

FEDERAL RESERVE BANK  
OF NEW YORK

[Circular No. 7873]  
May 14, 1976

GAO STUDY OF FEDERAL RESERVE SUPERVISORY RESPONSIBILITIES

To the Chief Executive Officer  
of the State Member Bank Addressed, and Others Concerned:

The Board of Governors of the Federal Reserve System has announced an agreement with the General Accounting Office on guidelines for conducting a study of the Federal Reserve's discharge of its bank supervisory responsibilities. Following is the text of a statement issued by the Board of Governors on May 6 in connection with this study:

The Board of Governors of the Federal Reserve System today announced agreement with the General Accounting Office on guidelines for a study by the GAO of the Federal Reserve's discharge of its bank supervisory responsibilities.

The attached Memorandum of Agreement defines the scope of the study as including those functions of the Federal Reserve System relating to the examination of State member banks, the detection in those banks of existing or potential unsafe or unsound conditions, or violations of law or regulations, and the process by which the Federal Reserve seeks to remedy such conditions or violations and to protect the solvency and soundness of State member banks.

The study by the GAO will also include the supervisory practices of the Federal Deposit Insurance Corporation with respect to non-member State banks and the Comptroller of the Currency with respect to national banks. It is being undertaken in response to a request last January by the Chairman of the Subcommittee on Domestic Monetary Policy of the House Committee on Banking, Currency and Housing.

The study will cover the Federal bank regulators' supervisory practices during the past five years, principally through the selection of banks, chosen by statistical sampling procedures, for detailed study. The agreement between the Board and the GAO includes the following provisions:

—The study will include bank examination practices with respect to the commercial, foreign operation, electronic data processing and trust functions of State members.

—The GAO will keep absolutely confidential the identity of all bank customers, bank officials and directors, or of banks selected for study.

In a letter to the Comptroller General regarding the study Chairman Arthur F. Burns noted that it is his understanding that the guidelines for maintaining confidentiality of private information will apply also to GAO's communications with the Congress. He said that the "Board is gratified that both the GAO and the Committee share our concern for maintaining the confidentiality and integrity of the examination process."

Enclosed for State member banks are copies of correspondence between Arthur F. Burns, Chairman of the Board of Governors, and Elmer B. Staats, Comptroller General of the United States, relating to the study, and a copy of the *Memorandum of Agreement Between the Board of Governors of the Federal Reserve System and the Comptroller General of the United States*, dated May 4, 1976. As indicated in the *Memorandum of Agreement*, strict confidentiality of System records will be maintained by the General Accounting Office and by all GAO personnel participating in the study. The identity of banks, bank officials, directors or stockholders, and bank customers will be safeguarded both by the General Accounting Office and by the Federal Reserve System throughout the conduct of the study and afterwards.

PAUL A. VOLCKER,  
*President.*





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

May 5, 1976

The Honorable Elmer B. Staats  
Comptroller General of the United States  
Washington, D. C. 20548

Dear Mr. Staats:

I am enclosing an executed copy of a Memorandum of Agreement between the Board of Governors and the Comptroller General relating to the study of the Board's performance of its bank supervisory responsibilities requested by the House Committee on Banking, Currency and Housing. This form of the Agreement has been approved by the Board of Governors.

I should point out that the Board has discussed the Agreement at great length. All of the Board members were profoundly concerned about violating our long tradition of maintaining rigid confidentiality of bank examination reports. Moreover, some members felt so strongly about breaching this tradition -- particularly with respect to those portions of the report dealing with names of bank customers -- that they could not accept even the carefully circumscribed disclosure to GAO provided for in the Agreement.

Two factors weighed heavily in the Board's decision to approve the Agreement: First, we believe that the provisions of the Agreement that prevent removal of documents and work papers from the Board's premises, and that categorically prohibit disclosure outside of GAO of the identity of the banks being studied or their officials or customers, offer reasonable assurance that confidentiality will be maintained. I cannot emphasize too strongly the need for strict adherence to these provisions of the Agreement.

Second, we understand that you will have an understanding with the House Committee on Banking, Currency and



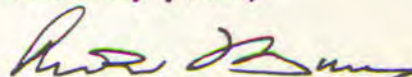
Housing that the Committee will not require GAO to breach its obligations of confidentiality under this Agreement or otherwise make available to the Committee or its staff information concerning the identities of banks or individuals covered by the GAO study. The Board is gratified that both GAO and the Committee share our concern for maintaining the confidentiality and integrity of the bank examination process.

