Minutes for August 17, 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 proposed to place in the record of policy actions required to be kept under the provisions of section 10 of the Federal Reserve Act an entry covering the item in this set of minutes commencing on the page and dealing with the subject referred to below:

Page 5 Amendment to Supplement to Regulation D, Reserves of Member Banks, relating to reserve requirements against time deposits.

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.

Chairman Martin
Governor Robertson
Governor Shepardson
Governor Mitchell
Governor Daane
Governor Maisel
Governor Brimmer
Minutes of the Board of Governors of the Federal Reserve System on Wednesday, August 17, 1966. The Board met in the Board Room at 10:00 a.m.

PRESENT: Mr. Robertson, Vice Chairman
Mr. Shepardson
Mr. Mitchell
Mr. Brimmer

Mr. Sherman, Secretary
Mr. Kenyon, Assistant Secretary
Mr. Holland, 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. Brill, Director, Division of Research and Statistics
Mr. Solomon, Director, Division of Examinations
Messrs. O'Connell and Hooff, Assistant General Counsel
Mr. Partee, Associate Director, Division of Research and Statistics
Mr. Daniels, Assistant Director, Division of Bank Operations
Messrs. Leavitt and Smith, Assistant Directors, Division of Examinations
Mrs. Semia, Technical Assistant, Office of the Secretary
Messrs. Pustilnik, Shuter, and Smith of the Legal Division
Messrs. Lyon and Rumbarger of the Division of Examinations

Request of American National Bank (Item No. 1). Unanimous approval was given to a letter to American National Bank, Parma, Ohio, granting its request for permission to continue to maintain the same reserves against deposits as are required to be maintained by nonreserve city banks, effective as of the date the bank opened its branch in downtown Cleveland. A copy of the letter is attached as Item No. 1.
During discussion Governor Brimmer suggested making sure that the circumstances requiring Board permission to maintain reduced reserves were generally understood at the Reserve Banks. In the present case, it appeared that the Cleveland Bank had not been aware that when the member bank opened a downtown branch it should seek permission to continue to maintain reserves at the country bank level.

Staff comments indicated that because of State law restrictions on branches the situation was unusual in Ohio. That probably accounted for the Reserve Bank's oversight, since it was clear that a bank became subject to reserve city bank reserve requirements if it opened a downtown branch in a reserve city, in the absence of special permission from the Board. There were, of course, many variables that might enter into the decision as to whether or not to grant permission to continue to maintain reduced reserves. If legislation eliminating the reserve city classification were enacted, the problem obviously would no longer exist.

Governor Brimmer reiterated his view that efforts should be made to assure that all Reserve Banks were aware of the practices followed in the present situation.

Request by Chairman Patman (Item No. 2). Mr. Cardon reported a recent telephone conversation in which Mr. Schremp, of the staff of Chairman Patman of the House Committee on Banking and Currency, had renewed the request made by Mr. Patman last March for work papers relating to the most recent examination of the trust department of The Cleveland
Trust Company, Cleveland, Ohio, for the stated purpose of evaluating the competence of the System's examiners. (The Board had replied to the earlier request by letter of March 31 stressing its obligation to maintain the confidentiality of relationships disclosed by member bank examinations and suggesting other possible means through which information that might serve Mr. Patman's purposes could be provided.)

After a discussion of alternatives through which the stated objective might be accomplished, unanimous approval was given to a letter to Chairman Patman in the form attached as Item No. 2.

Pension funds. There had been distributed a memorandum dated August 15, 1966, from Mr. Solomon regarding a request from Congresswoman Griffiths, Chairman of the Subcommittee on Fiscal Policy of the Joint Economic Committee, that he provide further views on the adequacy of public supervision of bank-administered and other pension funds, in supplementation of the statement he had submitted in connection with hearings of the Subcommittee in May 1966 regarding the Federal Reserve System's examination of trust departments, including pension funds held in State member banks. Attached to the memorandum was a draft of reply that had been prepared for Mr. Solomon's signature. While the draft disclaimed speaking for the Board, Mr. Solomon requested guidance as to whether the proposed treatment seemed generally appropriate.

