

FEDERAL RESERVE BANK
OF NEW YORK

ATCIR No 8373
June 20, 1978

To All Member Banks in the Second Federal Reserve District:

Enclosed for your information is a revision, effective May 31, 1978, of the regulation of the Board of Governors of the Federal Reserve System entitled "Reserve Bank Directors--Actions and Responsibilities."

The regulation has been amended in response to comments by Reserve Banks on the original edition of the regulation, a copy of which was sent to you on March 8, 1978.

PAUL A. VOLCKER,
President.

[6210-01]

Title 12—Banks and Banking

CHAPTER II—FEDERAL RESERVE SYSTEM

SUBCHAPTER A—BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

[Docket No. R-0144]

PART 264a RESERVE BANK DIRECTORS—ACTIONS AND RESPONSIBILITIES

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Final rule.

SUMMARY: The Board of Governors has adopted amendments to its regulation entitled Federal Reserve Bank Directors—Actions and Responsibilities. This regulation was published in the FEDERAL REGISTER on February 24, 1978, (43 FR 7610) and followed upon enactment of the Federal Reserve Reform Act of 1977 in which provisions of the United States Code relating to acts affecting a personal financial interest were amended to apply to directors of Federal Reserve Banks.

The regulation contains prohibitions against director participation in particular matters, sets forth proposed procedures under which a director may obtain an ad hoc exemption from such prohibitions, and identifies certain financial interests of directors that the Board of Governors has exempted from coverage by the statute as being too remote or too inconsequential to affect the integrity of directors' services. The substantive amendments principally involve (1) further identification of financial interests, the knowledge and existence of which will preclude a director from voting on extensions of credit, advances, or discounts to banks determined to be in hazardous financial condition and (2) identification of additional financial interests that the Board of Governors has determined to be too remote or too inconsequential to affect the integrity of directors' services.

EFFECTIVE DATE: May 31, 1978.

FOR FURTHER INFORMATION CONTACT:

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SUPPLEMENTARY INFORMATION: The Federal Reserve Act contemplates that Reserve Bank directors will be gainfully employed in several designated areas of endeavor, but will devote a portion of their time to Federal Reserve Bank functions. The

amended 18 U.S.C. 208 makes applicable to Reserve Bank directors a standard of conduct formulated principally for application to individuals serving the Federal Government full time and generally with no other substantial occupation or calling. While it was the judgment of the Board of Governors that the ethical standards historically adhered to by the boards of directors of Federal Reserve Banks have been in accord with the spirit of 18 U.S.C. 208, the unique position of Federal Reserve Bank directors was felt to warrant formulation by the Board of Governors of a regulation intended to resolve potential conflicts in a manner consistent with the interests of the public, the Federal Reserve System, and the directors involved.

Pursuant to 5 U.S.C. 553(b)(B), the regulation was published on February 24, 1978, as a final rule, without prior notice of proposed rulemaking but with opportunity for comment and subsequent amendments, as determined necessary or desirable. No comments were received from the public but suggestions were made by the Reserve Banks, reflecting their study of the regulation and operations under it. After a study of these suggestions, the Board has concluded that adoption of certain substantive and technical amendments would further the intended purpose of the regulation.

The amendments that have been adopted are as follows:

(1) Section 264a.2 is amended to add a new paragraph (g) defining the term "discussions," as used in section 264a.5(d). This amendment is intended to make clear that the term "discussions" includes votes taken or other forms of decisional action.

(2) Section 264a.3(b)(1)(iii) identifies those circumstances in which a director may not participate in deliberations of his board concerning extensions of credit to a bank in hazardous financial condition when the director, his spouse, or minor child owns stock of the borrowing bank. This section has been amended to include ownership of stock of the registered parent holding company of the borrowing bank.

(3) Section 264a.3(b)(2)(i) has been deleted and a new section 264a.3(b)(1)(iv) has been added to provide that a director may not participate in deliberations concerning extensions of credit to a bank in hazardous financial condition when the director, his spouse, or minor child is employed in a policymaking position with or serves as a director of the borrowing bank or the registered parent holding company of the borrowing bank. Previously, the regulation prohibits such participation only in circumstances in which the director was the officer or director of the borrowing bank.