You have asked for an expression of our willingness to discuss providing access to additional records of the Federal Reserve System if, during the study, you determine that such access is necessary. While the access provisions of the Agreement are already quite broad we will, of course, give serious consideration to any request you may make for access to additional records that are within the scope of the study and as to which a showing of need is made. In the same spirit, we would hope that if it appears that the access to examination reports we have granted is greater than is necessary for your purposes -- for example, with respect to the identities of bank customers -- you might consider agreeing to limitations, such as the masking of names, that would alleviate the concerns of Board members about disclosing information of a private nature.

In considering the request from the House Banking Committee that the Board voluntarily consent to such a study by GAO, the Board was concerned about the possibility that such consent on its part might be viewed by some as being inconsistent with the Board's position on legislative proposals to subject the Federal Reserve to periodic audit by GAO. However, we do not consider this study to be an "audit" in any sense of that term, nor do we understand it to be an inquiry that will be repeated on a regular periodic basis. I have stated on several occasions that the Board would welcome a meaningful inquiry by the Congress into our performance of our bank supervisory responsibilities, and I believe that the guidelines we have agreed to reasonably delineate the scope of an inquiry that will serve this purpose.

We appreciate your cooperative attitude and that of your staff in developing these guidelines, and we shall follow the progress of the study with interest.

Sincerely yours,



Arthur F. Burns





COMPTROLLER GENERAL OF THE UNITED STATES  
WASHINGTON, D.C. 20548

B-118535

May 4, 1976

The Honorable Arthur Burns  
Chairman, Board of Governors  
Federal Reserve System  
Washington, D.C.

Dear Mr. Burns:

On January 24, 1976, the Chairman, Subcommittee on Domestic Monetary Policy of the Committee on Banking, Currency and Housing, U.S. House of Representatives, requested that we undertake a comprehensive study of the bank regulatory functions of the Federal Reserve System. My representatives met on several occasions with senior Federal Reserve System officials to prepare a Memorandum of Agreement providing for our access to pertinent Federal Reserve System records and for necessary arrangements to protect the confidentiality of information obtained during the study.

These meetings culminated in a draft Memorandum of Agreement between our respective Offices dated April 28, 1976. I understand that this draft was presented to the Board of Governors for its review on Wednesday, April 28, 1976, and was approved subject to our acceptance of certain changes in the text.

The Board reviewed the draft in the context of the Subcommittee's January 24, 1976 letter to the Board. The Subcommittee asked the Board to cooperate with us in a study of the bank supervisory functions of the Federal Reserve System.

In meeting with your representatives to discuss the changes proposed by the Board, it became evident that the Board viewed its bank regulatory and supervisory functions as quite distinct and different. In discussions with the other bank supervisory agencies, they had not made such a distinction, and our draft had reflected this broader definition of supervisory and regulatory functions.

We understand that the Board does not feel that a study of bank supervision should encompass a general evaluation of how the Board has carried out its regulatory functions.



Because we are still in the earliest phase of this unique study, we are uncertain what effect the Board's distinction between its regulatory and supervisory functions may have on the conduct of the study. We think it is possible that our study of bank supervision may touch on certain regulatory aspects; however, I want to assure you that we do not envision any need to inquire into the Board's responsibilities for monetary policy or for central banking activities.

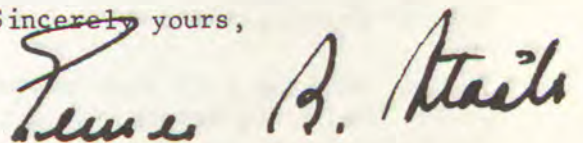
The enclosed draft, dated May 4, 1976, now reflects what we understand are the Board's views as to the appropriate scope of the study and the records to which we will be afforded access. Although the distinction made between supervisory and regulatory functions may affect the scope of our study and the extent to which Federal Reserve System records will be available to us, I believe our differences are relatively minor in relation to the major agreement we have reached in principle.

In order not to postpone the study, I am willing to enter into the enclosed Agreement if the Board finds its terms acceptable.

I think that the Agreement will prove to be adequate for our purposes. Since we are just beginning the study, we cannot be sure that the access to records afforded us under the proposed Agreement will provide us with all the information we might need. I would appreciate your expression of willingness to discuss the matter further with us if, during the course of the study, we determine that access to additional Federal Reserve System records is needed to complete the study of the bank supervisory functions of the Federal Reserve System as we have now defined them.

