division of Examinations
Mr. Sprecher, Assistant Director, Division of Personnel Administration
Miss Wolcott, Technical Assistant, Office of the Secretary
Messrs. Heyde, Sanders, and Shuter of the Legal Division
Messrs. Egertson and Poundstone of the Division of Examinations
Mr. Wood, Personnel Assistant, Division of Personnel Administration

Discount rates. The establishment without change by the Federal Reserve Bank of Boston on March 14, 1966, of the rates on discounts and

3/15/66

-2-

advances in its existing schedule was approved unanimously, with the understanding that appropriate advice would be sent to the Bank.

Approved letters. The following letters were approved unani-
mously after consideration of background information that had been made
available to the Board. Copies of the letters are attached under the
indicated item numbers.

	<u>Item No.</u>
Letter to United California Bank, Los Angeles, California, approving the establishment of a branch in the vicinity of Balboa and Genesee Avenues, San Diego.	1
Letter to Imlay City State Bank, Imlay City, Michigan, approving an investment in bank premises.	2
Letter to Western Bancorporation International Bank, New York, New York, approving an amendment to its Articles of Association.	3

Report on competitive factors. There had been distributed a
draft of report to the Comptroller of the Currency on the competitive
factors involved in the proposed consolidation of Shenandoah County
Bank and Trust Company, National Association, Woodstock, Virginia, and
Massanutten Bank of Strasburg, Strasburg, Virginia, in which the conclu-
sion read as follows:

Consummation of the proposed consolidation of Shenandoah
Bank and Trust Company, National Association, Woodstock, a sub-
sidiary of The First Virginia Corporation, Arlington, Virginia,
a registered bank holding company, and Massanutten Bank of
Strasburg would eliminate some competition existing between
them.

3/15/66

-3-

While the resulting bank would control about 51 per cent of the deposits held by banks in its service area, several alternative banking facilities would remain and it is not believed the remaining smaller banks would feel serious adverse effects as a result of the consolidation. On a county-wide basis, The First Virginia Corporation would hold approximately 52 per cent of the banking deposits held by banks in Shenandoah County.

At this meeting Mr. Leavitt reported that the Examinations and Legal Divisions now suggested that the second paragraph of the proposed conclusion be changed to read as follows:

The resulting bank would control about 51 per cent of the deposits held by banks in its service area, although within this area are several alternative banking facilities. On a county-wide basis, The First Virginia Corporation would hold approximately 52 per cent of the banking deposits held by banks in Shenandoah County.

Governor Maisel suggested deleting the word "some" toward the end of the first paragraph and then stating that the effect on competition would be adverse.

There followed a discussion of meanings that might be attributed to the word "adverse," particularly in light of the standards governing approval of applications that were contained in the new bank merger legislation. Mr. Leavitt observed that "adverse" could be interpreted in a harsh sense and said it was for this reason that the staff had offered the suggested language for the conclusion in the instant case. Governor Maisel pointed out, however, that when a bank resulting from a merger would control over 50 per cent of the deposits in its service area, this fact alone would seem to indicate a need for strong positive findings in

3/15/66

-4-

terms of the banking factors and the public interest to warrant approval of the application.

As to the particular case under consideration, Mr. Solomon suggested that figures for Shenandoah County might not be too indicative, for the banks appeared principally to serve individual trade areas, located at intervals along a stretch of highway. Governor Daane said he would have no objection to saying that the effect of the proposed merger on competition would be adverse, if the implication was that it would be somewhat adverse, rather than substantially or significantly adverse. Mr. Solomon agreed; he added, however, that the harsher meaning might be inferred by readers of the report.

After further discussion, Governor Robertson supported Governor Maisel's suggestion that the competitive effects be cited as adverse. He found it difficult to justify use of "somewhat adverse" when the resulting bank would control over half the bank deposits in its service area and when the holding company of which it would be a subsidiary controlled over half the bank deposits in the county.

Transmittal of the report, with the conclusion revised as follows, was then approved:

Consummation of the proposed consolidation of Shenandoah Bank and Trust Company, National Association, Woodstock, a subsidiary of The First Virginia Corporation, Arlington, Virginia, a registered bank holding company, and Massanutten Bank of Strasburg would eliminate competition existing between them.