(4) Section 264a.3(b)(2)(iii)(A), previously numbered 264a.3(b)(2)(iv)(A),

identifies circumstances in which a director is precluded from participating in deliberations concerning extensions of credit to a bank in hazardous financial condition when a business with which the director serves as a principal officer is known by the director to have outstanding or to be negotiating a direct extension of credit or line of credit from the borrowing bank. The Board of Governors has noted that large corporations often initiate such credit arrangements for a variety of business purposes and in various amounts at numerous institutions throughout a Reserve Bank district. Rather than require that the mere existence of any such extensions or lines of credit preclude director participation, the section has been amended to provide that only direct and substantial extensions or lines of credit will bar director participation.

(5) Section 264a.5(b)(1) of the regulation reflects a Board determination that financial interests of directors in deliberations concerning and ratification of ordinary and routine extensions of credit to a member bank that have previously been made by Reserve Bank officials under established procedures of the Federal Reserve System are too remote or too inconsequential to affect the integrity of directors' services and that, accordingly, the prohibitions of 18 U.S.C. 208 shall not apply to director participation in such matters. This contrasts with hazardous banking situations addressed by section 264a.3(b) in which numerous financial interests are identified that will preclude director participation. Experience under the regulation has shown that the exemption fails to address other situations that may arise in which credit extensions, advances, or discounts are the subject of Reserve Bank board deliberations. Upon study of such circumstances, the exemption has been amended to refer to deliberations concerning or ratification of extensions of credit, advances, or discounts to any bank that has not been determined to be in hazardous financial condition. These would include, for example, short-term advance credit, seasonal credit and emergency credit to member banks; advances to member banks; discounts to member banks and Federal intermediate credit banks, and indirect credit non-member banks, provided the credit extensions, advances, or discounts are in accordance with System policy and procedures.

(6) Sections 264a.5(b)(2) and 264a.5(b)(3) of the regulation identify financial interests which the Board of Governors has determined are too remote or too inconsequential to justify barring director participation in deliberations concerning financial institutions. The phrase "concerning or affecting a financial institution" in each

of these sections has been changed to "concerning or affecting any financial institution" to make clear that the exemptions apply regardless of the condition of the financial institution involved.

(7) A new § 264a.5(b)(4) has been added to reflect a Board determination that financial interests that a director or certain other persons may have in deliberations affecting a financial institution as a result of holdings in a diversified and widely held mutual fund, investment company, pension or retirement plan are too remote or too inconsequential to affect the integrity of directors' services, and that, accordingly, directors are not prohibited from participating in such deliberations, provided the director does not contribute to investment decisions of the fund, company, or plan.

(8) Section 264a.5(d) identifies topics that may be the subject of discussion by Reserve Bank boards and that are believed by the Board of Governors not to be particular matters of the type described by 18 U.S.C. 208. The section also reflects the judgment that even if the statute were held to be applicable, the financial interests of directors or certain other persons in such matters are too remote or too inconsequential to affect the integrity of directors' services and that, accordingly, the prohibitions of 18 U.S.C. 208 shall not apply to director participation in such matters. This section has been amended to include matters intended to have generally uniform application to banks within the Reserve Bank district.

(9) Technical or conforming amendments have also been made to sections 264a.2(c), 264a.3(b), 264a.3(c), 264a.5(c), 264a.5(c)(1) and 264a.5(c)(2).

Accordingly, 12 CFR Part 264a is revised to read as follows:

Sec.

264a.1 Purpose.

264a.2 Definitions.

264a.3 Prohibition against Director participation in particular matters.

264a.4 Granting of ad hoc exemptions.

264a.5 Exemption of remote or inconsequential financial interests.

AUTHORITY.—18 U.S.C. 208, as amended by the Federal Reserve Reform Act of 1977, Pub. L. No. 95-188, sec. 205, 91 Stat. 1387; 12 U.S.C. 248, 301.