I want you to know that I greatly appreciate the cooperation given us by the Board and by the Federal Reserve System staff in striving to reach agreement in this matter of vital importance to your agency and the Congress.

Sincerely yours,



Comptroller General  
of the United States



May 4, 1976

MEMORANDUM OF AGREEMENT  
BETWEEN  
BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM  
AND  
THE COMPTROLLER GENERAL OF THE U. S.

I. PURPOSE

On January 24, 1976, the Chairman, Subcommittee on Domestic Monetary Policy of the Committee on Banking, Currency and Housing, United States House of Representatives, requested the Comptroller General of the United States, through the General Accounting Office (GAO), to study and evaluate the supervisory responsibilities relating to banks under the jurisdiction of the Federal Reserve System. This request was reiterated by letter of February 5, 1976, from the Committee to the Chairman, Board of Governors of the Federal Reserve System.

The Board of Governors has consented to such a study, evaluation, and report so that GAO may assess the effectiveness of the Board in discharging its bank supervisory responsibilities. For the purpose of this Agreement, the term "bank supervisory responsibilities" shall mean those functions of the FRS involving the examination of State member banks and the detection of unsafe or unsound, or potentially unsafe or unsound conditions in such banks, or violations of law or regulation by such banks, and the process by which the FRS seeks to remedy such conditions or violations and otherwise protect the solvency and soundness of State member banks.



## II. OPERATIVE PROVISIONS

The Comptroller General, on behalf of the General Accounting Office, and the Board of Governors, on behalf of the Federal Reserve System (FRS), therefore agree to the following:

### (1) Scope of Study and Evaluation

(a) GAO will study the effectiveness of the Board of Governors in discharging its bank supervision responsibilities during the past five years. This study will include the procedures used by FRS bank examiners in their periodic on-site examinations of State member banks, the manner in which the findings and conclusions of bank examiners are reported, the manner in which financial data is collected from State member banks by the FRS for bank supervisory purposes, the systems employed by the FRS to identify and attempt to achieve correction of problems occurring at particular State member banks, the recruiting and training of bank examiners, the methods by which the FRS reviews its own bank supervisory performance and plans for its future needs in that area, and other subjects directly and clearly related to the bank supervisory process.

The GAO study will be conducted principally through the selection of one or more statistical samples of State member banks for detailed study. To the extent necessary to evaluate the manner in which the FRS has dealt with unsafe or unsound conditions, or potentially unsafe or unsound conditions, or violations of law or regulations,



detected in the bank supervisory process with respect to any bank selected for study in any such sample, GAO may inquire into the manner in which the FRS has dealt with applications from a parent bank holding company of such bank, or applications from the bank for the establishment of branches or for membership in the Federal Reserve System.

(b) The GAO study will include the following types of bank examination performed by FRS: commercial, foreign operations, electronic data processing and trust.

(c) Except insofar as regulatory actions of the FRS are directly related to banks selected for study in a sample, as provided in subsection (a) above, the GAO study shall not include an evaluation of the performance by FRS of its regulatory functions generally, such as its policies and procedures for implementing the Bank Holding Company Act, the Bank Merger Act, consumer protection statutes, the securities laws, or laws or regulations relating to bank reserves, payment of interest on deposits, or securities credit. In no event shall the study be deemed to include in any respect the monetary policy functions of the FRS or the operations of the FRS relating to the payments mechanism, such as check clearing or electronic funds transfer, or to the handling of currency or securities.

(2) Access to Records

FRS will afford authorized GAO personnel access to, and permission to examine, all FRS records, books, and documents and other material relating to the bank supervisory functions of FRS.



FRS examination reports of State member banks will be included in such documents to the extent such banks are selected for study in the sample(s) referred to in paragraph (5) (b), together with work papers and correspondence files related to such reports, whether or not a part of the report, and all without any deletions.

The GAO study will be conducted in such a manner as to cause a minimum of disruption in the normal operations of the Board of Governors and the Federal Reserve Banks. Recognizing that FRS may in certain cases require priority use of its records, mutually agreeable arrangements will be made with respect to availability of those records in current, active use. Similar arrangements will be made regarding the availability of agency officials for interviews.

Authorized GAO personnel will be permitted to make whatever notes or whatever copies they deem necessary during the study, all to be contained in the GAO workpapers. These workpapers will be safeguarded in accordance with paragraph (6) of this Agreement.