3/15/66

-5-

The resulting bank would control about 51 per cent of the deposits held by banks in its service area. On a county-wide basis, The First Virginia Corporation would hold approximately 52 per cent of the banking deposits held by banks in Shenandoah County. The competitive effects of the proposed consolidation would be adverse.

Bank Holding Company Act. Governor Robertson referred to hearings on S. 2353, S. 2418, and H.R. 7371, bills to amend the Bank Holding Company Act of 1956, on which Chairman Martin was scheduled to testify tomorrow. He noted that question seemed likely to be raised whether approval by the Board, the agency charged with responsibility for supervision of bank holding companies, should not be required in the case of a proposed merger involving a bank controlled by a holding company. In his opinion a bank within a holding company system should not be permitted to expand through merger except with the consent of the Board.

(In a report to Congress of May 7, 1958, concerning the Bank Holding Company Act, the Board expressed the view that a holding company bank's absorption of an independent bank, by merger or otherwise, should be subject to the provisions of the Act. This recommendation was withdrawn following amendment of the Federal Deposit Insurance Act in 1960 to provide that bank mergers and absorptions must have the prior approval of one of the Federal bank supervisory agencies and that those agencies must take into consideration factors similar to those enumerated in the Bank Holding Company Act. At that time the Board noted that extending the coverage of the Holding Company Act to include mergers involving holding company banks would entail a duplication of supervision.)

3/15/66

-6-

During the ensuing discussion Governor Shepardson indicated that although he was sympathetic to closing the loophole of holding company expansion through the merger route, he would favor a clear-cut shift of responsibility that would result in placing jurisdiction over mergers of holding company subsidiary banks in the Board alone. In this connection Mr. Cardon mentioned that he understood Senator Douglas might suggest amendments tomorrow that would prohibit a merger involving a holding company bank with any other bank located outside the home State of the holding company and would require that any merger involving a holding company subsidiary bank be subject to Board approval under the Bank Holding Company Act. If the latter amendment should be suggested, the view could be expressed that the requirement for approval under the Bank Merger Act of a merger involving a holding company subsidiary bank should then be removed. There was general agreement that this would be appropriate.

Single note issue (Item No. 4). At the meeting on March 2, 1966, the Board was advised of amendments that the Treasury reportedly proposed to submit to the Ad Hoc Subcommittee of the House Committee on Banking and Currency assigned to review H.R. 5305, a bill to authorize revised procedures for the destruction of unfit Federal Reserve notes, including local destruction at the Federal Reserve Banks, and to permit allocation of credit for destroyed notes without sorting by Bank of issue. One of the proposed amendments would strike from section 16 of the Federal Reserve

3/15/66

-7-

Act the sentence reading "Notes so paid out shall bear upon their faces a distinctive letter and serial number which shall be assigned by the Board of Governors of the Federal Reserve System to each Federal Reserve bank." This amendment would, in effect, authorize a single issue of Federal Reserve notes, but without affording the full benefits of such a change. It was agreed that the staff should give the Treasury the drafting assistance needed to round out the proposed amendment.

A letter had now been received from Congressman Patman, Chairman of the House Committee on Banking and Currency, asking for the Board's views on the proposed deletion of the sentence in section 16. The letter also stated it was Chairman Patman's understanding that this was the only proposed amendment to H.R. 5305 for which the Ad Hoc Subcommittee had not received specific approval by the Board as to both form and substance.

There had been distributed a memorandum from Mr. Cardon dated March 14, 1966, indicating that Congressman Weltner, who had obtained approval in Subcommittee for an amendment authorizing a single note issue, was prepared to offer to the full Committee the additional amendments furnished as a technical service by the Board's staff, if the Board was prepared to go on record as favoring them. Attached to the memorandum was a draft letter that would state that the Board favored the amendments as agreed to by the Subcommittee; that the full benefits of a single note issue could be achieved only by two additional steps, i.e., applying the gold certificate reserve requirement to all 12 Reserve Banks in the aggregate and eliminating the 5 per cent redemption fund; but that the Board

3/15/66

-8-

would still favor the originally proposed amendment, with needed conforming amendments, even if the Committee did not adopt the other two steps.