After a discussion during which it was suggested that the letter might appropriately include references to specific situations illustrative
of certain problems encountered by the System in supervising pension fund administration by State member banks, it was understood that Mr. Solomon would transmit the letter with such revisions as appeared to him desirable in the light of the comments made. A copy of the letter, as sent, has been placed in the Board's files.

All members of the staff except Messrs. Sherman, Kenyon, Holland, Molony, Cardon, Fauver, Hackley, Brill, and Partee then withdrew from the meeting.

Discount administration. Governor Mitchell asked Mr. Holland whether the latter felt that an interpretation of Regulation A (Advances and Discounts by Federal Reserve Banks) could be drafted for circulation to Reserve Bank Presidents and discount officers that would be consistent, without changing the regulation itself, with a view that the System's discount facilities should not be available to member banks to make adjustments incident to run-offs of certificates of deposit unless certain management policies were agreed to by the borrowing member bank.

Governor Robertson commented that Mr. Holland was working on a memorandum along those lines for the Board's consideration within the next few days.

Mr. Holland expressed the view that such a communication was needed under present circumstances. He understood that the main thrust of such a document would be that discount window accommodation would be conditioned on the willingness of a member bank to make adjustments in
terms of its lending policies rather than through dumping securities on the market. The System's purposes might be served better if member banks were allowed to borrow longer at the discount window while they adjusted their lending policies rather than if they were told they could not come to the window, thus forcing a divestment of securities.

Governor Mitchell commented on the need for a uniform System posture, and Mr. Holland noted the unlikelihood of uniformity in the absence of a Board communication.

There followed further discussion regarding problems that might have to be covered in such a document, and it was understood that Mr. Holland would expedite the preparation of a draft for the Board's consideration.

Reserve requirements (Items 3-4). The Vice Chairman summarized for the other members of the Board a meeting he had attended yesterday at which consideration was given by Treasury officials, members of the Council of Economic Advisers, and other Administration officials to the position that should be taken by the Administration regarding this week's increase in the commercial bank prime loan rate from 5-1/2 per cent to 6 per cent. During the meeting, Governor Robertson said, question was raised about the possibility of Board action to increase from 5 per cent to 6 per cent the reserve requirement against time deposits (other than savings deposits) in excess of $5 million at any member bank. There was complete agreement on the part of those at the meeting that such an increase
would be appropriate, that it would help to make monetary policy more effective in a manner that needed to be accomplished. There was agreement that such a procedure would be preferable to pursuing a comparable degree of credit tightening through open market operations, because it would work in a more selective fashion.

Governor Robertson added that in his own view this was the way in which the Federal Reserve should proceed, with an announcement in which the Board would point out that the action was a part of the credit-tightening process in order to curtail the expansion of bank credit and thereby combat inflationary pressures. During the adjustment period banks would be obliged to come to the discount window, but the administration of the window could be such as to aid the adjustment process only on condition that the applicant banks were curtailing their business loans and shoring up their liquidity positions.

Governor Robertson also said that subsequent to the meeting question arose as to whether there was not something to be said for the Board's taking action on reserve requirements in advance of debate by the House of Representatives on current legislative proposals relative to the regulation of rates on time deposits. Accordingly, he had contacted Governor Daane by telephone but found that the latter did not expect to be back in Washington today. That fact argued in favor of postponing consideration of Board action until Friday.

However, Governor Robertson continued, this morning he began to wonder about the impact of any Board action in terms of the forthcoming
auction of $3 billion of Treasury tax anticipation bills. Consequently, he called Mr. Sternlight of the Treasury and asked him the specific question whether it would be preferable for the announcement of any Board action to come before or after the auction. Mr. Sternlight expressed the view that it would be preferable for any announcement to come before the auction, since it would be unfair to make such an announcement after bids had been made for the bills. Mr. Sternlight authorized Governor Robertson to report this view to the Board.