(3) Authorized GAO Personnel

(a) The Comptroller General will have sole authority for assigning the GAO personnel to be engaged in the study.

(b) GAO will provide FRS with a list of its personnel authorized to have access to FRS records in connection with this study and evaluation at the time this agreement is executed, with the list updated as changes occur. Assigned GAO personnel will obtain necessary credentials for entering FRS



facilities and will carry official GAO credentials that will be presented to FRS personnel on request.

(c) To the extent possible, GAO will use personnel with experience in reviewing reports of depository institutions.

(4) FRS Liaison Official; Facilities

(a) FRS will designate a liaison official to facilitate the GAO access to FRS records and personnel for the purpose of this study. GAO will clear all requests for documents and interviews through the liaison official.

(b) FRS will provide GAO with suitable, lockable office space and furniture, telephone and access to copying facilities. These working facilities will be adequate for up to ten GAO representatives, the exact number to be determined later.

(5) Procedures

(a) This study and evaluation will be conducted in accordance with procedures and standards prescribed by the Comptroller General, subject to the terms of this Agreement.

(b) The selection of examination reports for GAO study will be made on a statistical sampling basis determined by the GAO to be adequate for the purposes of the study, after consultation with the Board of Governors. Depending on the purpose of the study, it may be necessary to select more than one sample.

(c) In making its study, the GAO will interview FRS personnel, including bank examiners and Federal Reserve Bank Officers and staff, in order to obtain an adequate understanding



of all phases of FRS' bank supervisory responsibilities. GAO will not evaluate the accuracy of the examiner's factual findings or make separate examinations of the banks involved.

(d) The GAO will prepare a report to the Congress with its conclusions as to the matters specified in paragraph (1). An advance draft of the GAO report will be made available to the Board of Governors, who will be afforded an adequate opportunity to comment on the contents of the proposed report. The final report will include as an addendum any written comments submitted by the Board of Governors.

(5) Safeguarding the Identity  
of Banks and Customers

In making its study, strict confidentiality shall be maintained by GAO and all GAO personnel participating in the study. GAO will safeguard the identity of banks, bank officials and bank customers as follows:

(a) All GAO workpapers, and whatever FRS documents or records come into GAO possession during the study will remain on the premises of FRS. Such material will be maintained in such a way as to prevent unauthorized access. When not in use, such material will be kept in secure, locked file cabinets.

(b) GAO, in its report and otherwise outside of GAO, will not (i) identify bank customers; (ii) identify any bank or bank officers, directors or stockholders; or (iii) provide detail that can lead to identification of any bank, bank customer, bank officer, director or stockholder.



Within these limitations, GAO, in its report and otherwise outside of GAO, may discuss the condition or operations of a particular bank.

GAO shall make no disclosure whatsoever outside of GAO or the Federal Reserve of the identity of any bank selected as a sample bank for purposes of the study, whether to the bank being studied or otherwise.

(c) The limitations of this paragraph shall not prohibit GAO or its employees from discussing particular banks, bank officials or bank customers: (i) with officials of the Office of the Comptroller of the Currency or of the Federal Deposit Insurance Corporation if those agencies were involved in transactions or supervisory procedures related to such bank or bank customers; or (ii) with officials of FRS.

(d) The non-disclosure provision of this paragraph shall apply with respect to any affiliate of a bank covered by the study.

(e) Upon completion of the study and issuance of the report, all GAO files and workpapers will be retained for a period of ten years. They will be kept on the premises of the Board of Governors for one year from the date of issuance of the report, provided, however, that authorized GAO personnel shall have the continued right of access to such material during that time period. After one year from



the date of issuance of the GAO Report, FRS may send the files and workpapers to the Federal Records Center storage for an additional nine years, provided, however, that FRS will recall such files and workpapers from storage at GAO request so that GAO personnel may have access to them on the premises of FRS. On or after ten years from the date of issuance of the GAO report, FRS may direct destruction of the files and workpapers unless notified to the contrary by GAO.

RECEIVED  
GENERAL INVESTIGATIVE DIVISION  
MAY 13 1976  
FEDERAL RESERVE BANK  
NEW YORK  
GAO FILES

(7) Field Activities

To the extent the conduct of the study will be outside of the Washington, D.C. area, mutually agreeable procedures, consonant with the Agreement, will be developed concerning access to and security of records.

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Chairman, Board of Governors  
Federal Reserve System

\_\_\_\_\_  
Comptroller General  
of the United States

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Date

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Date