In discussion Mr. Cardon pointed out that for the first time the Board was being asked to take a positive position on a single note issue at the Congressional Committee level. There was general agreement that this step should be supported, and the letter to Chairman Patman therefore was approved unanimously. A copy is attached as Item No. 4.

Secretary's Note: Mr. Cardon's memorandum also had pointed out that one of the amendments to H.R. 5305 adopted by the Ad Hoc Subcommittee would authorize the General Accounting Office to audit "the cancellation and destruction, and accounting with respect to such cancellation and destruction, of any currency of the United States unfit for circulation" and would give the Comptroller General access to any records "he deems necessary" to facilitate the audit. Mr. Cardon recommended that no objection be interposed, and there was no discussion of the point at this meeting.

Department store reports. There had been distributed a memorandum from Mr. Sherman dated March 14, 1966, referring to the arrangement approved by the Board in 1965 under which the Bureau of the Census would compile individual city comparisons of monthly department store sales for substantially the same cities for which such data had been compiled by the Reserve Banks in the past. The work to be done by Census was to be under contract with the Board at a cost of \$30,000 for a 12-month

3/15/66

-9-

period. The Board's action contemplated that it would reimburse Census at that rate from February 1966 through June 1967, with the understanding that it would review the matter in the spring of 1967 to determine whether the System would pay the cost of these compilations after July 1 of that year.

In the summer of 1965, announcement regarding the discontinuance by the Reserve Banks of department store data, after figures for January 1966 were completed, was made to respondent stores and to the public. Since that time work had been under way to effect the withdrawal of the Federal Reserve from this field and to develop a reporting system at Census to enable it to publish representative comparisons of monthly department store sales.

In connection with this work, Census was advanced \$10,000 by the Board in December 1965. The Census Bureau had now requested payment by the Board of an additional \$45,000 to carry this work through the month of January 1967. The total included \$25,000 to cover the initial costs of developing the program as well as the 12-month compilation cost of \$30,000. No reference to developmental costs had been made during earlier discussions with Census. The costs, which arose from developing mailing lists, testing the statistical validity of the reporting groups, collecting monthly data to permit year-to-year comparisons, and initiating the monthly report setup, appeared justified, but the Board would have to consider whether it wished to make this further investment in the Census Bureau arrangement.

3/15/66

-10-

Following discussion, it was agreed to accept the Census Bureau's request for payment of the developmental costs of \$25,000, as well as the 12-month compilation cost of \$30,000 to carry the program through January 1967. The Board also authorized any overexpenditure in the pertinent account of this year's budget of the Division of Research and Statistics occasioned by such payments.

Employment Security Regulations (Items 5 and 6). There had been distributed a memorandum from the Division of Personnel Administration dated February 24, 1966, (copy attached as Item No. 5), recommending revisions in the Regulations Relating to the Employment Security Program of the Board of Governors of the Federal Reserve System, last revised January 15, 1960, to make them conform to certain changes directed by the President in the Government security program, as set forth in a November 18, 1965, letter from Chairman Macy of the Civil Service Commission. There had also been distributed a memorandum dated March 11, 1966, (copy attached as Item No. 6), in which a change was proposed in one of the recommended revisions in light of a suggestion by Governor Maisel.

After discussion based on comments by Messrs. Johnson and Harris, the recommendations contained in the memorandum from the Division of Personnel Administration, as modified in one respect by acceptance of the suggestion of Governor Maisel, were approved unanimously.

Supplemental retirement allowance (Item No. 7). In a letter dated January 21, 1966, Chairman Hall requested that the Board consider

3/15/66

-11-

a possible amendment to the January 14, 1960, agreement between President Hickman and the Federal Reserve Bank of Cleveland concerning Mr. Hickman's supplemental retirement allowance. Chairman Hall referred to the January 6, 1966, letter from the Board indicating that Presidents and First Vice Presidents would normally be expected to retire at age 65, or not more than 90 days following the date such age was attained. He pointed out that President Hickman, if reappointed in 1971, would reach age 65 less than two months after the completion of that five-year term. In these circumstances he might not receive a further appointment, in which event there would be a slight resulting reduction in his creditable service and in his retirement allowance.