Governor Robertson also said that he had verified this morning that Governor Daane could not be here today. Thus the question was whether it would be preferable, in all the circumstances, to consider taking action today or to postpone the decision.

Governor Shepardson observed that one of the points stressed in supporting legislation that would provide flexible authority for the regulation of interest rates on time deposits was that the Board could and would act promptly to meet situations as they might arise. It seemed to him that in the circumstances, including those mentioned by Governor Robertson, it would be appropriate for the Board to act promptly.

Governor Mitchell also expressed the view that there was something to be said for acting promptly. He went on to say that since the question of reserve requirement action was last discussed by the Board he had been giving some further thought to the market impact of action of that kind. In talking with various people he had gotten the impression
that there was presently a much more serious intent on the part of banks to put their houses in order, and a much greater realization that they could not support a public posture, in a period of monetary restraint, in which their aggregates continued to increase at the rate at which they had been rising. If, however, the Board wanted to avoid the kind of announcement impact that would bring down on it, needlessly, the wrath of State and local Government authorities, he felt that the Board must include in its announcement some reassuring reference to the use of the discount window; and that the reference should be followed up by more specific action so that everyone was made aware, on a uniform basis, of the posture of the System insofar as discount administration was concerned.

Governor Mitchell added that he was not as apprehensive as the System Open Market Account Manager about the possibility of a disorderly securities market. However, there was evidence of a great deal of pressure in the municipal market, which indicated that the adjustment process should be cushioned to some extent so far as that market was concerned. That might be accomplished through a discount policy geared toward inducing adjustment of lending policies by banks rather than a selling off of municipal securities.

Governor Brimmer, who had stepped out of the room somewhat earlier, said he had talked by telephone with Governor Daane, who was experiencing transportation difficulties at an out-of-town location. Governor Brimmer said he had reported to Governor Daane the nature of the conversation
between Governor Robertson and Mr. Sternlight, and had asked Governor Daane specifically whether he would like to have a Board decision deferred until this afternoon in the hope that he would be able to return to Washington by that time. However, Governor Daane had said that since the Board understood his serious reservations about the proposed action, which he still held, he would not ask that Board action be held up on his account.

Continuing, Governor Brimmer said that the reservations he had expressed when the proposal was discussed previously by the Board turned on a number of considerations. For one thing, he had stressed that it would be unfortunate if Board action provided a peg on which commercial banks could hang an increase in the prime rate. Obviously, in view of the subsequent increase in the prime rate, that consideration was no longer germane. He had also expressed doubts about the process of adjustment banks would follow. He had accepted the fact that the most likely outcome would be a further upward adjustment in the general level of rates, but such would also be the likely consequence of further gradual tightening through open market operations, although the processes by which rates moved upward would differ.

As to the way in which banks would in fact adjust, Governor Brimmer said he felt that the main impact would be on the municipal market in the present context. Banks could be expected to sell some of their present holdings of municipals, and to participate less frequently
and with greater reluctance in underwriting syndicates. Some adverse impact in this sector must be anticipated.

Having said this, Governor Brimmer continued, he nevertheless believed that the proposed action was justified. Apparently the Account Manager had serious reservations about such a move in terms of the present fabric of the market, and feared that disorderly conditions might develop. He could not say that the Manager was wrong, for he respected the Manager's judgment, and he noted that Mr. Holland also had expressed some apprehensions.

Mr. Holland said that while he did have some concern, his feelings were not as strong as those of the Manager.