§ 264a.1 Purpose.

Directors of Federal Reserve Banks are charged by law with the responsibility of supervising and controlling the operations of the Reserve Banks, under the general supervision of the Board of Governors, and for assuring that the affairs of the Banks are administered fairly and impartially. The Federal Reserve Act provides that Reserve bank directors will be selected with due consideration to the interests of various segments of the population

and the economy, thus assuring that the Federal Reserve System will receive the benefit of the experienced judgment of individuals from a broad spectrum of the communities that will be affected by actions of the System. For example, the provisions of section 4 of the Federal Reserve Act, as amended by the Federal Reserve Reform Act of 1977, provide that both class B and C directors shall be chosen to represent the public and with "due but not exclusive consideration to the interests of agriculture, commerce, industry, services, labor, and consumers." Section 4 further provides that class A directors "shall be chosen by and be representative of the stockholding banks" of the Federal Reserve System. Recognizing that Reserve Bank directors may have, in their private capacities, business, consumer, or other interests to which legitimate attention is to be given; but recognizing also that these same individuals have fiduciary responsibilities as directors of Reserve Banks, this regulation is promulgated for the purpose of assuring preservation of and adherence to the intent of both the Federal Reserve Act and section 208 of Title 18, United States Code.

§ 264a.2 Definitions

For purposes of this part, the following definitions shall apply:

(a) The term "director," unless otherwise indicated, means a head office or branch director of a Federal Reserve Bank.

(b) The term "Board of Governors" means the Board of Governors of the Federal Reserve System.

(c) The term "board" means the board of directors of a Federal Reserve Bank or branch of a Federal Reserve Bank.

(d) The term "related person" means (1) a partner of a director, (2) any organization in which the director is serving as an officer, director, trustee, partner or employee, or (3) any person or organization with whom the director is negotiating or has any arrangement concerning prospective employment.

(e) The term "participate" means to act through decision, approval, disapproval, recommendation, the rendering of advice, investigation, or as is otherwise within the meaning of the provisions of 18 U.S.C. § 208.

(f) The term "particular matter" means a judicial or other proceeding, application, request for a ruling or other determination, contract, claim, controversy, charge, accusation, arrest or other subject within the meaning of the provisions of 18 U.S.C. § 208.

(g) The term "discussions" means the consideration of a matter by a board and may include, depending upon the board's statutory authority, votes taken or other decisional action.

§ 264a.3 Prohibition against director participation in particular matters.

(a) Pursuant to the provisions of 18 U.S.C. § 208(a), no director may participate personally and substantially in a particular matter in which, to the director's knowledge, the director, the director's spouse or minor child, or related persons have a financial interest unless such action is otherwise permitted by 18 U.S.C. § 208(b) and §§ 264a.4 or 264a.5 of this part.

(b) Except as provided by 18 U.S.C. § 208(b) and sections 264a.4 or 264a.5 of this part, no director shall participate in deliberations or decisions of a Reserve Bank board when the question presented is whether the board should approve or ratify an extension of credit, advance, or discount by a Reserve Bank to a bank which is, in the opinion of the President of the Reserve Bank, in a hazardous financial condition, and

(1) Where the director has knowledge that he, his spouse, or minor child has a financial interest in the proposed transaction as a result of:

(i) Being a borrower or applicant for credit from the borrowing bank, other than consumer credit as defined in Regulation Z (12 CFR 226.2(p));

(ii) Maintaining a depository relationship with the borrowing bank in an amount exceeding that covered by Federal deposit insurance;

(iii) Owning stock, stock options, bonds, notes or other forms of indebtedness issued by the borrowing bank, or its registered parent holding company, the market value of which exceeds \$100,000 or represents more than 1 percent of the value of that class of stock, stock option, bond, note, or other form of indebtedness issued by the borrowing bank or its registered parent holding company; or

(iv) Employment in a policy making position or service as a director with the borrowing bank or the registered parent holding company of the borrowing bank.