A memorandum from the Division of Personnel Administration dated February 23, 1966, which had been circulated to the Board, listed various reasons for the recommendation, reflected in a proposed letter to Chairman Hall, that no change be made in the agreement between President Hickman and the Reserve Bank. The Division underscored the importance of consistency in such agreements, which supplemented allowances from the Retirement System of the Federal Reserve Banks based on uniformity of application, and noted the difficulties that would be involved in tailoring individual agreements to meet possible contingencies.

The proposed letter was discussed in the light of the memorandum and additional remarks by Mr. Sprecher. While there was general agreement with the basic position reflected therein, changes in language to soften

3/15/66

-12-

the tone of the letter somewhat were suggested. Unanimous approval then was given to a letter in the form attached as Item No. 7.

Request for technical assistance. Governor Shepardson reported that a request had been received from the Agency for International Development for technical assistance to the Central Bank of the Dominican Republic. A consultant was needed for a period of six months to a year, for purposes specified in a memorandum from Mr. Irvine, Adviser, Division of International Finance, dated March 14, 1966. It was proposed that the name of Julio Castellanos, Senior Examiner at the New York Reserve Bank, be submitted for consideration, and there was no objection to proceeding in this manner.

The meeting continued from this point with limited staff attendance, and Governor Daane reported informally on the meetings of the Deputies of the Group of Ten, held last week in Paris, at which further consideration was given to proposals for international monetary reform.

The meeting then adjourned.

Secretary's Notes: A letter was sent today to Bank of America National Trust and Savings Association, San Francisco, California, extending to June 30, 1966, the time for establishment of a branch in Tamuning, Territory of Guam. (A letter of March 19, 1965, had acknowledged receipt of the bank's notice of intent to establish this branch.)

On March 11, 1966, Governor Shepardson approved on behalf of the Board a memorandum from the Office of the Secretary

3/15/66

-13-

recommending the transfer of Helen B. Wolcott from the position of Secretary to Governor Balderston to the position of Technical Assistant in the Office of the Secretary, with no change in basic annual salary at the rate of \$10,797, effective March 13, 1966. In accordance with the usual procedure, it was understood that her position would be reviewed at the end of six months for the appropriate classification grade.

Governor Shepardson today approved on behalf of the Board the following items:

Letter to English Language Services, Inc., Washington, D. C., agreeing to the termination of its agreement with the Board to provide instruction in Conversational Spanish for members of the Board's staff (as an activity of the Board's Employee Training and Development Program).

Letter to Mr. Hickman, Chairman of the Presidents' Conference Committee on Currency and Coin, advising that the Board had designated John R. Farrell, Director of the Division of Bank Operations, to serve as associate member of the Subcommittee on Currency and Coin.

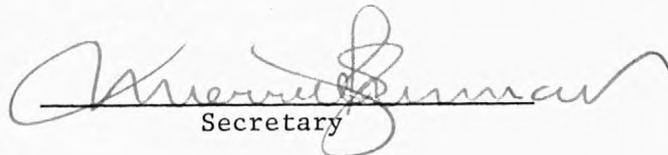
Memoranda recommending the following actions relating to the Board's staff:

Salary increase

Barbara Ann Kemp, Stenographer, Division of Research and Statistics, from \$4,149 to \$4,641 per annum, effective March 27, 1966.

Transfer

James H. Lowden, from the position of Messenger in the Division of Administrative Services to the position of Messenger in the Board Members' Offices, with an increase in basic annual salary from \$3,864 to \$4,201, effective upon assuming his new duties.


Secretary

Item No. 1
3/15/66

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

March 15, 1966



Board of Directors,
United California Bank,
Los Angeles, California.

Gentlemen:

The Board of Governors of the Federal Reserve System approves the establishment by United California Bank, Los Angeles, California, of a branch in the vicinity of the intersection of Balboa and Genesee Avenues, San Diego, California, provided the branch is established within one year from the date of this letter.