Governor Brimmer then went on to say that because of his own concern about the possible development of disorderly markets, he thought that consideration should be given to some adjustment through open market operations to cushion the effect of the Board's action. Access to the discount window during the process of adjustment should be assured, but he doubted whether that should be the sole instrument of cushioning. Banks should be told that the discount window would in fact be available to aid in the process of adjustment, under condition that the borrowing banks would put their houses in order, but he would also be prepared to see some adjustment through open market operations as necessary if disorderly market conditions seemed to be developing. He favored a moderate reduction of credit availability, and was willing to take the risk involved, but he recognized the risk.
Mr. Holland then distributed a table relative to bank reserve positions in the statement weeks ahead. Question was raised whether, in view of the prospective circumstances, including pressures likely to occur around the mid-September tax and dividend dates, any Board action should carry an effective date as far forward as October. It was noted that the contemplated action would add about $360 million to the reserve requirements of reserve city banks and about $80 million to the reserve requirements of country banks. The unanimous view of the Board was against deferring the effective date of the action for too long a period. Comments were made that once the action was announced, banks might be expected to begin making preparations accordingly. Comments also were made on the role that the discount window might be expected to play in the adjustment process. Since the need for an understanding of the posture of discount policy seemed clear, it was suggested that the Board meet with the Presidents on the date of the next Open Market Committee meeting (August 23), prior to which it would be hoped that a draft paper outlining a strategy of procedure could be made available to the Presidents for consideration.

The outcome of the foregoing discussion was a consensus that any Board action on reserve requirements should be made effective September 8 for reserve city banks and September 15 for country banks.

There followed additional discussion of the state of the municipal market and what might be done by way of discount administration to
help avoid substantial further pressure on that market as banks adjusted their positions.

Governor Robertson then commented that he would favor the reserve requirement action in terms of its being a further step to tighten monetary policy and make it effective in curtailing the expansion of bank credit, particularly business loans. There would admittedly be risks in a credit-tightening action, and steps should be taken promptly to clarify the purposes for which the discount window could properly be used in the forthcoming period. But the Board would have to be prepared to live with the impact of any restrictive action. It must expect rates to move up. Personally, however, he did not feel that the impact of reserve requirement action would be as severe as some of the statements at today's meeting seemed to suggest.

A vote then was taken on increasing from 5 per cent to 6 per cent the reserve requirement against time deposits (other than savings deposits) in excess of $5 million at any member bank, such action to be effective September 8, 1966, for reserve city banks and September 15, 1966, for other member banks. The vote was unanimously in favor of such action. A copy of the notice subsequently submitted for publication in the Federal Register is attached as Item No. 3.

There ensued discussion with regard to the type of statement to be issued by the Board. Several suggestions were made, and it was understood that a statement would be drafted for the Board's consideration this afternoon.
The meeting then recessed and reconvened at 2:00 p.m. with the same attendance as at the conclusion of the morning session except that Mr. Cardon was not present.

A draft of press release on the reserve requirement action had been prepared, and various suggestions were made for changes in the draft, after which unanimous approval was given to the issuance later this afternoon of a press statement in the form attached as Item No. 4.

The meeting then adjourned.

Secretary's Notes: Attached as Item No. 5 is a copy of a letter sent today to the Federal Reserve Bank of Richmond approving a special Grade 16 maximum of $21,500 in the salary structure applicable to the head office, as requested in the Bank's letter of July 25, 1966. The letter was sent pursuant to the authorization given to the Secretary at the meeting of the Board on June 29, 1966.

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

Letter to Mr. Francis, Chairman of the Presidents' Conference Committee on Sundry Operations, advising that the Board had designated John R. Farrell to serve as associate of the ad hoc subcommittee that is being appointed to conduct a study of the possibility of Federal Reserve offices servicing commercial banks outside their own boundaries.

Letter to the Federal Reserve Bank of Kansas City (copy attached as Item No. 6) regarding arrangements whereby Assistant Examiner Richard C. Cornelison would be assigned to the Board's Division of Examinations for a period of approximately three months beginning September 12, 1966.

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

John Harlan Rhinehart as Operations Research Analyst, Division of Data Processing, with basic annual salary at the rate of $17,550, effective the date of entrance upon duty.