(2) Where the director has a financial interest in the proposed transaction as a result of:

(i) Service by the director as an officer or director of another bank that is known by the director to be located in the same geographic market for local banking services as the borrowing bank and is known by the director to be in direct and substantial competition with the borrowing bank;

(ii) Service by the director as an officer or director of another bank that is known by the director:

(A) To have outstanding or to be negotiating an extension of credit from, or to, the borrowing bank, other than Federal funds or foreign exchange transactions; or

(B) To maintain a correspondent or depository relationship with the borrowing bank in an amount exceeding

that covered by Federal deposit insurance; or

(iii) Service by the director as one of the principal officers of any business enterprise that constitutes the director's primary business or professional occupation where such business enterprise is known by the director:

(A) To have outstanding or to be negotiating a direct and substantial extension of credit or line of credit from the borrowing bank;

(B) To maintain a principal depository relationship with the borrowing bank in an amount exceeding that covered by Federal deposit insurance; or

(C) To own stock, stock options, bonds, notes or other forms of indebtedness issued by the borrowing bank, the market value of which exceeds \$100,000 or represents more than 1 percent of the value of that class of stock, stock options, bonds, notes or other form of indebtedness issued.

(3) Where the director has knowledge that a partner of the director has a financial interest in the proposed transaction; or

(4) Where the director has a financial interest in the proposed transaction as a result of the director's participation in current negotiations or arrangements concerning prospective employment with the borrowing bank.

(c) It is recognized that a Reserve Bank board can, within the spirit and letter of its responsibilities, delegate to appropriate officials of the Reserve Bank authority to act with respect to extensions of credit to individual banks determined to be in hazardous financial condition, thus avoiding both ratification by the board and applicability to the directors of the prohibitions of this section. Such delegation would not preclude continued advice to the board of appropriate information regarding bank conditions in the district so as to enable the board to perform fully its general oversight responsibilities.

§ 264a.4 Granting of ad hoc exemptions.

(a) The prohibitions of 18 U.S.C. §208 and section 264a.3 of this part shall not apply if the director first advises the Board of Governors of the nature and circumstances of the particular matter before the board and makes full disclosure of the financial interest involved and receives in advance a written determination made by the Board of Governors, or its designee, pursuant to 18 U.S.C. § 208(b)(1), that the interest is not so substantial as to be deemed likely to affect the integrity of the services which the Federal Reserve System may expect from such director.

(b) Telegraphic communications from the President, First Vice President, Secretary or General Counsel of a Reserve Bank to the Board of Governors on behalf of a director and set-

ting forth the precise nature of both the particular matter before the board and the financial interest involved shall be considered to meet the director's duty of full disclosure set forth in paragraph 264a.4(a). Telegraphic response to the same identified officials of the Reserve Bank by the Board of Governors, or its designee, shall be deemed to meet the requirement of a written determination by the Board of Governors set forth in paragraph 264a.4.

264a.5 Exemption of remote or inconsequential financial interests.

(a) Pursuant to the provisions of 18 U.S.C. § 208(b)(2), certain actions of directors of Federal Reserve Banks may be exempted from the prohibitions of 18 U.S.C. § 208(a) and section 264a.3 of this part, if by general rule or regulation published in the FEDERAL REGISTER, the financial interest involved has been determined to be too remote or too inconsequential to affect the integrity of directors' services. Financial interests will be viewed as too remote or too inconsequential:

(1) In circumstances in which a director's action on a matter will not directly, substantially, and predictably affect the financial interest; or

(2) In circumstances in which a director's independence of judgment will not be affected by the financial interest.