Very truly yours,

(Signed) Karl E. Bakke

Karl E. Bakke,
Assistant Secretary.

(The letter to the Reserve Bank stated that the Board also had approved a six-month extension of the period allowed to establish the branch; and that if an extension should be requested, the procedure prescribed in the Board's letter of November 9, 1962 (S-1846), should be followed.)

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

Item No. 2
3/15/66

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

March 15, 1966



Board of Directors,
Imlay City State Bank,
Imlay City, Michigan.

Gentlemen:

Pursuant to the provisions of Section 24A of the Federal Reserve Act, the Board of Governors of the Federal Reserve System approves an investment in bank premises of \$128,000 by Imlay City State Bank, Imlay City, Michigan, for the purpose of constructing a new branch building.

Very truly yours,

(Signed) Karl E. Bakke

Karl E. Bakke,
Assistant Secretary.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

Item No. 3
3/15/66

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

March 15, 1966.



Western Bancorporation
International Bank,
61 Broadway,
New York, New York. 10015

Gentlemen:

Reference is made to your letter of March 10, 1966, referring to the Board's letter of December 15, 1965, in which the Board approved an amendment to your Articles of Association increasing the capital stock of your Corporation to \$7,500,000. The Board's letter also granted consent to your Corporation to purchase shares of Philippine Commercial and Industrial Bank, Manila, Philippines, at an approximate cost of US\$3,846,150.

As you are aware, Section 25(a) of the Federal Reserve Act provides that any such increase in capital shall be fully paid in within ninety days after such approval by the Board and no provision is made for an extension of time within which such payment may be made.

You state that because of a delay in securing approval of the Philippine Monetary Board for the issuance of shares of Philippine Commercial and Industrial Bank, your Corporation is not yet ready to use the additional capital and you request the Board of Governors to again approve the amendment to Article SEVENTH of your Articles of Association to increase the capital stock of your Corporation to \$7,500,000.

In the circumstances, the Board of Governors approves the amendment to Article SEVENTH of your Articles of Association. Please advise the Board of Governors when the capital increase has been effected.

Very truly yours,

(Signed) Karl E. Bakke

Karl E. Bakke,
Assistant Secretary.



BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

Item No. 4
3/15/66

OFFICE OF THE CHAIRMAN

March 15, 1966

The Honorable Wright Patman,
Chairman,
Committee on Banking and Currency,
House of Representatives,
Washington, D. C. 20515

Dear Mr. Chairman:

This is in reply to your letter of March 9 concerning H.R. 5305. Your letter asks for the Board's comments with respect to a proposed amendment to the third paragraph of section 16 of the Federal Reserve Act, which would in effect authorize a "single Issue" of Federal Reserve notes, and states that it is your understanding that the other amendments recommended by the Subcommittee are approved by the Board. We have considered the amendments as agreed to by the Subcommittee, a copy of which was furnished by your Committee's counsel, and the Board has approved them, subject to certain changes regarding the single issue amendment, as discussed below.

The Board is in favor of replacing the present Federal Reserve notes, which identify the issuing Bank, with Federal Reserve notes which do not bear such identifying symbols. The full benefits of such a change could be realized only if two additional statutory amendments were made: (1) to put the 25 per cent gold certificate reserve requirement on an aggregate basis for all twelve Reserve Banks, with a conforming change as to payment of tax on any deficiency, and (2) to abolish the now obsolete five per cent redemption fund that the Federal Reserve maintains in the Treasury Department. With such changes (which are enumerated in items "1" and "2" of the enclosure), the System operations could be simplified, resulting in some reduction of operating expenses, although these savings would be only a fraction of those involved in the bill as introduced.

The Board recommends adoption of these two additional amendments. If, however, the Committee decides against either or both, the Board will still favor adoption of the single-issue amendment, with certain conforming amendments that are listed in item "3" of the enclosure.

Sincerely yours,

(Signed) Wm. McC. Martin, Jr.

Wm. McC. Martin, Jr.