Title change

June E. Burns, change in title from Administrative Assistant to Assistant to the Director, Division of Personnel Administration, with no change in basic annual salary at the rate of $13,201, effective August 28, 1966.

Acceptance of resignations

Helen D. Cunney, Research Assistant, Division of Research and Statistics, effective the close of business August 11, 1966.

Gayle F. Jamison, Records Clerk, Office of the Secretary, effective the close of business August 19, 1966.

A. Helen Peery, Key Punch Operator, Division of Data Processing, effective the close of business August 24, 1966.

Janet L. Lemley, Stenographer, Division of International Finance, effective August 26, 1966.

Mary Ellen Smith, Statistical Clerk-Typist, Division of Research and Statistics, effective the close of business August 31, 1966.

Secretary
Board of Directors,
American National Bank,
Parma, Ohio. 44129

Gentlemen:

With reference to your request submitted through the Federal Reserve Bank of Cleveland, the Board of Governors, acting under the provisions of Section 19 of the Federal Reserve Act, grants permission to the American National Bank to continue to maintain the same reserves against deposits as are required to be maintained by nonreserve city banks, effective as of the date it opened its branch in downtown Cleveland.

Your attention is called to the fact that such permission is subject to revocation by the Board of Governors.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.
August 18, 1966.

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

Dear Mr. Chairman:

This is in further reference to your letter of March 25, 1966 and our reply of March 31 regarding examination work papers. We understand from conversations between Mr. Schremp and Mr. Cardon that you would like to look over the examination work papers and report of examination of the Trust Department of the Cleveland Trust Company, in order to evaluate the competence of the System's examiners.

As indicated in our letter of March 31, we want to find a way to furnish your Committee with the information it needs without disclosing confidential information relating to the private affairs of individuals. Accordingly, we suggest that both objectives can be accomplished by providing Mr. Schremp with a copy of a report of the examination of a trust department of an unidentified State member bank and the related work papers, after deleting names of individuals and other confidential information that would not assist your Committee in evaluating the work of the examiners. We assume that some arrangement could be agreed upon for selecting at random a bank with a trust department large enough to indicate how these examinations are conducted. One way to do this would be for us to furnish copies of the necessary papers for the bank with the largest trust department that was being examined on any date that you select.

Sincerely,

(Signed) J. L. Robertson

J. L. Robertson.
1. Effective as to member banks in reserve cities at the opening of business on September 8, 1966, and as to all other member banks at the opening of business on September 15, 1966, Supplement to Regulation D is amended to read as follows:

§ 204.5 Supplement.

(a) Reserve percentages. Pursuant to the provisions of section 19 of the Federal Reserve Act and § 204.2(a) and subject to paragraph (b) of this section, the Board of Governors of the Federal Reserve System hereby prescribes the following reserve balances which each member bank of the Federal Reserve System is required to maintain on deposit with the Federal Reserve bank of its district:

(1) If not in a reserve city--

   (i) 4 per cent of its savings deposits, plus
   (ii) 4 per cent of its other time deposits up to $5 million and 6 per cent of such deposits in excess of $5 million, plus
   (iii) 12 per cent of its net demand deposits.

(2) If in a reserve city (except as to any bank located in such a city which is permitted by the Board of Governors of the
Federal Reserve System, pursuant to § 204.2(a)(2), to maintain the reserves specified in subparagraph (1) of this paragraph—

(i) 4 per cent of its savings deposits, plus

(ii) 4 per cent of its other time deposits up to $5 million and 6 per cent of such deposits in excess of $5 million, plus

(iii) 16-1/2 per cent of its net demand deposits.

(b) Counting of currency and coin. The amount of a member bank's currency and coin shall be counted as reserves in determining compliance with the reserve requirements of paragraph (a) of this section.