(b) The Board of Governors has determined that the financial interests of a director, the director's spouse or minor child, or related persons in the following matters are too remote or too inconsequential to affect the integrity of directors' services and, accordingly, the prohibitions of 18 U.S.C. § 208(a) and section 264a.3 of this part shall not apply to a director's participation in such matters:

(1) Deliberations concerning or ratification of extensions of credit, advances, or discounts to any bank that has not been determined to be in hazardous financial condition by the President of the Reserve Bank, provided such credit extensions, advances, or discounts are made under appropriate provisions of the Federal Reserve Act, regulations and policies of the Board of Governors and the Federal Reserve Banks, and the established operating procedures at the director's Reserve Bank;

(2) Deliberations concerning or affecting any financial institution, to the extent the financial interest in such matters results from:

(i) Maintenance at the financial institution of a checking or other depository account covered by Federal Insurance;

(ii) A fiduciary relationship involving the utilization of the financial institution's trust or investment advisory services;

(iii) The receipt from the financial institution of consumer credit, as that term is defined in Regulation Z (12 CFR 226.2(p)); or

(iv) Participation in Federal funds or foreign exchange transactions with the financial institution;

(3) Deliberations concerning or affecting any financial institution or other enterprise to the extent the financial interest results from ownership of stock, stock options, bonds, notes, or other forms of indebtedness, the market value of which is less than \$100,000 and represents less than 1 percent of the value of that class of stock, stock option, bond, note or other form of indebtedness issued by the financial institution or other enterprise.

(4) Deliberations concerning or affecting any financial institution or other enterprise to the extent the financial interest results from holdings in a diversified and widely held mutual fund, investment company, pension or retirement plan that, in turn, may have invested in the financial institution, provided that the director does not contribute to investment decisions of the fund, company, or plan.

(c) Section 264a.3(b) of this part specifically identifies certain financial interests, the existence and knowledge of which will preclude a director from participating in deliberations or decisions of a Reserve Bank board (except through recourse to the procedures set forth in § 264a.4) when the question presented is whether the board should approve or ratify an extension of credit, advance, or discount by a Reserve Bank to a bank which is, in the opinion of the President of the Reserve Bank, in hazardous financial condition. Financial interests identified in § 264a.3(b) are viewed by the Board as offering a clear potential for conflict. The Board has determined that any other financial interest that a director, the director's spouse or minor child, or related persons may have in such extensions of credit, advances, or discounts to banks in hazardous condition are too remote or too inconsequential to affect the integrity of directors' services and, accordingly, the prohibitions of 18 U.S.C. § 208(a) and § 264a.3 of this part shall not apply to a director's participation in such matters. These would include, for example, financial interests that might result from:

(1) A Director's ownership of stock of a bank or business, other than a registered parent holding company of the borrowing bank, that may have an interest in the condition of the borrowing bank; or

(2) A director's service as a director or trustee of a business or other organization, other than a bank or the registered parent holding company of the borrowing bank, that may, itself or

through a subsidiary, have an interest in the condition of the borrowing bank.

(d) The functions of directors often include their participation in discussions concerning (1) international, national, and regional economic and financial conditions, (2) monetary policy, (3) general conditions, trends or issues with respect to bank credit, (4) establishment of rates to be charged for all advances and discounts by Federal Reserve Banks, subject to review and determination of the Board of Governors pursuant to the Federal Reserve Act, (5) matters intended to have generally uniform application to banks within the Reserve Bank district, and (6) statutes and proposed or pending legislation in which the Federal Reserve System has a legitimate

interest. The foregoing matters are not particular matters of the type described in 18 U.S.C. § 208 and, therefore, that statute is not applicable to participation in such matters. However, even if the statute were held to be applicable to participation in such matters, the Board of Governors has determined that the financial interests of a director, the director's spouse or minor child, or related persons in such matters are too remote or too inconsequential to affect the integrity of directors' services and, accordingly, the prohibitions of 18 U.S.C. § 208(a) and § 264a.3 of this part shall not apply to a director's participation in such matters.

(e) Nothing in this section shall preclude a director from refraining, to the

extent consistent with responsibilities imposed upon the directors by the Federal Reserve Act, from participation in a particular matter. The Board hereby gives notice of its intention to undertake a continuing review of the experience of Reserve Bank boards under this regulation with a view to assuring preservation of and adherence to the intent of both the Federal Reserve Act and 18 U.S.C. § 208, as amended. In the course of such review, particular attention will be given to the provisions of this section.

Board of Governors of the Federal Reserve System, May 31, 1978.

THEODORE E. ALLISON,
Secretary of the Board.

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