Enclosure

1. Amendments to put gold certificate reserve requirement on an aggregate basis:

- (1) In the third paragraph of section 16, change "Every Federal Reserve bank shall maintain reserves in gold certificates of not less than 25 per centum against its Federal Reserve notes" to read "The Federal Reserve banks shall maintain an aggregate reserve in gold certificates of not less than 25 per centum against all Federal Reserve notes".
- (2) In the last sentence of section 11(c), change "bank" to read "banks" wherever it occurs.

2. Amendments to eliminate the 5 per cent redemption fund:

- (1) In section 15, first paragraph, strike "and the funds provided in this Act for the redemption of Federal Reserve notes".
- (2) In section 16--
 - (a) strike the third and fourth sentences of paragraph 3;
 - (b) strike the first sentence of paragraph 4;
 - (c) strike the second sentence of paragraph 6; and
 - (d) strike the fourth sentence of paragraph 7.

3. Amendments to provide for a single issue of notes, but keep the gold certificate reserve on an individual Bank basis, and keep the 5 per cent redemption fund (all of these amendments would be to section 16):

1. In the third paragraph, change "its Federal Reserve notes" to "its liability with respect to Federal Reserve notes" in the second sentence, and change "such bank" to read "the Federal Reserve banks" in the third sentence.

2. In the fourth paragraph, second sentence, insert "liability with respect to" before "outstanding Federal Reserve notes".

-2-

3. In the fifth paragraph, strike "its" the second and third time it appears.
4. In the seventh paragraph, change "its Federal Reserve notes issued to it" to "Federal Reserve notes" in the first sentence and strike "any of its" in the second sentence.
5. In the ninth paragraph, strike "and shall bear the distinctive numbers of the several Federal Reserve banks through which they are issued."
6. In the tenth paragraph, strike "or in the subtreasury or mint of the United States nearest the place of business of each Federal Reserve bank" and change "such bank" to read "the Federal Reserve banks".

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Item No. 5
3/15/66

Office Correspondence

Date FEB 24 1966

To Board of Governors

Subject: Revision of Board's Security

From Division of Personnel Administration

Regulations

Introductory

The Board's Employment Security Program operates under regulations approved by the Board pursuant to its authority under the Government security program. The last revision of these regulations was January 15, 1960.

The President has directed that certain changes be made in the Government security program (see John W. Macy, Jr.'s letter, attached) which basically provide that all positions presently designated as sensitive be split into critical-sensitive positions and noncritical-sensitive positions. Currently, all positions designated as sensitive by the Board carry a "TOP SECRET" clearance and require the incumbents to be cleared by full field investigations. The changes in Mr. Macy's letter provide that only incumbents of positions determined to be critical-sensitive would carry "TOP SECRET" clearance and require a full field investigation. The criteria designated to determine which positions are critical-sensitive indicates that the number of "TOP SECRET" clearances could be substantially reduced at the Board and at the Federal Reserve Banks and Branches. The noncritical-sensitive positions would carry only up to "SECRET" clearance and could be cleared by merely a National Agency Check.

Also, the President has specifically directed that (1) there be a reinvestigation made of all incumbents of critical-sensitive positions at intervals of five years following initial clearance, (2) that persons considered for sensitive positions be provided the opportunity to explain or refute derogatory information developed in an investigation before being rejected or nonselected on security grounds.

In his letter which transmits the President's directives, Mr. Macy advised the Board that the Department of Justice is of the view that recent court decisions require modification in the procedure for hearings under Executive Order 10450. These cases indicate constitutional due process requires that at such hearings an employee, whose removal is sought, must be afforded access to investigation information available to the hearing board (or the Board of Governors, on appeal). Also, the Department of Justice has advised, informally, that the employee must be assured an opportunity to confront (cross-examine) persons who offer testimony against him, and the decision of the hearing board will be based solely upon the evidence presented at the hearing.

Accordingly, a provision to restrict the information furnished to the hearing board or Board of Governors to that available to the employee has been inserted, and, in conformity with the foregoing, certain instructions regarding limits on cross-examination and confidential information have been deleted.

To: Board of Governors

-2-

This Division has carefully reviewed the Board's current security regulations and makes the following recommendations to incorporate these changes.