2a. This amendment is issued pursuant to the authority granted to the Board of Governors by section 19 of the Federal Reserve Act to change reserve requirements to prevent injurious credit expansion or contraction (12 U.S.C. 462b). The only change is to increase the reserves that must be maintained against time deposits (other than savings deposits) in excess of $5 million from 5 per cent to 6 per cent.

b. There was no notice and public participation with respect to this amendment as such procedure would result in delay that would be contrary to the public interest and serve no useful purpose. The effective dates were deferred for less than the thirty-day period referred to in section 4(c) of the Administrative Procedure Act because the Board found that the general credit situation and the public interest compelled it to make the action effective no later than the dates adopted.

Dated at Washington, D.C., this 17th day of August, 1966.

By order of the Board of Governors.

(SEAL) (Signed) Merritt Sherman
Merritt Sherman,
Secretary.
For immediate release.  

The Board of Governors of the Federal Reserve System announced today an increase from 5 per cent to the statutory ceiling of 6 per cent in reserve requirements against time deposits (other than savings deposits) in excess of $5 million at each member bank. To permit orderly adjustments by banks, the effective date of the increase will be the reserve computation period beginning September 8, 1966 for reserve city banks, and the period beginning September 15 for other member banks.

It is estimated that the action will increase required reserves by about $450 million—approximately $370 million at reserve city banks and $75 million at other member banks. This increase is expected to affect mainly the few hundred larger banks issuing savings certificates and other certificates of deposit (CD's) in substantial volume.

This action by the Board follows a similar increase, from 4 per cent to 5 per cent, in reserve requirements on these categories of deposit that was announced at midyear. Like that earlier measure, today's action is designed to exert a tempering influence on bank issuance of time certificates of deposit, and to apply some additional restraint upon the expansion of bank credit to businesses and other borrowers.
Monetary actions already taken have resulted in some moderation of the rate of bank credit growth thus far this year. However, in view of increasing pressures on prices stemming from recent developments in the economy, today's action is being taken to reinforce the anti-inflationary effects of overall monetary restraint.

The Board recognizes that in the period ahead some banks may be faced with unusual pressures, and in such circumstances Federal Reserve discount facilities will be available to assist member banks while they are making an orderly adjustment in their positions. However, such adjustments will be expected to emphasize increased restraint in lending policies and maintenance of an appropriate degree of liquidity on the part of borrowing banks.
CONFIDENTIAL (FR)

Mr. Edward A. Wayne, President,
Federal Reserve Bank of Richmond,
Richmond, Virginia. 23213

Dear Mr. Wayne:

The Board of Governors has approved a special Grade 16 maximum of $21,500 in the salary structure applicable to the Head Office of the Federal Reserve Bank of Richmond, effective the date of this letter. We understand from your letter of July 25, 1966, that this action is taken to improve the Bank’s ability to retain and recruit employees of the desired quality in professional-level positions.

Very truly yours,

(Signed) Merritt Sherman

Merritt Sherman,
Secretary.
Mr. George H. Clay, President,
Federal Reserve Bank of Kansas City,
Kansas City, Missouri.  64106

Dear Mr. Clay:

In accordance with the tentative arrangements made with Chief Examiner Maurice J. Swords by the Board's Division of Examinations, it is understood that your Bank will make available for a period of approximately three months, beginning September 12, 1966, the services of Mr. Richard D. Cornelison, an Assistant Examiner for your Bank. While in Washington, Mr. Cornelison will be assigned to the foreign banking section of the Board's Division of Examinations, but it is also hoped he will have an opportunity to become generally familiar with the work of the Division as a whole and to visit other divisions of the Board. While on assignment in Washington, Mr. Cornelison will be designated as a Federal Reserve Examiner.

It is understood that the Federal Reserve Bank of Kansas City will absorb all of Mr. Cornelison's salary and travel expenses in connection with the assignment.

The Board of Governors appreciates the cooperation of your Bank in making the services of Mr. Cornelison available during this period.

Very truly yours,

(Signed) Karl E. Bakke

Karl E. Bakke,
Assistant Secretary.