Recommendation

It is recommended that the "Regulations Relating to the Employment Security Program of the Board of Governors of the Federal Reserve System" (as revised January 15, 1960) be further revised as follows:

- A. Page 1 - A new paragraph be added and designated Section 1(c) as follows:

For the purpose of conducting investigations under the program, sensitive positions shall be divided into two categories, critical-sensitive and noncritical-sensitive. The criteria to be applied in designating a position as critical-sensitive shall be as follows:

Any position the duties of which include:

- (1) Access to "TOP SECRET" defense information;
- (2) Development or approval of war plans, plans or particulars of future or major special operations of war, or critical and extremely important items of war;
- (3) Development or approval of plans, policies or programs which affect the overall operations of a department or agency, i.e., policy-making or policy-determining positions;
- (4) Investigative duties, the issuance of personnel security clearances, or duty on personnel security boards; or
- (5) Fiduciary, public contact, or other duties demanding the highest degree of public trust.

Other sensitive positions which do not fall within the above criteria shall be designated as noncritical-sensitive.

To: Board of Governors

-3-

- B. That Section 4, Paragraph (c) be revised to prefix the word "critical" in the three instances where "sensitive position" is used. Also, the following additional sentence should be placed at the end of that paragraph:

A National Agency Check and inquiry shall be the minimum investigation for a person employed in a noncritical-sensitive position.

- C. That a new Paragraph (f) be added to Section 4, as follows:

(f) A person being considered for a sensitive position shall, whenever appropriate in the judgment of the Security Officer, have an opportunity to explain or refute derogatory information developed in an investigation before being rejected or nonselected on security grounds.

- D. That a new Paragraph (g) also be added to Section 4, as follows:

(g) The incumbent of each critical-sensitive position shall be required, five years after his initial clearance, and at least once each succeeding five years, to submit an updated personnel security questionnaire to the Security Officer who shall review the questionnaire, together with the personnel file of the incumbent, previous reports of investigation concerning him, and any other appropriate documents. A determination shall then be made regarding what further action, if any, is appropriate--such as, a check of local police and credit records, a National Agency Check, or an updated full field investigation.

- E. That Section 5, Paragraph (g), Subsection (1) be revised to include the following as an added sentence:

Before issuing or amending a written statement of charges, the Department of Justice shall be consulted to assure that the rights of employees are fully considered.

- F. That Section 9, Paragraph (e) be revised to include the following new third sentence:

To: Board of Governors

-4-

Investigative information furnished the hearing board or the Board of Governors must be made available to the employee whose termination is sought.

and delete the fourth and part of the fifth sentence as indicated below:

(e) Both the Board of Governors and the employee may introduce such evidence as the hearing board may deem proper in the particular case. Rules of evidence shall not be binding on the hearing board, but reasonable restrictions shall be imposed as to the relevancy, competency, and materiality of matters considered, so that the hearings shall not be unduly prolonged. Investigative information furnished the hearing board or the Board of Governors must be made available to the employee whose termination is sought. If the employee is, or may be, handicapped by the nondisclosure to him of confidential information or by lack of opportunity to cross-examine confidential informants, the hearing board shall take that fact into consideration. If a person who has made charges against the employee and who is not a confidential informant is called as a witness but does not appear, his failure to appear shall be considered by the hearing board in evaluating such charges, as well as the fact that there can be no payment for travel of witnesses.

Note: Underscoring denotes parts to be deleted.

G. That Section 9, Paragraph (k) be revised by deleting the last part of the first sentence and the entire second sentence as indicated below:

(k) The hearing board shall reach its conclusions and base its determination on the transcript of the hearing, together with such confidential information as it may have in its possession. The hearing board, in making its determination, shall take into consideration the inability of the employee to meet charges of which he has not been advised, because of security reasons, specifically or in detail, or to attack the credibility of witnesses who do not appear. The decision of the hearing board shall be in writing, and shall be signed by all members thereof. One copy

To: Board of Governors

-5-

of the decision of the hearing board, together with the complete record of the case, including investigative reports, shall be sent to the Board of Governors.

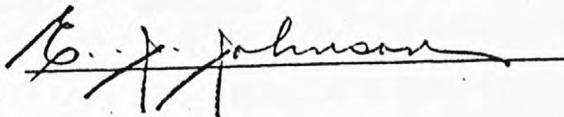
Note: Underscoring denotes parts to be deleted.

Upon approval of the preceding changes, it is further recommended that the Board's Security Officer review "TOP SECRET" clearances at the Board and at the Federal Reserve Banks and Branches (after consulting with Mr. Innis Harris) for the purpose of determining those which can be designated as critical-sensitive and noncritical-sensitive, subject to the approval by the Board Member in charge of internal administrative affairs. Future designations are to be handled in the same manner.

Discussion

As of February 1, 1966, there were 154 Board employees who have "TOP SECRET" clearances. We believe that by distinguishing between noncritical-sensitive and critical-sensitive, the number of "TOP SECRET" clearances could be reduced considerably. This reduction would result in a savings of both time and money, as it now takes approximately three months and costs \$415 to process a full field investigation by the Civil Service Commission. National Agency Checks, on the other hand, take approximately two to three weeks to complete at no cost to the Board. By reducing the number of "TOP SECRET" clearances, we would also realize a savings in time in not having to reinvestigate on a five-year cycle the incumbents of those positions, the designation of which will be changed from sensitive to noncritical-sensitive.

There are currently 326 personnel of the Federal Reserve Banks and Branches who have been cleared for "TOP SECRET" on the basis of their involvement in either the banks' Emergency Preparedness Program or their participation in the work of the FOMC. These will be carefully reviewed to reduce them to a necessary minimum. Mr. Harris has stated that he believes those "TOP SECRET" clearances issued in connection with the work of the banks' Emergency Preparedness Program could be substantially reduced, with considerable savings both of time and money.



Attachments

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEMItem No. 6
3/15/66

Office Correspondence

Date March 11, 1966.To Board of GovernorsSubject: Revision of Board's SecurityFrom Division of Personnel AdministrationRegulations

With reference to the Division's memorandum of February 24, 1966, regarding a revision of the Board's security regulations, on the basis of a suggestion by Governor Maisel, it is proposed that the suggested paragraph "C" on page 3 be changed to read as follows:

C. That a new Paragraph (f) be added to Section 4, as follows:

- (f) A person being considered for a sensitive position shall, ~~whenever-appropriate-in-the-judgment-of-the Security-officer;~~ EXCEPT WHERE IT IS FOUND TO BE INAPPROPRIATE IN THE JUDGMENT OF THE BOARD, have an opportunity to explain or refute derogatory information developed in an investigation before being rejected or nonselected on security grounds.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

WASHINGTON, D. C. 20551

Item No. 7
3/15/66

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

March 18, 1966.

CONFIDENTIAL (FR)

Mr. Joseph B. Hall,
Chairman of the Board,
Federal Reserve Bank of Cleveland,
Cleveland, Ohio. 44101

Dear Mr. Hall:

The Board of Governors has reviewed your letter of January 21, 1966, concerning a proposed amendment to the agreement between President Hickman and the Federal Reserve Bank of Cleveland dated January 14, 1960, which provides for supplementing the retirement allowance that Mr. Hickman would receive if he retires from his present position after having completed at least ten years of service.

The Board recognizes that the application of the present contract could cause some diminution in the maximum potential retirement allowance of President Hickman, in the event some of the circumstances your letter relates were to occur. Obviously, it is not possible at this time to judge with any degree of accuracy what individual decisions as to continuation of service of a given person may be made ten years hence or what the reasons for such decisions might then be. The present contracts that have been executed with the Board's approval between a number of the Reserve Banks and short service Presidents are identical as to their basic terms, and the Board believes that consistency in these agreements is important, particularly since the contracts provide for supplementing the regular allowances that would be paid under the Retirement System of the Federal Reserve Banks which, as you know, are applied uniformly.

For these reasons, and also because it does not follow from the Board's letter of January 6, 1966, that a Reserve Bank President would necessarily need to retire before attaining age 65 simply because he might reach that age during a five-year term of office, the Board is not prepared to approve the modification mentioned in your letter in the basic contract between your Bank and President Hickman.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.